PART 1
AUSTRALIAN COMMERCIAL LAW
CONTRACT LAW
AND COMMERCIAL
REGULATORS
1.0 Introduction

This chapter addresses the fundamental rules of contract law and introduces nine of the significant regulators operating within the Australian commercial landscape. Contracts are of enormous importance in most established economies as they provide a means by which promises made as part of a commercial bargain can be legally enforced. Contracts also underlie a large number of transactions entered into by the principal commercial regulators in this country, and so this chapter provides a useful backdrop against which we can explore more specific concepts in Australian commercial law.

1.1 Contracts in commerce

The law of contract is fundamental to the notion of voluntary exchange, which forms the basis of any market for goods and services in such countries as Australia. The legal enforcement, in a certain and predictable manner, of agreements to exchange resources fosters confidence among market participants and increases economic growth and overall commercial prosperity. As such, contract law quite literally ‘underpins our economy’.¹ While specific courses within law curricula will educate you as to the more specific and complex principles pertaining to contract law, it is essential in any examination of Australian commercial law to have at least a general understanding of the basics so as to appreciate the role and importance of contracts in commerce.

There is no general agreement among scholars as to what a ‘contract’ actually is. This difficulty in part stems from the fact that the term refers not only to the bargain manifested between the parties, but often also to the physical form of that agreement. That is, ‘contract’ describes not just the substance of the agreement but, where a written agreement is used, the document itself. Most people in business assume a ‘contract’ to be simply a written agreement. However, a contract does not need to be written down, and so it is probably more accurate to define a contract as an agreement or set of promises made between parties that the law will enforce.² In whatever form, for an agreement to be a ‘contract’ it need only satisfy four key requirements, which will be discussed later in the chapter.

Importantly, gifts and social agreements are not ‘contracts’ and so are not legally enforceable. These do not carry the force of law because they either lack consideration (in the case of gifts, as we will discuss in detail shortly) or were objectively not intended to attract legal consequences if breached. If the law regarded all such agreements as contracts, then legal liability would be unintentionally assumed in a countless number of situations and the courts would be inundated with (largely trivial) lawsuits. As such, the law of contract is careful to identify whether an agreement bears all the hallmarks of a legal contract or whether it is simply an unenforceable arrangement.

¹ Biotechnology Australia Pty Ltd v Pace (1988) 15 NSWLR 130, 132.
1.1.1 Common types of contract

Contracts can be classified in a number of ways and so there can be said to be numerous ‘types’. One basic classification relates to the form of the agreement. There are two basic forms: *formal* and *simple*. A formal contract, otherwise known as a *contract under seal*, is one recorded in a deed. A deed is a special written document that transfers or affirms the transfer of property or some other interest.\(^3\) The common law rules concerning deeds have been largely modified by statute. A simple contract, on the other hand, can be made orally and/or in writing and requires consideration (which we will hear about shortly). Formal contracts do not require consideration, and so an agreement lacking consideration can be incorporated into a deed to avoid any potential issues with enforceability.

Another classification of contracts is by nature of the obligations they impose upon the parties. Contracts can be either *bilateral* or *unilateral*. A bilateral contract is one in which both parties exchange promises to do or not to do something; the legal obligation on each party to fulfil their respective promises arises at the point of exchange. For example, Frank offers to mow Bill’s lawns for $20 on a specific date, and Bill accepts this offer. Both parties are now obligated to perform: Frank to mow Bill’s lawns on the agreed date, and Bill to pay Frank $20 for this service. A unilateral contract is one in which one party has made a promise to do or not to do something upon the performance of a *specified act*. The legal obligation to perform arises at the point a second party performs the act specified by the first party. For example, Melissa posts an advertisement offering $200 to anyone who finds and returns her missing dog. There is no legal obligation on anyone who sees the advertisement to go and find the dog, and so there is no contract at this point. If, however, another person finds Melissa’s dog and returns it to her, then that person is entitled to the $200 offered by Melissa. The finder has performed the specified act (found and returned the dog) and so the legal obligation on Melissa to perform (pay the reward) arises at this point; there is now a contract. A useful way to summarise is that with bilateral contracts *both* parties exchange promises, whereas with unilateral contracts only *one* party makes a promise (offer).

A third classification of contracts concerns the manner of their creation. Contracts can be created *expressly* or by *implication*. When most people hear the word ‘contract’, they normally envisage a written document.\(^4\) However, contracts can arise in situations where no documentation is involved at all, or where a combination of spoken and written words (in whatever form) is used to construct the agreement. An express contract is one in which the parties have explicitly stated the terms of their agreement, either orally or in writing. This is overwhelmingly the more common type of contract, as most people tend to employ effort and comprehensively outline terms when forging contractual arrangements with others. Alternatively, an implied contract is one which is inferred from the conduct of the parties within the context of the surrounding circumstances. By way of example, when boarding a bus you are implicitly agreeing to abide by the terms of carriage, even though you have not signed anything or even said a word.\(^5\)

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5. This is assuming that the terms of carriage have been appropriately brought to the attention of the passenger. The concept of notice is discussed briefly later in the chapter when terms and performance are addressed.
1.1.2 General principles and ‘fragmentation’ of contract law

The Australian legal framework, and therefore a large number of its legal rules and principles, derive from England and can be traced back centuries. Throughout the 19th century, scholars endeavoured to make sense of the complicated and disordered body of contract principles that abounded and thankfully were successful in discerning what is now generally agreed to be the basic set of rules underlying the formation, performance and termination of contracts.

Of course, over time, as industries have matured and specific requirements surrounding contractual agreements have developed for each, the principles of contract have been refashioned by parliament and the courts to suit. McKendrick has referred to this process of gradual specialisation as ‘fragmentation’.6 While the basic principles may in particular instances have undergone customisation – such as in the case of insurance and real estate contracts, which have their own sets of legislative rules – they retain significance to all contracts and underlie the more particular rules that have developed for particular contexts. We will now briefly examine the key principles relevant to all stages of a contract’s life from birth (formation) through to death (termination).

1.1.3 Formation

For a contract to exist, four essential elements must be present: (1) offer and acceptance (agreement); (2) consideration; (3) intention to create legal relations; and (4) certainty and completeness of terms. There are also two peripheral requirements in capacity and legality.7 We will consider each of these elements in turn.

1.1.3.1 Element 1: Offer and acceptance (agreement)

An offer is an indication by one party of a willingness to be bound to the terms of a promise they make to another party, with the latter having the option of accepting or rejecting the proposal.8 The offer can be made orally, in writing, by conduct, or through a combination of these means. An offer must be distinguished from other forms of communication such as the supply of information or an invitation to treat. A supply of information is not an offer. For example, merely stating the lowest price you would sell property for when asked is not offering the property at that price; it is responding to the request for information.9 Similarly, invitations to treat are not offers. An invitation to treat is an invitation to enter into negotiations. Typical instances of invitations to treat that you will encounter in the commercial world include the display of goods in a shop, advertised goods in catalogues/newspapers, auctions and tenders. In each case, parties are invited to make offers by way of proffering the price stipulated or making bids through the auction or tender processes. A common error made by laypeople is to mistake all of these scenarios as offers that they are accepting, rather than as

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7 These concepts are not considered in this chapter, save to say that a party must have legal capacity to contract (e.g. be of sound mind, and an appropriate age in most circumstances) and cannot enter into contracts that involve or facilitate illegal conduct.
8 *Brambles Holdings Ltd v Baturst City Council* (2001) 53 NSWLR 153, 171.
9 *Harvey v Facey* [1893] AC 552.
invitations in response to which they are making offers. In other words, they think they are the ones who have to accept, rather than make, the offer.

An offer can be revoked at any point prior to its being accepted, so long as the revocation is communicated to potential offerees. The revocation can be verbal, in writing, or occur via conduct. It will be more difficult to revoke an offer in the case of unilateral contracts. Recall that a unilateral contract arises when A performs the act specified by B. To use our earlier example, could Melissa revoke her offer to pay $200 to whoever finds and returns her missing dog if someone had already found the dog and was in the process of returning it (e.g. driving to her house)? The courts typically decide whether revocation is possible in such circumstances by considering a number of factors such as the relative benefit or detriment suffered by the offeree in performance, the offeror's appreciation of the risk assumed, and the intentions of the parties.

Once an offer is rejected, whether expressly or by conduct indicating that the offer has been turned down, it is terminated and cannot be accepted. Again, it is a common misconception that a vendor can simply go back to an offeror (potential purchaser) and say they have 'changed their mind' and will accept the price offered; the offer has died and cannot be revived. Rather, the offeror must make another offer to start the process again. There also seems to be a general misunderstanding in commerce as to the effect of a counteroffer. A counteroffer terminates the offer on foot and supplants it; the other party can then choose to accept or reject the counteroffer.

In other words, the roles reverse when a counteroffer is made. If Rachael advertises her car for $5000 (invitation to treat) and Mason contacts her and offers $4500, Mason is making an offer. If Rachael responds with 'How about $4800?', she has proposed a counteroffer – this terminates Mason's original offer of $4500 and converts Rachael to offeror. Rachael is now making an offer to Mason, which Mason can either accept or reject.

It is also critically important to note that a mere request for information or further particulars does not amount to a rejection of an offer.

To use the example above, if Rachael made a counteroffer of $4800 for her car, and Mason said "Would you be willing to come down a bit more on price?" or 'Does that include the alloy rims on the tyres?', Mason has not rejected the offer. Instead, he simply seeks further information upon which to make his decision whether to accept Rachael's counteroffer or not.

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10 Byrne & Co v Leon Van Tienhoven & Co (1881) LR CPD 344. Dickinson v Dodds (1876) 2 Ch D 463.
12 Hyde v Wrench (1840) 3 Beav 354.
13 Stevenson Jacques & Co v McLean (1880) 5 QBD 346.
It is essential to examine the precise words used when determining if a party is requesting further information or actually making a counteroffer that rejects the original offer. The courts consider the parties' language to try and elucidate the meaning and effect of their dialogue.

A final observation relevant to the cessation of offers is that an offer will lapse if it is not accepted within a reasonable time, as determined in the circumstances of the particular case.\(^\text{14}\)

Acceptance is the reciprocal stage of agreement and signals the 'meeting of the minds' (consensus ad idem) between the parties. To effect a valid acceptance, the offeree must be aware of the offer presented to them. This may sound odd, though it is possible for a contract to be formed inadvertently and so it must be determined if the offeree was aware of what they were agreeing to. In \(R\ v\ Clarke,\)
\(^\text{15}\) for example, the Western Australian Police offered a £1000 reward to anyone who provided information leading to the arrest and conviction of the person(s) who murdered two police officers. The plaintiff provided this information not knowing, however, that there was a reward at stake. As he was implicated in the murders himself, he offered this information to clear his name and not to claim the reward. The High Court held that the plaintiff was not entitled to the reward, as a unilateral contract can only be formed where the act required for acceptance is performed on the faith of the offer.

Acceptance must also be communicated to the offeror.\(^\text{16}\) Where a mode or manner of acceptance is prescribed by the offeror, the offeree's communication must occur in this way.\(^\text{17}\) Generally speaking, acceptance should occur via the same means in which the offer was conveyed; however, in practice, it is rare for commercial offers to stipulate an exclusive method of acceptance. Importantly, silence does not constitute acceptance.\(^\text{18}\) As such, one cannot say, ‘If I don’t hear from you by Friday, I’ll assume you agree.’ This undermines the notion of voluntarily assumed obligation. A rare exception is where, in the absence of an express acceptance, an offeree’s conduct demonstrates that they are accepting the offer. In such cases, this may suffice as valid acceptance.\(^\text{19}\)

For example, if Rachael offered Mason the chance to buy her yacht at a discounted price provided a $1000 deposit was paid by Mason before the end of the day, and Mason, without saying anything at all, simply paid the $1000 into Rachael's bank account, this naturally implies that he has accepted Rachael's offer.

An important exception to the rule that acceptance must be communicated is the postal acceptance rule. Where acceptance is expected to be sent by post, the acceptance becomes effective as soon as it is posted (as opposed to when it is actually received by the offeror).\(^\text{20}\)

The rule emerged in the 19th century at a time when commercial parties either contracted in

\(^{14}\) Ramsgate Victoria Hotel Co v Montefiore (1866) LR 1 Ex 109.
\(^{15}\) (1927) 40 CLR 227.
\(^{16}\) Tinn v Hoffman (1873) 29 LT 271.
\(^{17}\) Gilbert McCaul (Australia) Pty Ltd v Pitt Club Ltd (1954) 76 WN (NSW) 72.
\(^{18}\) Felthouse v Birldley (1862) 11 CB (NS) 869.
\(^{19}\) Empirinall Holdings Pty Ltd v Macbon Paull Partners Pty Ltd (1988) 14 NSWLR 523.
\(^{20}\) Adams v Lindsell (1818) 106 ER 250.
person or via letters mailed to one another when distance proved too much. As such, the rule reflects a concern that parties might revoke an offer prior to physically receiving an acceptance, despite the offeree having done all they can to inform the offeror of their acquiescence. The advent of electronic communication technologies has somewhat complicated matters. It has been judicially stated that instantaneous forms of communication (such as telephone, telex, facsimile etc.) are not subject to the postal acceptance rule. Emails have been recognised as analogous to telex and so acceptance would be deemed to have been communicated when the email was received, rather than when it was sent.

Interestingly, s 14(1) of the Electronic Transactions Act 1999 (Cth) provides that, unless otherwise agreed by the parties, the time of dispatch of an electronic communication (such as an email) is the time it leaves the information system under the control of the sender. If the system is not under the control of the sender, which would typically be the case between commercial parties utilising external servers to transmit their emails, dispatch instead occurs when the addressee receives the electronic communication.

1.1.3.2 Element 2: Consideration

The second element of contract formation is consideration. The doctrine of consideration requires that something be given in return for a promise in order for that promise to be legally binding. As such, it distinguishes gratuitous promises from legally enforceable promises. There are two basic elements to consideration: benefit/detriment and bargain. This can be a difficult concept to comprehend as the term ‘consideration’ encompasses both whatever is exchanged and the process for this exchange. Looking at the first element, Lush J in Currie v Misa defined consideration as ‘some right, interest, profit, or benefit accruing to the one party, or some forbearance, detriment, loss, or responsibility, given, suffered, or undertaken by the other’. Consideration can therefore be anything of sufficient legal value. Not only must consideration be in the nature of one or more of the things listed by Lush J (above), it must also have been given in return for a promise. That is, it must have been bargained for. As Lord Dunedin explained in Dunlop Pneumatic Tyre Co Ltd v Selfridge & Co Ltd: An act or forbearance of one party, or the promise thereof, is the price for which the promise of the other is bought, and the promise thus given for value is enforceable.

There are many rules attending the doctrine of consideration, though we will only briefly summarise these here. First, consideration must be legally sufficient but need not be adequate. The law of contract is not concerned with whether parties have received a ‘fair’ price; if they have willingly accepted that price, then the law will enforce the arrangement. Second, promising to perform (or actually performing) an existing legal duty will not suffice as consideration. In other words, you cannot receive more in return for the same; this is a gratuitous promise, as there is no quid pro quo given that nothing extra is being exchanged.

23 (1875) LR 10 Ex 153, 162. See also Beaton v McDivitt (1987) 15 NSWLR 162, 181.
24 Thomas v Thomas (1842) 2 QB 851.
26 Westlake v Adams (1858) 5 CB (NS) 248, Chappell & Co Ltd v Nestlé Co Ltd [1960] AC 87.
27 Stilk v Myrick (1809) 2 Camp 317, Wigan v Edwards (1973) 1 ALR 497.
So, if Rachael engages Mason to build her house for $400,000, and Mason asks for additional money midway through the job (which Rachael promises to pay), Rachael is not obliged to pay the additional money. Mason has given nothing extra in addition to what he was already obligated to do.

This rule can easily be avoided by, for example, tendering fresh consideration in return for the additional consideration from the other party, or putting the agreement into a deed (which we heard about earlier).

Controversially, in *Williams v Roffey Brothers & Nicholls (Contractors) Ltd*,[28] it was held that where one party promises additional consideration to the other party in return for what they were already due to receive, consideration may be found in the ‘practical benefit’ the promisor derives from the modification. In that case, Mr Williams was hired by Roffey Bros to complete some carpentry work under a subcontract. He started to run out of money and was not sure he could continue, so Roffey Bros promised an additional £10,300 – to be paid in instalments – to finish the work. When instalments that had fallen due were not paid, Williams sued to recover them. The English Court of Appeal held that, while Williams had merely promised to perform an existing legal duty in return for the additional money (violating the existing legal duty rule), he had provided practical consideration to Roffey Bros. They did not, for example, have to employ other subcontractors, the haphazard payment scheme was replaced with a new streamlined scheme, and the penalty clause under the head contract was avoided. The practical benefit principle has been accepted, though slightly modified, in Australia.[29]

An intriguing extension of the existing legal duty rule is the part-payment of debt rule, which basically states that a debtor’s promise to pay part of a debt is not good consideration for the creditor’s reciprocal promise to discharge the debt.[30] The rationale underlying the rule is that the offer of a lesser sum can never satisfy the greater sum due, such that the creditor is giving more than they are receiving. There are numerous exceptions to the rule, such as where the debtor repays in something other than money[31] or where a third party promises to make the part-payment.[32]

A third and final rule concerning consideration relates to when it is given. Consideration will not be found in something done or given prior to the making of a promise. This is because bargain theory requires that consideration be reciprocal.[33] One exception to this rule is where a party is requested to perform a service, performs that service, and the requesting party subsequently promises to pay for the service. In such cases, there is an implied understanding that the payment is in satisfaction of the service performed.[34]

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29 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723.
30 *Pinnel’s case* (1601) 5 Co Rep 117a; *Poakes v Beer* (1884) 9 App Cas 605.
31 *Pinnel’s case* (1601) 5 Co Rep 117a.
32 *Hirachand Panamchand v Temple* [1911] 2 KB 330.
33 *Roscorla v Thomas* (1842) 3 QB 254.
34 *Lampleigh v Brathwait* (1615) Hob 105; *Ipex Software Services Pty Ltd v Hosking* [2000] VSCA 239.