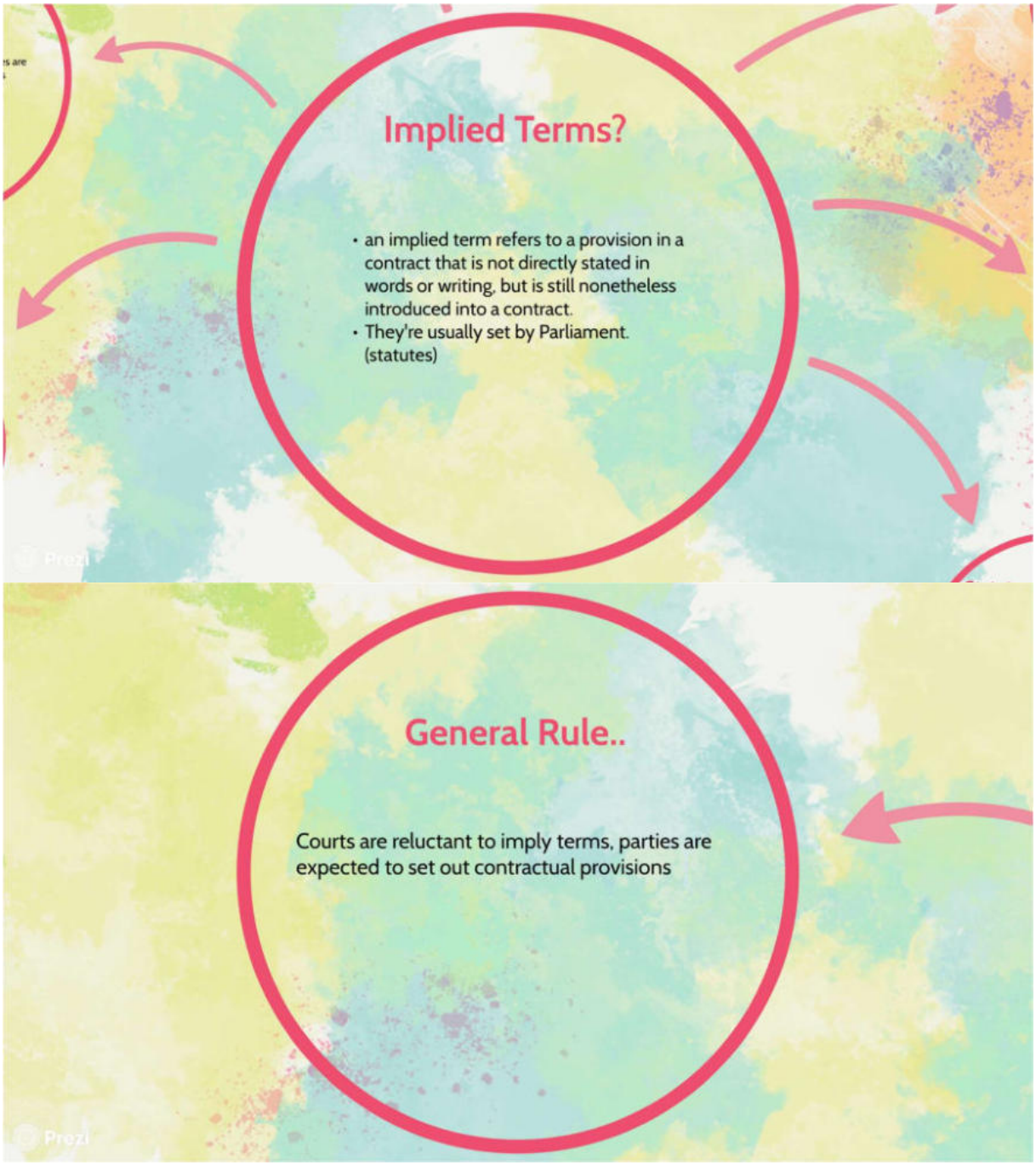
Week 9: The Contents of the Contracts Implied Terms



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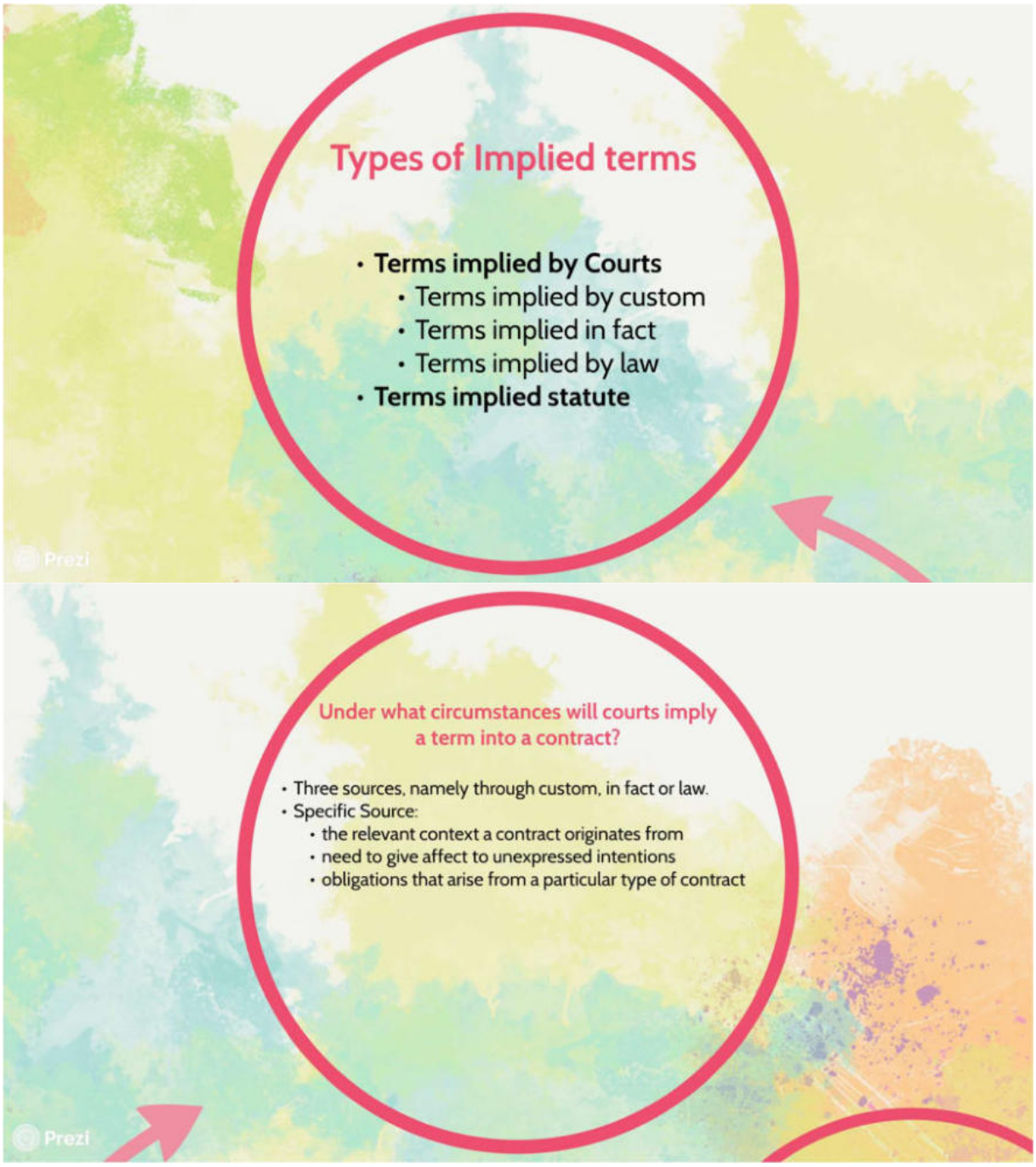

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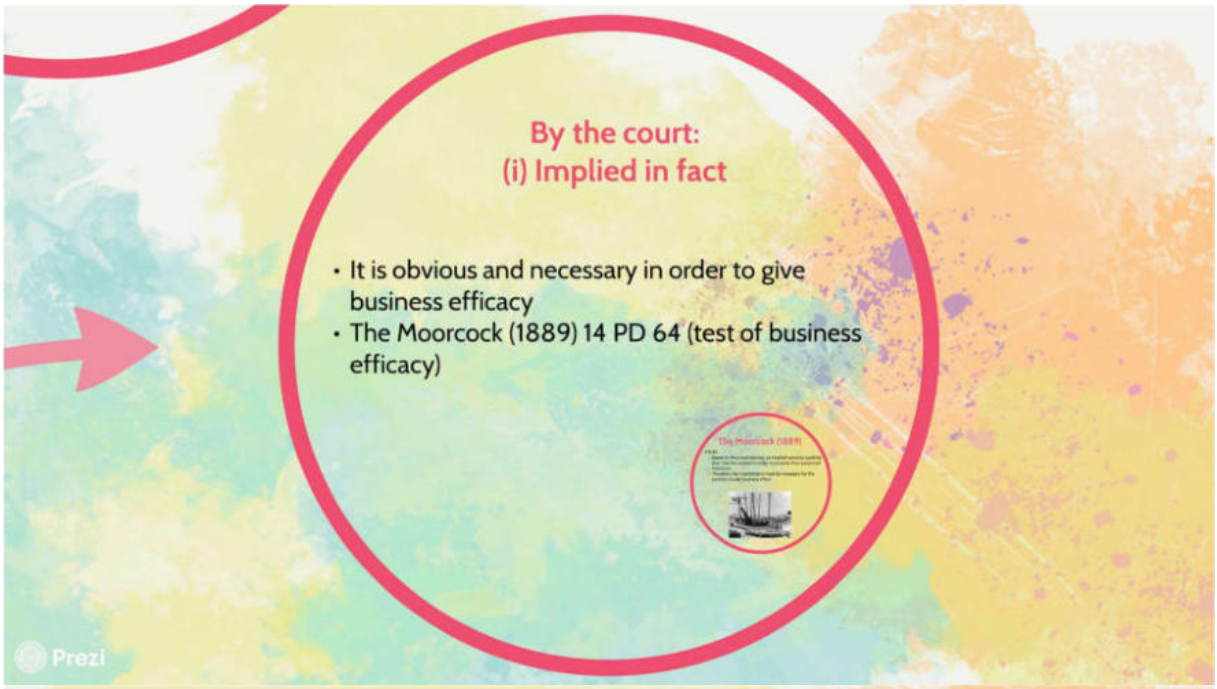

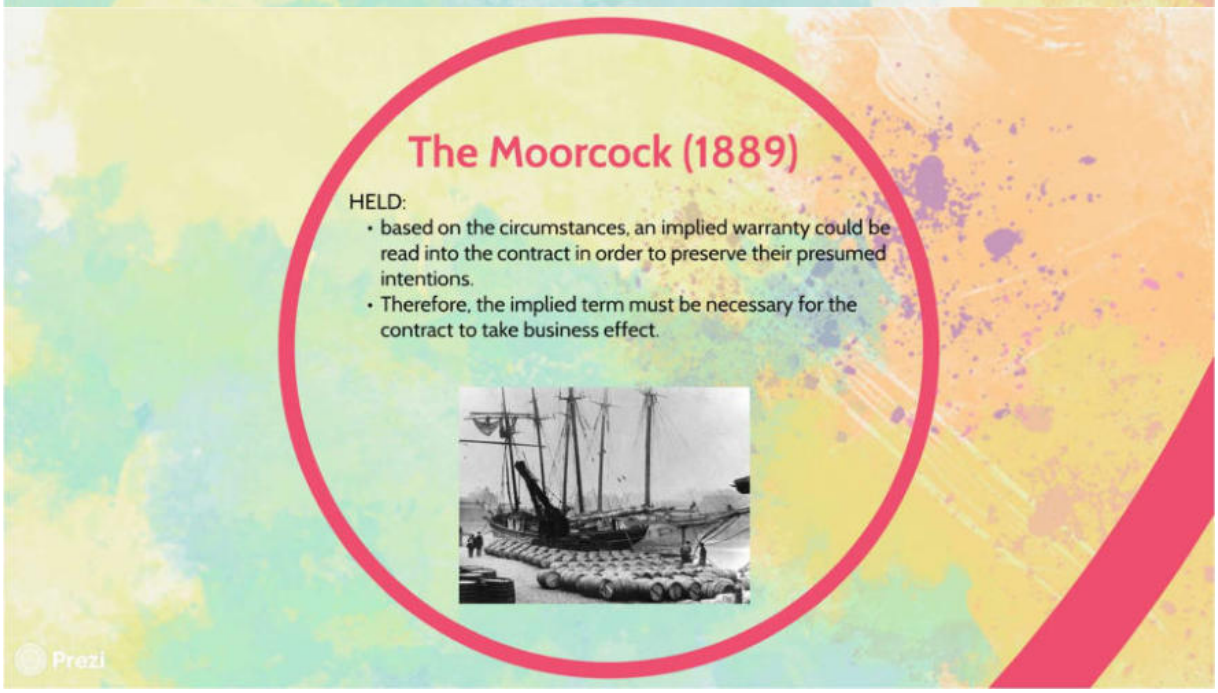

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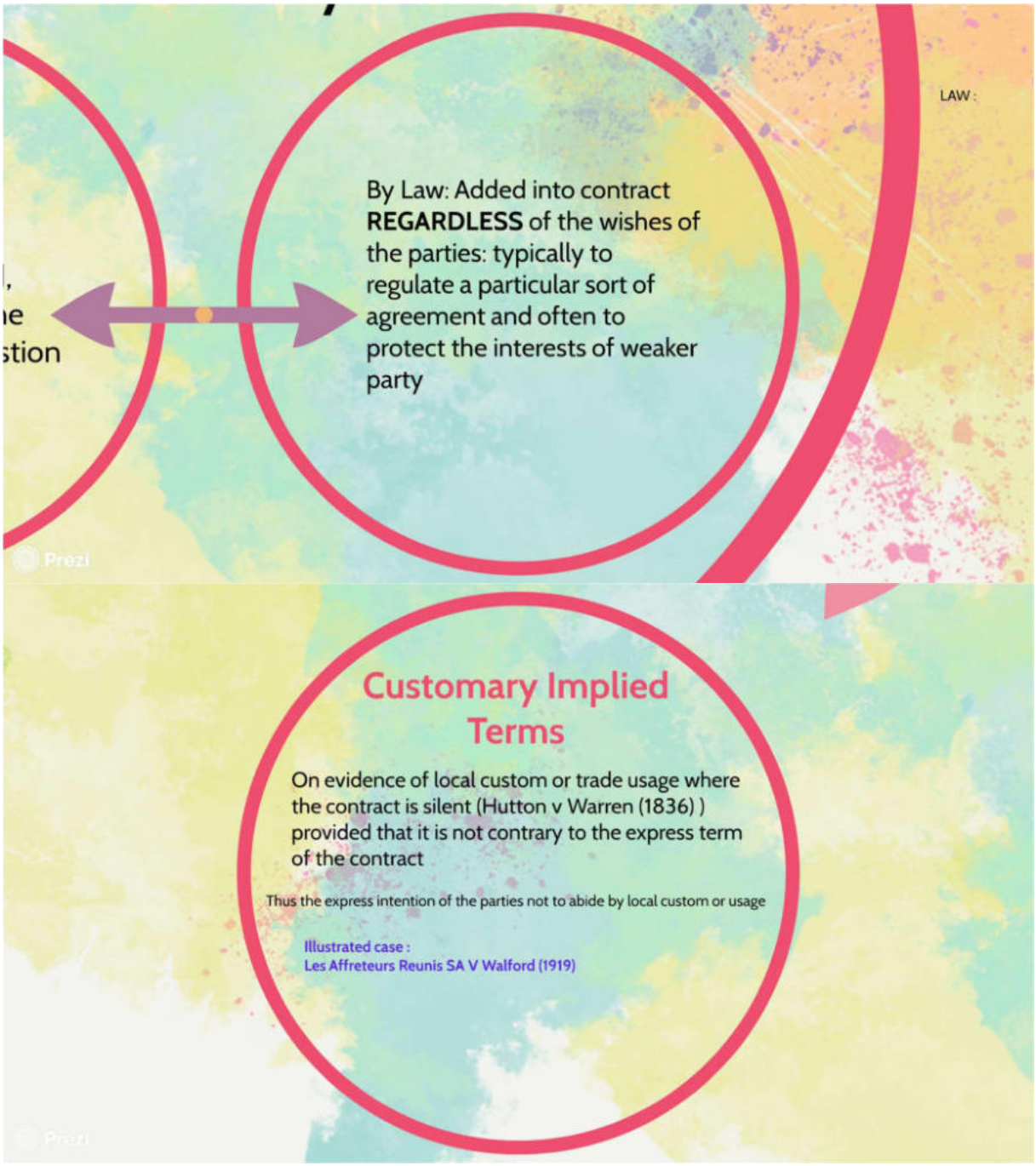

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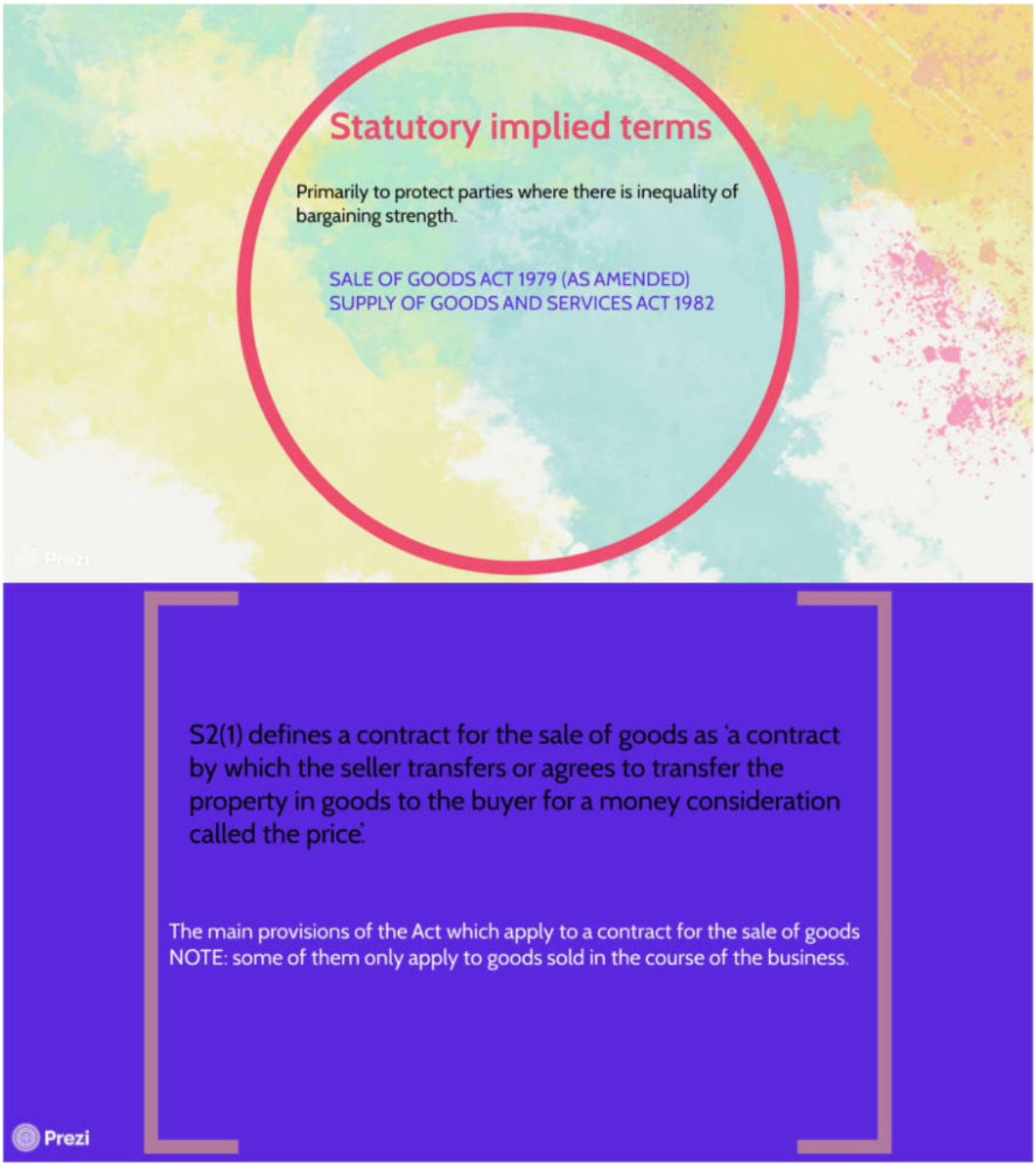

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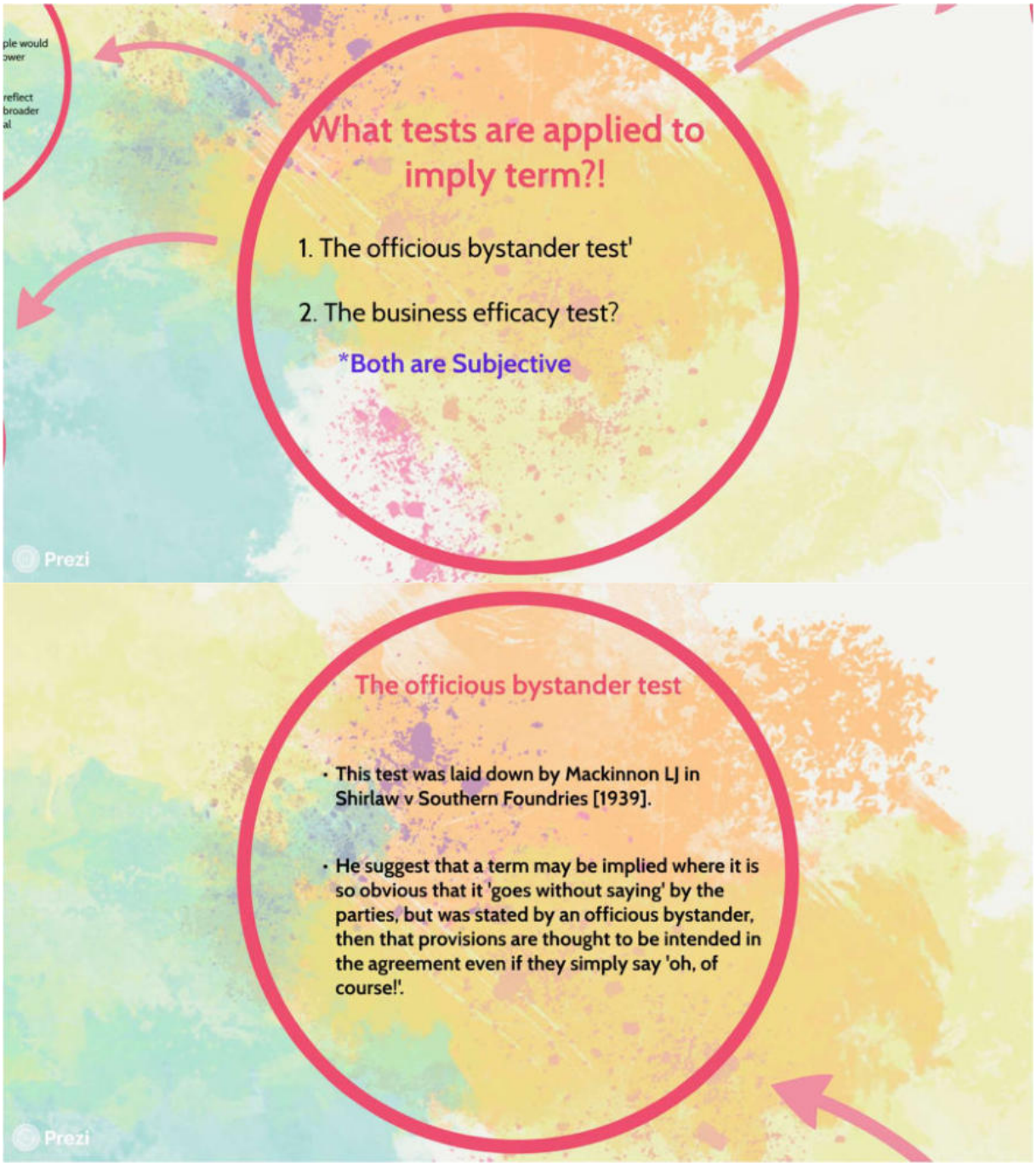

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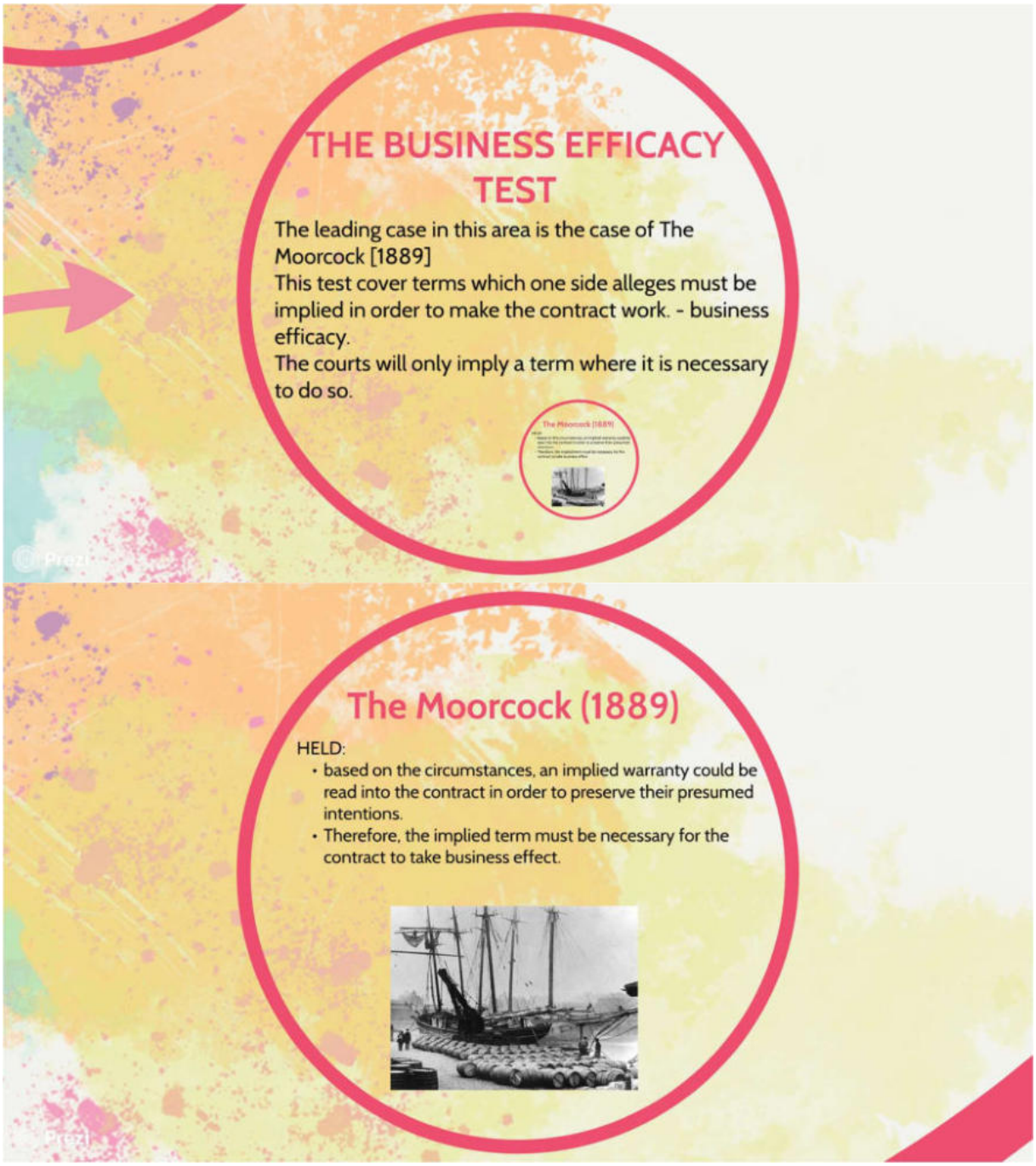

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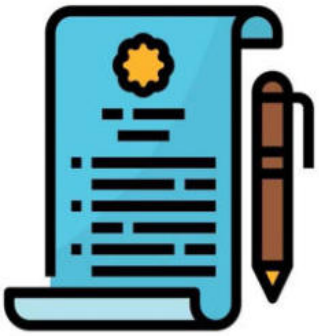
Week 9: The Contents of the Contracts Implied Terms

Introduction to Implied Terms

- A normal contract is not an isolated act, but an incident in the conduct of business
- Contracts are frequently set against a background of usage, familiar to all who engage in similar negotiations
- Implied terms are just as binding as express terms



Implied Terms – Perspective

Terms implied by fact → Officious bystander & business efficacy tests

Terms implied by law → SGA, SGSA

Terms implied by custom → Rabbits

Implied Terms

- **[1/3] Terms Implied by Fact**
  - Terms which reflect the *"unexpressed intention"* of the parties
  - Could be left out by mistake, or they could be so obvious that it goes without saying (the "*officious bystander test*") – ***Shirlaw v Southern Foundries (1926)***

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Week 9: The Contents of the Contracts Implied Terms

Implied Terms

- **[2/3] Terms Implied by Law**
  - Sale of Goods Act 1979
    - S12(1) – Title to goods
    - S13(1) – Sale by Description
    - S14(2) – Quality
    - S14(3) – Fitness for Purpose
    - S15(2) – Sale by sample
  - Sale of Goods and Services Act 1982
    - S13 – Reasonable Skill and Care

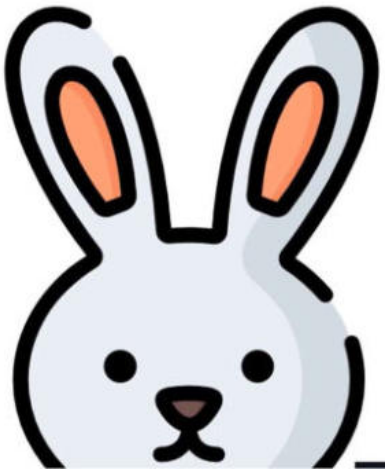
Implied Terms

- **[2/3] Terms Implied by Law**
  - Sale of Goods Act 1979
    - S12(1) – Title to goods → CONDITION s.12(5A)
    - S13(1) – Sale by Description → CONDITION s.13(1A)
    - S14(2) – Quality → CONDITION s.14(6)
    - S14(3) – Fitness for Purpose → CONDITION s.14(6)
    - S15(2) – Sale by sample → CONDITION s.15(3)

    Right to reject
    ↑ N
    Was breach slight? Unreasonable to reject? s.15A(1)
    ↓ Y
    Right to damages
  - Sale of Goods and Services Act 1982
    - S13 – Reasonable Skill and Care

Implied Terms

- **[3/3] Terms Implied by Custom**
  - Terms can be implied into a contract if there is evidence that, under local custom, they would normally be there – ***Smith v Wilson (1832)***
  - 10,000 rabbits = 12,000 rabbits…



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judges to attribute to the parties an intention which they plainly could not have had.

6.6 IMPLIED TERMS

An implied term is one that is not expressed orally or in writing by the parties to the contract, but which is implied by the court through fact, law, custom or statute, to deal with a specific situation before it.

6.6.1 IMPLIED TERMS IN FACT

The courts will imply a term if they consider that it represents the true intention of the parties on a particular issue. The term is implied on the basis that, as a matter of fact, this was the intention of the parties, even though the parties had not thought about the issue at the time the contract was agreed. It is not sufficient that the term makes the contract more fair or more reasonable; it must be necessary to imply such a term. Nor will a term be implied to deal with an eventuality which the parties had not anticipated; if they failed to anticipate it they cannot be said to have intended that a particular term would apply to the situation (see *Crest Homes (South West) Ltd v Gloucestershire County Council* [1999] EWCA Civ 1642).

Traditionally, the courts would apply the following key tests when implying a term into a contract as a matter of fact:

- The officious bystander test: "if, while the parties were making the bargain, an officious bystander were to suggest some express provision for it in the agreement, they would testily suppress him with a common "Oh, of course!" (*Shirlaw v Southern Foundries* [1939] 2 KB 206, MacKinnon LJ).

- The business efficacy test: the terms had to be implied to make the contract work; *The Moorcock* (1889) 14 PD 64. Subsequent case law made clear that that term could only be implied if the contract could not work without it; *Trollope & Colls Limited v North West Metropolitan Hospital Board* [1973] 1 WLR 601.

The officious bystander and business efficacy tests were later refined by Lord Simon of Glaisdale in *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266 when describing the overlapping conditions which were thought to be necessary to imply a term in fact: "(1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that 'it goes without saying' (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract" (282-283).

However, according to Lord Hoffman, giving the lead judgment of the Judicial Committee of the Privy Council in the case of *Attorney General of Belize and others v Belize Telecom Ltd and another* [2009] UKPC 10 (*Belize*), going forward the correct approach to the question when to imply a term into a contract involves arriving at a proper construction or interpretation of the contract by applying an *objective 'construction' approach only*. According to this approach: "[i]n every case in which it is said that some provision ought to be implied in an instrument, the question for the court is whether such a provision would spell out in express words what the instrument, read against the relevant background, would reasonably be understood to mean" (at paragraph 21 of the judgment). Lord Hoffman said that the previous tests are but pointers which might or might not help to explain the parties' contractual intention.

6.6.2 REQUIREMENT OF NECESSITY

In *Mediterranean Salvage & Towage Ltd v Seamar Trading & Commerce Inc (The Reborn)* [2009] EWCA Civ 531, the Court of Appeal applied the approach set out by Lord Hoffman in *Belize*, but affirmed that the requirement of necessity was still a determining factor in whether to imply a term into a contract. Sir Anthony Clarke MR said that Lord Hoffman was "not in any way resiling from the often stated proposition that it must be necessary to imply the proposed term. It is never sufficient that it should be reasonable."

6.6.3 TERMS IMPLIED BY CUSTOM

Terms may be implied by custom or usage of a particular trade or business, market or locality. Thus, in one case, the owner of a crane hired it to a contractor who was engaged in the same business. It was held by the Court of Appeal that the owner's terms, which were usual in the business (and a "common understanding" between the parties), were binding on the hirer, although they had not actually been communicated at the time of hiring (*British Crane Hire v Ipswich Plant Hire* [1975] QB 303).

Terms of collective agreements between trade unions and employers may be incorporated into individual employees' contracts by implication, on the basis that the terms of the collective agreement are uniformly observed for the group of workers, of which the employee is a member.

6.6.4 TERMS IMPLIED BY LAW

Terms implied by statute may be of two kinds: (a) obligatory terms, as in consumer protection legislation; (b) terms which will apply, unless the parties contract out of the statutory terms, such as the terms of a partnership implied by the Partnership Act 1890, which may be excluded.

Occasionally, the courts imply a term that the parties would not, in fact, have considered. This is an instance where the courts imply as a matter of law how they think the contract should be performed. In *Liverpool City Council v Irwin* [1977] AC 239, the House of Lords spelt out that it was an implied term of the lease held by the council that the council should take reasonable care to maintain a property in a reasonable state of repair. In *Irwin*, Lord Denning rejected the argument that such terms should be exclusively subject to a business efficacy test. The court could, he stated, imply a term whenever it was just and reasonable to do so, whether the term was incorporated into the contract or not.

6.6.4.1 Sale of Goods

Certain terms are implied in contracts for the *sale* of goods (as opposed to gifts, barters, contracts for the supply of services, agency contracts, loan contracts with goods as security, hire purchase contracts, etc.).

The main statute is the Sale of Goods Act 1979, which codified the terms implied into contracts of sale.

The 1979 Act implies the following terms:

(A) IMPLIED TERMS ABOUT TITLE

Seller's right to sell goods

Section 12 implies a term on the part of the seller that he has the right to sell the goods (or will

have the right to sell them when property in the goods is transferred), as well as a warranty of freedom from encumbrance and quiet possession. So, where the seller owns the goods, but he can be prevented by a third party from selling them, this condition will be broken. In light of this, *Rowland v Divall* [1923] 2 KB 500 stands for the principle that a sale of goods contract is not defined by the use of the goods, but by the transfer of ownership.

In *Butterworth v Kingsway Motors* [1954] 1 WLR 1286, A sold a car to B, before all hire purchase payments had been made. B then sold to C and C sold to Kingsway Motors, which then sold the car to Butterworth. The final hire purchase payment had still not been paid. Butterworth used the car for 11 months before he found this out, and then told Kingsway he was cancelling the contract. The court held that there had been a breach of section 12 and Butterworth could repudiate the contract, as the title had not been fed. Kingsway, B and C could only claim damages.

In *Niblett v Confectioners Materials* [1921] 3 KB 387, Confectioners sold 3,000 tins of condensed milk to Niblett. Confectioners argued that, under an oral contract, the milk would be one of three brands – "Freedom", "Tucson" or "Nissley". Confectioners delivered 2,000 cases of "Freedom" and then 1,000 tins of "Nissley". In November, Niblett received a letter from Nestlé, stating that "Nissley" imitated the Nestlé trademark and asked Niblett not to sell it. It also threatened to take proceedings against Niblett. Niblett signed an undertaking not to sell, advertise or offer for sale the "Nissley" condensed milk. They then, unsuccessfully, asked Confectioners to take it back and, unsuccessfully, applied for an export licence for it. Niblett claimed damages for breach of warranty that:

- the milk was of merchantable quality;
- Confectioners had a right to sell it;
- Niblett should have enjoyed quiet possession; and
- there was an implied condition or warranty that the label on the milk would not infringe any trademark.

Bankes N J, of the Court of Appeal, found that there was a clear breach of section 12 of the Sale of Goods Act because Confectioners had no right to sell the goods, as they were, and Niblett had never enjoyed quiet possession.

Sale by Description

Section 13 implies a term that, where goods are sold by description, the goods will correspond with the description. This applies even where the buyer examined the goods before purchasing them. The seller has strict liability: even if he was not in any way at fault, he will still be liable if his goods do not conform to the description applied to them. In *Beale v Taylor* [1967] 1 WLR 1193, a car was advertised as, and the buyer inspected the car and found it to be, a 1961 Triumph Herald 1200. In fact, only the back half corresponded with the description. The sale was held to be a sale by description, despite the buyer's pre-contract inspection.

(B) IMPLIED TERMS ABOUT QUALITY & FITNESS

Section 14(2) provides that, where the seller sells goods in the course of a business, there is an implied term that the goods are of satisfactory quality. For example, in *Rogers v Parish (Scarborough) Ltd* [1987] QB 933, it was established that a series of defects in an expensive car model would make it unmerchantable, even though it was fit to drive. A key component in the s. 14(2) SOGA analysis is, therefore, that, if a person pays a high price, he is entitled to a similarly high standard of quality.

The Sale and Supply of Goods Act 1994 made substantial amendments to s. 14 of the Sale of Goods Act 1979. The new sections 14(2A) and (2B) define "satisfactory quality" as being of a standard that a reasonable person would regard as satisfactory, having regard to description, price and all other relevant circumstances. Quality even includes aspects such as appearance and finish, and freedom from minor defects. However, if any defect making the goods unsatisfactory was specifically drawn to the attention of the buyer, or if he examined the goods before purchase, and the examination revealed or ought to have revealed the defect, then the terms implied by s. 14(2) do not apply (s. 14(2C)(b)).

Section 14(3) provides that, where the seller sells goods in the course of a business and the buyer makes known to the seller any particular *purpose* for which the goods are being bought, there is an implied – strict liability – term that the goods are reasonably fit for that purpose, whether or not that is the common purpose of such goods.

Notwithstanding the foregoing, the buyer need not expressly state the purpose for which the goods are required, if it is obvious (e.g. milk containing typhoid germs was held not fit for its purpose (drinking), even though it had not been stated by the buyer that the milk would be drunk[3]) – save where the buyer did not rely, or it would have been unreasonable for him to rely, on the seller's skill or judgement. Nevertheless, in *Griffiths v Peter Conway* [1939] 1 All ER 685, the claimant purchased a tweed coat, which had been tailored to her specific instructions. The coat gave her dermatitis, due to her having abnormally sensitive skin. Even though the coat turned out not to be suitable for the purpose, the Court of Appeal held the defendant not liable.

Sale by Sample

Section 15 provides that, in the case of a contract for sale by sample, there is an implied term that the bulk will correspond with the sample, in quality; that the buyer will have a reasonable opportunity of comparing the bulk with the sample; and that the goods will be free from any defect rendering them of unsatisfactory quality, which is not apparent on reasonable examination of the sample.

6.6.4.2 Sale of Goods and Services

The Supply of Goods and Services Act 1982 extends the terms of the Sale of Goods Act 1979 to contracts which are mainly concerned with the supply of services, such as contracts of repair. The 1982 Act contains provisions which correspond to those in the 1979 Act, e.g. that the supplier must carry out the service he is providing with reasonable skill and care; that he will carry out his service in a reasonable time; and that if the price for the service is not fixed by contract or determined by the course of dealing, the party contracting with the supplier will pay a reasonable charge.

6.6.4.3 Exemption Clauses

As we have seen, the terms implied into contracts of sale have largely evolved from case law. Much depends on whether an implied term is a condition or a warranty, and on whether one party to the contract is dealing as a consumer.

Normally, the implied terms can be varied or negated by express agreement or by trade usage. However:

- An express term will only negate an implied term if it is inconsistent with it.

[3] *Frost v Aylesbury Dairy Co Ltd* [1905] 1 KB 608.

- Any express term exempting the seller from all or any of the implied obligations as to title in s. 12 is void (s. 6(1) UCTA 1977).
- The statutory terms in a consumer sale (i.e. when the buyer is not buying in the course of a business) relating to contract description, sample, quality or fitness for purpose (ss. 13-15 SOGA) cannot be excluded or restricted. The onus is on the seller to prove that a particular sale is *not* a consumer sale (s. 6(2) UCTA 1977).

Where the buyer is *not* dealing as a consumer (e.g. he is in business to re-sell), ss.13-15 SOGA may be excluded or restricted, provided it is fair and reasonable to do so (s. 6(3) UCTA 1977). In this regard, even a business can operate as a consumer, e.g. where it purchases a car for one member of staff.