THE EFFECT OF EXCLUSION CLAUSES

G. H. L. FRIDMAN*

The extent to which parties to a contract are free to arrange the existence and scope of their respective liabilities by the use of exemption clauses under a contract is a concern touching an unclear area of the law. Professor Fridman, recently appointed to the Faculty of Law of The University of Alberta and commencing tenure in the 1969-70 academic year, surveys the case law and concludes that proper judicial control of the freedom of contract is essential to the protection and future usefulness of that freedom.

Limitation or total exclusion of liability by agreement is a familiar legal phenomenon. In the law of tort it is manifested most clearly in cases in which the courts have applied the maxim *volenti non fit injuria*, the employment and exposition of which has caused much concern and not a little inelegance from the standpoint of principle.[1] The application in the law of tort of the idea of auto-limitation is not the concern of the present essay. In the ensuing pages the subject for consideration is the extent to which, as the law now stands, the parties to a contract are free to arrange the existence and scope of their respective liabilities under such contract, particularly in respect of any breach. Not very long ago, and elsewhere, the present writer discussed the more general idea of freedom of contract, and included in that discussion some reference to the question of limitation or exclusion of liability.[2] In the context there was no opportunity for anything more than a very superficial glance. Such consideration as there was, however, may be taken as the starting-point for the present discussion. In brief the argument advanced in that essay was that, despite the decision of the House of Lords in *Suisse Atlantique Societe d'Armament Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale*,[3] there might still be some life in the doctrine of "fundamental breach" or "breach of fundamental term", so as to permit the courts to negate the effects of an attempt by one party, or both, to oust or delimit his or their liability. Was this a fair conclusion? To answer this question it is necessary to examine the nature of the problem involved in this area of the law: how the courts dealt with it prior to the recent decision: and what was said in the House of Lords.

The nature of the problem can be indicated by looking at the facts of some recent Canadian cases. In *Knowles* v. *Anchorage Holdings Co. Ltd.*[4] in 1964, a contract for the sale of a boat engine provided among other things that "the Buyer relies solely on his own judgment that the equipment . . . is fit for the purpose for which it is required and that . . . there are no representations, warranties, or conditions express or implied, statutory or otherwise, other than those herein contained. . . ." This language, which stems from the line of English cases, commencing with *Wallis* v. *Pratt*,[5] in which the language of exclusion or exemption was gradually developed, fell to be considered by Verchere, J., of the British

* M.A., B.C.L., LL.M., Barrister-at-Law, Reader in Law, University of Sheffield.

1 Fridman, *Modern Tort Cases* 94-101 (1968).
2 Fridman, *Freedom of Contract* (1967), 2 Ottawa L. Rev. 1, 12-14.
3 [1966] 2 All E.R. 61.
4 (1964), 63 D.L.R. (2d) 300.
5 [1911] A.C. 394: see Fridman, *Sale of Goods* 186-188 (1966).

Columbia Supreme Court when the seller delivered an engine which was so defective that it was not really workable: it did not function normally. Was the effect of the language of the contract such as to deprive the buyer of such remedies as he would otherwise legitimately have been entitled to pursue by reason of the provisions of the Sale of Goods Act relating to implied terms as to fitness for purpose and merchantability? A year later the Manitoba Court of Appeal dealt with the same issue in *Western Processing and Cold Storage Ltd.* v. *Hamilton Construction Co. Ltd. and Dow Chemicals of Canada Ltd.*[6] In this instance the contract was for the building of a cold storage plant by Hamilton using insulating material purchased from Alsip and manufactured by Dow. The material was relatively new and untested and was shipped by Dow without being properly cured and while still being likely to shrink. As a consequence of the use of this material the cold storage plant was unsatisfactory. So far as liability was concerned, the order forms between Dow, the manufacturer, and Alsip, the distributor, purported to place all responsibility for loss or damage resulting from the use of goods sold on the distributor. Other agreements between Dow and Alsip provided that Dow made no warranty concerning the goods sold except that they should be of the quality and specifications stated in the contract and that the buyer assumed all responsibility and liability for loss or damage resulting from the handling or use of the goods. Once it was decided that such terms governed the oral agreement which was made between Dow and Alsip in the instant case,[7] was the effect of such terms to exonerate Dow from any responsibility to the plaintiffs for whom Hamilton was making the plant and in the manufacture of which Dow's material was being used? The third case arose in Alberta: *Canadian-Dominion Leasing Corporation Ltd.* v. *Suburban Superdrug Ltd.*[8] Here the contract was for the lease of an automated commercial display. The contract provided, *inter alia,* that the lessor made no representations or warranty, express, implied, statutory or otherwise, as to any matter whatsoever, including, without limitation, the condition of the equipment, its merchantability or its fitness for any particular purpose. The selector which was leased under this agreement turned out to be defective. When repaired or replaced the selector operated for a very short period of time and then broke down again. After the third breakdown the lessee put the machine into a basement of his premises and did not use it. Consequently it was of no use to him for the purposes for which he agreed to rent it. Was the lessor able to claim arrears of rent under the lease? That depended upon whether he could be held liable for the defective quality of the goods supplied under that lease. Finally, reference may be made to another Manitoba case, decided after the *Suisse Atlantique* case, but containing no mention of it. This is the decision of Tritschler, C.J.Q.B., in *Keelan* v. *Norray Distributing Ltd.*[9] in 1967. This was concerned with the sale of prototype models of coin-operated vacuum cleaners by a company established to market them to a partnership of businessmen who were going to make commercial use of them. The standard form printed conditional sale contract which related to these machines contained a term (in small print) under which

6 (1965), 51 D.L.R. (2d) 245.
7 This gave rise to another issue not relevant to the present discussion.
8 (1966), 56 D.L.R. (2d) 43.
9 (1967), 62 D.L.R. (2d) 466.

the seller excluded all representations, collateral agreements, conditions or warranties, express or implied, by statute or otherwise, with respect to the property. The machines as delivered were worthless.

> From the first day of use the experience was very bad. Almost every machine broke down and breakdowns were continuous. The malfunctions were various. Hoses would come off their reels; hose reels would jam and could not be unwound or would jam with the hoses extended and not automatically re-wind; customers faced with a 'jammed out' hose would push it back into the machine and cause further damage; there was a failure of vacuum; the coin mechanisms were defective.[9a]

Could the purchasers under the conditional sale agreement repudiate and rescind this contract? Or were they bound by the exclusion clause therein?

These various facts pose in a dramatic fashion the dilemma of the courts. On the one hand, pledged as they would seem to be to the notion of upholding the sanctity of contracts entered without fraud, duress or other vitiating element, they would appear to be compelled to give effect to a clause which excluded any kind of liability for the sort of breach which occurred in each of these cases. On the other hand, to permit a party to exclude all possible liability for misperformance of his contract would seem to be the very negation of the notion of contract. It would countenance the idea that whereas A might be bound by the terms of a contract to perform vis-a-vis B, B might not be bound to do anything vis-a-vis A. In the context of these cases, the engine might be useless but the buyer was bound to pay the price and had no redress: the cold storage plant would not work but the person for whom it was constructed could not be recompensed: the selector could lie idle in the basement, but the rent for its leasing was due: the vacuum cleaners would not work, but the price still had to be paid. Such a result, to any reasonable mind, would appear to be ridiculous, illogical, and unjust. However, a strict and logical application of the 'rules' of the law of contract would seem to dictate just such a result. Failing proof of such sharp practice as would be tantamount to fraud, a person relying upon the trustworthiness of the other party to his contract, signing away all the other's obligations, possibly after failing to read or to understand the small print contained in, or more usually on the back of the standard form, printed contract, seemingly immutable in its terms, would be bereft of any remedy when he discovered that he had obtained something that was useless to him. This is precisely the situation which the logical development of the law of contract engendered in the English case of *L'Estrange* v. *Graucob*.[10]

A way out of this doctrinal impasse was metaphorically blasted by the English courts in a series of cases which may be said to have their foundation in the decision of the House of Lords, on appeal from Scotland, in *Pollock & Co.* v. *Macrae*,[11] though one writer[12] has put forward the alternative suggestion that the modern doctrine starts its history with the somewhat later House of Lords decision in *Hain* v. *Tate & Lyle*.[13] Whatever the starting-point, later cases were not backward in seizing

9a *Id.*, at 475.
10 [1934] 2 K.B. 394.
11 [1922] S.C. 192; though in some respects the whole doctrine may be said to stem from the language of Lord Abinger, C.B., in *Chanter* v. *Hopkins* (1838), 4 M. & W. 399; 150 E.R. 1484.
12 Coote, *Exception Clauses* 104 (1964).
13 [1936] 2 All E.R. 597.

upon the hints provided in earlier decisions. In a variety of situations, involving several different kinds of contract, viz., sale of goods,[11] hire-purchase,[15] bailment,[16] and shipping,[17] the same approach was adopted. It may be stated succinctly in these words of Denning, L.J., as he then was, one of the principal protagonists of this modern view, in *Karsales (Harrow) Ltd.* v. *Wallis*:[18]

> The principle is sometimes said to be that the party cannot rely on an exempting clause when he delivers something 'different in kind' from that contracted for, or has broken a 'fundamental term' or a 'fundamental contractual obligation'. However, I think that these are all comprehended by the general principle that a breach which goes to the root of the contract disentitles the party from relying on the exempting clause.

Put differently, by one of the many commentators who have written on this subject in the past few years:[19] "A party who has been guilty of a fundamental breach of contract cannot rely on an exemption clause inserted in the contract to protect him."

Hence in the Canadian cases outlined earlier, the innocent party who was the victim, albeit in circumstances which did not reveal that he was necessarily the deliberate victim,[20] of the other party to the contract, was able to recover damages, or repudiate or escape liability, whichever was appropriate, despite the inclusion in the contract of an exclusion or disclaiming clause. In all these instances the Canadian court followed the earlier English authorities and applied the doctrine stated above. Thus Verchere, J., said: "I find here that the defendant was in breach of a fundamental term of the contract to purchase an engine of workable character, that is to say, an engine that would operate as it should have, and cannot therefore rely on the exemption clause."[21] Monnin, J.A., delivering the judgment of the Court in the *Western Processing Case*,[22] said: ". . . I am unable to accept that Dow can be released from its specific duty to supply a satisfactory product simply by relying on the aforesaid clauses of the acknowledgement of order form. These were exempting clauses and they cannot be relied upon where there has been a clear breach by Dow of a fundamental term going to the root of the contract." Similarly Tritschler, C.J.Q.B.:[23] "As Norray was guilty of a breach which went to the very root of the contract, it cannot rely upon the exempting clause." In all these instances, therefore, there was "a breach of contract of a flagrant nature," to quote the language of Bastin, J.,[24] cited and approved by Kane, J.A., in the Alberta case,[25] such as justified the invocation of the principle in the *Karsales* case.

With the innate justice of this approach and the results its application produced there can be scarcely any dispute. The strict doctrines of con-

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14 *U.G.S. Finance Ltd.* v. *National Mortgage Bank of Greece* [1964] 1 Lloyd's Rep. 446; cf. *Pinnock Bros.* v. *Lewis & Peat* [1923] 1 K.B. 690.

15 *Karsales (Harrow) Ltd.* v. *Wallis*, [1956] 2 All E.R. 866; *Yeoman Credit Ltd.* v. *Apps*, [1961] 2 All E.R. 281; *Astley Industrial Trust Ltd.* v. *Grimley*, [1963] 2 All E.R. 33; *Charterhouse Credit Co. Ltd.* v. *Tolly*, [1963] 2 All E.R. 432.

16 *Smeaton Hanscomb & Co. Ltd.* v. *Sassoon J. Setty Son & Co.*, [1953] 2 All E.R. 1471; *Spurling* v. *Bradshaw*, [1956] 1 W.L.R. 461; cf. *Hunt* v. *Winterbottom* v. *B.R.S.*, [1962] 1 Q.B. 617.

17 *Sze Hai Tong Bank Ltd.* v. *Rambler Cycle Co.*, [1959] 2 All E.R. 182.

18 *Supra*, n. 15, at 869.

19 Guest, *Fundamental Breach of Contract* (1961), 77 L.Q.R. 98. For further references see Coote, *op. cit. supra*, n. 12, at 104, n. 1.

20 Note, however, Lord Denning's exposition of "deliberate" disregard of obligations as constituting fundamental breach in the *Sze Hai Tong* Case, *supra*, n. 17, at 186.

21 *Supra*, n. 4, at 304.

22 *Supra*, n. 6 ,at 250-251.

23 *Supra*, n. 9, at 476.

24 *Schmidt* v. *International Harvester Co. of Canada Ltd.* (1962), 38 W.W.R. 180, 183.

25 *Supra*, n. 8, at 56: Lord Denning in the *Sze Hai Tong* case, *supra*, n. 20.

tract, if strictly enforced, could lead to some absurd consequences. A party could deliver something totally different from that which he had contracted to deliver: or otherwise perform in a totally different manner from what he had undertaken: given an appropriately worded exemption clause he might not be responsible for any loss or damage ensuing from his actions. Only a society which viewed the functions and status of contractual obligations through blinkers could tolerate or justify such a situation. However, acceptance of the notion of 'fundamental breach' or 'breach of fundamental term' did not eradicate all juristic difficulties. On the contrary.[26]

In the first place, there was uncertainty whether the doctrine was properly to be described as 'fundamental breach' or 'breach of fundamental term.' That this is no mere semantic differentation can be illustrated by reference to the law of sale of goods, where the basic distinction of contractual terms into conditions and warranties, with, seemingly, no room for any third type of term, more 'fundamental' or basic than a condition, caused writers, if not judges, some concern. Perhaps the same problems did not, or need not have arisen in relation to other contracts, in respect of which the condition-warranty dichotomy was not essential in the sense of being dictated by statute. Nevertheless, the cases indicated that the pattern of sales contracts applied to others, and therefore, possibly without substance, produced the same juristic crisis as cases dealing with sale of goods. Secondly, whatever the nature of the doctrine juristically speaking, it gave rise to the suggestion that there was a limit to the extent to which parties could effectively oust the jurisdiction of the courts, by removing any cause of action at the instance of an aggrieved party. This would seem to be in conflict the principle to be found in well-known decisions[27] that parties could so 'agree' (to use a neutral term) that their bargain was to be binding in honour only and not to be taken as evidencing any intent to create binding, legal obligations. Thirdly, by way of corollary to this, the doctrine could be used to enable courts to reconstruct a contract for parties, albeit within certain well-defined boundaries, and substitute what the court felt was just and fitting in place of what the parties, voluntarily and without any error on either side, had assented to between themselves. In consequences of this, it became suggested that, as a matter of law, it was not possible for parties to contract out of whatever was the 'fundamental' obligation inherent in their particular contract. Finally, and by no means least importantly, there was the problem of deciding what was a 'fundamental' breach or a 'fundamental' obligation. The difficulty of deciding whether the conduct of a party merited his being deprived of the protection he had attempted to provide for himself by the contract, permitted the courts to play a major role in the decision of liability, over and above the normal part played by the courts in discovering the facts and applying settled pirnciples of law to them. The indefiniteness of the doctrine, as expounded in the cases, and the way that decisions in which the doctrine was invoked depended upon the particular view taken by the court at the time of the nature of the alleged defect or defects in the alleged wrongful party's per-

[26] Cf.: Coote, op. cit. *supra*, n. 12, at 108-111.
[27] E.g. *Rose & Frank* v. *Crompton Bros.* [1925] A.C. 445.

formance of his obligations,[28] thereby rendering it impossible to tell in advance whether or not there was any substance in the injured party's attempt to resist the operation of an exemption clause, meant that the law was uncertain in the very area in which certainty was an eminently desirable end to attain, namely commercial transactions. Thus the emergence of this novel doctrine, although perhaps dictated by the development of the law as to exemption clauses and the growing importance of such clauses in commercial situations, produced uncertainties of principle and of application.

Perhaps in order to harmonise this new doctrine with the notion of absolute freedom of contract, which seemingly was placed in jeopardy by the logical extension and juristic explanation of this doctrine, an attempt was made by one writer[29] to expound the characteristics of exemption clauses in a different way. This explanation took the form of regarding exemption clauses in the main as substantive, rather than as procedural in their effect. An exemption clause did not operate to deprive a party of a remedy he otherwise would have been able to pursue for breach of contract. The function of such a clause was "to place substantive limitations upon the rights to which they apply, and, accordingly, to help delimit and define those rights."[30] Such a clause would "not have effect merely as a shield to claims for damages. It would in fact, prevent those rights from accruing in the first place."[31] In this regard the analogy was drawn (with some reason and justification, it may be said) between the effect and function of exemption clauses and the operation of the doctrine of consent or assumption of risk in the law of tort, notably the law of negligence. There might still be exemption clauses which were procedural rather than substantive, e.g. a clause which limited the time within which a claim could be made, as opposed to a clause which excluded the operation of all conditions, warranties, etc., statutory or otherwise, express or implied. Apart from such special instances, however, and in the situations which were covered by the leading cases, an exemption clause was relevant not at the stage of litigation, when the rights of action of a party were in question, but, long before that, at the stage when the obligations of the party in whose favour the exemption clause had been inserted were being investigated. In this regard cases on "deviation" in relation to shipping contracts, and the principle enunciated by Scrutton, L.J., in *Gibaud* v. *Great Eastern Rly.*[32] of performance within the "four corners" of the contract, were of vital importance and relevance.[33]

This argument, and the reasoning adduced in its support, were favoured by Windeyer, J., dissenting it should be noted, in the High Court of Australia in *Thomas National Transport (Melbourne) Pty. Ltd.* v. *May & Baker (Australia) Pty. Ltd.*[34] decided after the *Suisse Atlantique* case. There an action was brought in respect of the loss by fire of a consignment of goods. Over a number of years a consignor had employed a particular company to carry its goods from one State to another. These goods were regularly collected by a contractor who

[28] Contrast e.g. the cases cited in *supra*, n. 15.
[29] Coote, *op. cit. supra*, n. 12, at 7-14.
[30] *Id.*, at 7.
[31] *Ibid.*
[32] [1921] 2 K.B. 426, 433: see also *Lilley* v. *Doubleday* (1888), 7 Q.B.D. 570.
[33] Coote, *op. cit. supra*, n. 12, Chapters 6, 7.
[34] (1966), 115 C.L.R. 353.

took them to the carrier's Melbourne depot whence they were taken for delivery to the consignee. All this was known to the consignor. The form of contract between the consignor and the carrier did not specify any route to be taken or state that the goods collected should be taken to the depot. Each form of contract contained a clause exempting the carrier and its agents from responsibility for loss, damage or misdelivery of goods "in transit or in storage" for any reason whatsoever. On one occasion the sub-contractor was unable to leave the goods in the depot, because his round concluded later than usual. After trying unsuccessfully to communicate with the depot by radio, he left the goods in the truck in which he had collected them in his garage, which contained no fire extinguisher and had no side door. In the middle of the night a fire occurred, from an unknown external source, and the goods were destroyed. In an action by the consignor against the carrier and the sub-contractor it was held by the majority of the court that the carrier was liable, despite the exemption clause. This was because it was an implied term of the contract of carriage that the goods collected would be taken to the carrier's depot at the end of each collection round: and there had been a departure from the contract by the carrier which was of such a nature as to prevent the carrier from relying on the exemption clause.

The majority of the court came to this conclusion without considering the *Suisse Atlantique* case, or the earlier decisions on fundamental breach or breach of fundamental term, or the juristic problems to which they have given rise. Nonetheless the case is very relevant to the present issue, notably because of the judgment of Windeyer, J. To appreciate why this is so, it is necessary at this juncture to consider the decision and speeches in the *Suisse Atlantique* case.

Oddly enough that case was not properly about the effect of an exclusion clause. The point was argued for the first time in the House of Lords, and was really otiose, since their lordships had already decided against the appellants, the owners of a ship which was under charter to the respondents, on other grounds, and only considered the argument relating to exclusion clauses to avoid delay and expense. Even if the point had arisen, there were grounds for saying that the clause in issue was not an exclusion clause in the strict sense, giving rise to the problem. If it were such a clause, then the remarks made in the House indicate that its construction would not have permitted it to be effective in the way argued by the appellants. Lastly, even if it had been so effective, the House was by no means sure that the facts supported a conclusion that was argued for by the appellants.

The case arose out of a claim by the appellants for damages for breach of a charterparty under which they chartered a vessel to the respondents for two years' consecutive voyages for the carriage of coal from the United States to Europe. Briefly, what happened was that fewer journeys were made than ought to have been made during the contract period. As a result the appellants argued that they were deprived of the freights they would have earned had the correct number of voyages been undertaken. In this respect the respondents claimed that their liability was limited under a clause of the contract to demurrage calculated at the rate of $1,000 a day. Acceptance of their con-

tention would have meant that their liability was in fact about one quarter of the amount sought by the appellants on the basis of damages calculated at large. The real decision in favour of the respondents turned on the question whether the appellants were right in arguing that they had a contractual right to a certain number of voyages. On this the appellants lost. Hence it really became unnecessary to discuss the issue of the limitation clause in the contract. Nonetheless their lordships did discuss this, at great length. However, it must be pointed out that what was truly in issue was a clause limiting liability, not a clause excluding liability in the same way as liability was excluded in the contracts which had come before courts in earlier litigation, some of which have been considered above. Rightly and strictly speaking, therefore, it could be said that their lordships' remarks were, if not *obiter dicta* in a literal sense, at least not as authoritative as if they had been made in a case which squarely involved the problem of an exclusion clause. It would be folly to deny any value or importance to carefully considered statements about the law made by the House of Lords. On the other hand, it is suggested that, in the light of the circumstances in which such remarks were made, there is scope for debate about their effect as well as their meaning.

Viscount Dilhorne[35] differentiated a fundamental breach from a breach of fundamental term. The former involved paying attention to "the character of the breach" and determining "whether in consequence of it, the performance of the contract becomes something totally different from that which the contract contemplates." The latter was something underlying the whole contract so that, if it is not complied with, the performance becomes something totally different from that which the contract contemplated. Is this really a difference? If so, wherein does it lie? In the moment of time at which the 'fundamental' quality or character of whichever is involved, i.e. term or breach, is being decided? Or in the manner in which such 'fundamental' quality is determined? Whether what is involved is a fundamental breach or the breach of a fundamental term, Viscount Dilhorne[36] was sure that there was no rule of law prohibiting or nullifying a clause exempting or limiting liability for either kind of breach. "Such a rule of law would involve a restriction on freedom of contract." The true position was that it was a question of construction of the individual contract concerned. The earlier cases were explicable on the ground that "on construction of the contract as a whole, it is apparent that the exempting clauses were not intended to give exemption from the consequences of the fundamental breach."

Lord Reid[37] considered the theoretical possibilities, i.e. whether the doctrine of no exclusion of liability for a fundamental breach was substantive or a matter of construction, the earlier and more modern cases, and the arguments for and against making such a doctrine into a rule of substantive law, and concluded[38] that "no such rule of law ought to be adopted," at any rate by the courts, because "this rule would not be a satisfactory solution of the problem which undoubtedly exists." Exemption clauses differed so greatly in so many different respects

35 *Supra*, n. 3, at 68.
36 *Id.*, at 67.
37 *Id.*, at 71-76.
38 *Id.*, at 76.

that it would be undesirable for the courts to create such a rule as was argued for, making it impossible to contract out of liability for fundamental breach. Parliament could and should consider whether such a rule was desirable, and should introduce it, if necessary. But not the courts.

Lord Hodson[39] was loathe to differentiate minutely and analytically between different expressions like fundamental breach and breach of fundamental term. Whatever expression was used referred to the same situation, namely, breaches of contract so serious as to justify the injured party in throwing up the contract if he chose. He, too, thought that the rule was one of construction, so that "normally an exception or exclusive clause or similar provision in a contract should be construed as not applying to a situation created by a fundamental breach of contract." It was always to be remembered that one was construing a document and not applying some rule of law superimposed on the law of contract so as to limit the freedom of the parties to enter into any agreement they like within the limits the law prescribes.

The foregoing speeches seem, therefore, to be very limited in scope. They do not usefully clarify the fundamental breach/fundamental term division: they simply state that exclusion clauses require construction in the light of the strict *contra proferentem* rule: they purport to limit the operation of earlier cases to particular situations and particular contracts which permitted of a construction that enabled the courts to declare that the exclusion clauses involved were not competent to destroy the basic liability of the party attempting to rely thereupon. In the speeches of Lords Upjohn and Wilberforce there is more to consider.

Thus Lord Upjohn, after concluding that the demurrage clause in the contract before the House was an "agreed damage" clause, for the benefit of both parties, not a clause of exception or limitation inserted for the benefit of one part only,[40] went on to discuss, at length, the problem now in hand. First he distinguished fundamental breach and breach of fundamental term more thoroughly than had Viscount Dilhorne, making it abundantly clear that fundamental breach is a matter of *ex post facto* construction of the circumstances, whereas a fundamental term is a matter of express or implied agreement (in fact or in law) right from the beginning, even before any acts have been committed by either party.[41] Then he considered the development in the cases, particularly the 'deviation' cases, and concluded that no special rule of law applied.[42] The general law of contract governed, under which a fundamental breach would end the contract, if accepted as such by the innocent party, or would leave it still in force, including any clauses of exception or limitation, if it were not accepted by the innocent party as terminating the contract (which would seem to have been the situation in the *Suisse Atlantique* case—according to some interpretations). By contrast, where a breach of fundamental term is involved the law's attitude was firmer. Instead of looking at the conduct or reaction of the innocent party, the law took the line that there was a "strong, though rebuttable, presumption that, in inserting a clause of exclusion or

39 *Id.*, at 78-79.
40 *Id.*, at 85.
41 *Id.*, at 85, 86.
42 *Id.*, at 86-88.

limitation in their contract, the parties are not contemplating breaches of fundamental terms and such clauses do not apply to relieve a party from the consequences of such a breach even where the contract continues in force."[43] This result has been reached by a "robust use," in Lord Upjohn's phrase,[44] of a well known canon of construction about construing wide words so as to give business efficacy to a contract, on the footing that both parties are intending to carry out the contract fundamentally. But it must be pointed out: first, a presumption only is involved, not a dogmatic rule of law applicable despite the circumstances: secondly, the approach of Lord Upjohn, unlike that of the previously considered members of the House, suggests that there is a big difference between fundamental breach and breach of fundamental term, so far as the effects of a limitation or exclusion clause are concerned. If this is correct, then it would be of vital importance to be able to tell which of the two is involved.

Lord Wilberforce does not touch upon the notion of breach of fundamental term. For him, what is relevant is the idea of "fundamental breach" or, which is presumably the same thing, as he says, "a breach going 'to the root of the contract'."[45] He does distinguish, however, between (i) totally different performance from what is contemplated in the contract and (ii) breach of contract that is more serious than a breach entitling the other party to damages, in fact entitling the other party to refuse performance or further performance. These two meanings of 'fundamental breach' gave rise to two separate questions. Only the first related to exception or exclusion clauses, viz., whether such a clause applied as regards a particular breach. The second meaning gave rise to the question whether the other party was entitled to elect to refuse further performance. These meanings, and the issues to which they gave rise, were not to be confused.[46] In Lord Wilberforce's words,[47] which merit exact citation:

> There is . . . no necessary coincidence between the two kinds of (so-called fundamental) breach. For, though it may be true generally, if the contract contains a wide exceptions clause, that a breach sufficiently serious to take the case outside that clause will also give the other party the right to refuse further performance, it is not the case, necessarily that a breach of the latter character has the former consequence. An act which, apart from the exceptions clause, might be a breach sufficiently serious to justify refusal of further performance, may be reduced in effect, or not made a breach at all, by the terms of the clause.

This last sentence seems to be stating the same kind of approach as was put forward by the New Zealand writer Coote, and accepted by Windeyer, J., in the recent Australian case. But Lord Wilberforce's language, after this passage, seems to turn away from such a conclusion and return to the idea that it is a question of construction whether the parties have effectively ousted liability for the breach that actually occurred. What he says[48] is that the parties cannot have contemplated in a contract that an exceptions clause should have so wide an ambit as in effect to deprive one party's stipulations of all contractual force. To do so would reduce the contract to a mere declaration of intent. To such extent there may be a rule of law against the application of an

[43] *Id.*, at 89.
[44] *Ibid.*
[45] *Id.*, at 91.
[46] *Ibid.*
[47] *Id.*, at 91-92.
[48] *Id.*, at 92.

exceptions clause to a particular type of breach. But, short of this, "it must be a question of contractual intention whether a particular breach is covered or not, and the courts are entitled to insist . . . that the more radical the breach the clearer must the language be if it is to be covered." The conception of "fundamental breach" as one which, through ascertainment of the parties' contractual intention, falls outside an exceptions clause is well recognized and comprehensible. It need not be extended. Such contractual intention is to be ascertained not just grammatically from words used, but "by consideration of those words in relation to commercial purpose (or other purpose according to the type of contract)." This is flexible enough.

Flexible enough for what? To permit a court to refuse to apply an exclusion clause to a flagrant departure from the contract purpose or intent? To permit the parties to oust all kind of liability completely by an appropriate choice of words? To render all that was said by the House of Lords in this case unnecessary and meaningless? To make it unnecessary to differentiate different classes of exclusion clauses, or to suggest it is advisable to distinguish fundamental breach from breach of fundamental term?

Mention of the uncertainties of this passage inevitably lead on to the general impression of indecision and indefiniteness left upon the mind of any reader of these speeches. One commentator[49] legitimately and reasonably points out, first, that none of the cases in which the suggested substantive doctrine relating to exclusion clauses was applied has been overruled: secondly, that the process of construction set out in the House leaves a considerable discretion to the courts: and thirdly that there might still be some continued existence of the substantive doctrine. The conclusion of the writer in question was that "the new approach to the problem of fundamental breach has not greatly reduced the area of judicial discretion though it may affect the direction of its exercise."[50] As another writer put it: ". . . it may be doubted whether this decision will materially affect the outcome of such cases" (i.e. cases in which a contract contains an exclusion or exemption clause) "in the future. . . . The rules of construction set out in the judgments of the House are a powerful weapon in the hands of a court determined to do justice. . . ."[51] All that would seem to emerge from a study of the speeches in this case is that a more flexible approach must be adopted in the future by courts faced with the kind of exclusion or exception clause which was included in the contracts in the cases examined earlier in this article. At the same time the speeches indicate what Windeyer, J., explained the case settled, in the Australian decision referred to above,[52] namely "that there is no doctrine that every exemption clause, however widely expressed, is nullified by a 'fundamental breach'." A question involving such clauses must be "resolved by construing the language that the parties used, read in its context and with any necessary implications based upon their presumed intention. It is not to be resolved by putting exemption clauses into a position of peculiar vulnerability."

Having said that, however, Windeyer, J., proceeded to stipulate cer-

49 Treitel (1966), 29 Mod. L. Rev. 546, 551-553.
50 *Id.*, at 553: Cp. 556.
51 Thompson, [1966] J.B.L. 210.
52 *Supra*, n. 34, at 376.

tain established rules of law which perhaps provide a more satisfactory basis for dealing with situations and contracts of this kind than the approach engendered by the conflicting, uncertain, and indecisive language of the House of Lords. Apart from the doctrine of strict construction, and the rule that language must be clearly capable of covering the alleged exonerated conduct, the central proposition is this: ". . . a condition absolving a party from liability . . . is construed as referring only to a loss which occurs when the party is dealing with the goods in a way that can be regarded as an intended performance of his contractual obligation. He is not relieved of liability if, having obtained possession of the goods, he deals with them in a way that is quite alien to his contract."[53]

On this some comments must be made. First of all, Windeyer, J., was speaking particularly of a bailment situation, as arose in the case in question. Secondly, he was not speaking with the majority of the court. Thirdly, the rule he was expressing, viz., the "four corners rule," as expounded and explained by him, is not exactly what the House of Lords would seem to have had in mind in their lordships' discussion of fundamental breach and breach of fundamental term in the *Suisse Atlantique* case, even though Lord Hodson expressly[54] and Lords Upjohn[55] and Wilberforce[56] by implication from their references to the *Gibaud* case used this doctrine to illustrate the way the cases had developed. Despite the hint in Lord Wilberforce's speech, the division suggested prior to the *Suisse Atlantique* case between different classes of exclusion or limitation clauses does not seem to have been basic to the view taken by the House, whereas the language Windeyer, J., seems to indicate his acceptance of such division as helpful in the assessment of the meaning, value and effect of such clauses.

To Windeyer, J., such clauses may well serve to define the content of a party's obligations under the contract, so as to establish the circumstances in which he will be liable. The speeches in the House of Lords, on the other hand, seem to be directed towards regulating the weight that is to be given to such clauses from the point of view of determining a party"s liability for an undoubted breach of his contract. Although both approaches appear to involve construction of contract rather than the application of substantive, normative, obligatory rules of law, they differ in respect of the ends which such construction is intended to achieve.

There is another important difference which a consideration of these cases suggests. The doctrine as expounded by Windeyer, J., leaves much greater freedom to the parties to define and delimit the scope and extent of their contractual obligations. The 'flexible' approach of the House of Lords, while purporting to be founded firmly on the notion of upholding freedom of contract, and non-interference by the courts, is capable of being applied in such a manner as to permit the courts to exercise very great control over the scope of a contract, its performance, and the question of liability for its breach. While there is still much room for argument about the final effects of this case, it may be suggested with some confidence that the nature and content of the speeches

[53] *Id.*, at 3.
[54] *Supra*, n. 3, at 80.
[55] *Id.*, at 87.
[56] *Id.*, at 93.

in the House of Lords will not materially interfere with the exercise by courts of some kind of jurisdiction to 'strike down,' if it may be put thus, exemption or exclusion clauses which seem too widely drawn and too stringent in their consequences as respect an innocent party. If this is a valid conclusion, then it may be said that the *Suisse Atlantique* case, ironically enough, is authority for the very proposition which their lordships purported to deny, namely, that parties are not completely free to make whatever contractual arrangements they wish: that, on the contrary, the courts may still intervene in appropriate situations and regulate the mutual rights and liabilities of the parties, despite the attempt to oust the power and jurisdiction of the court. This, it may be suggested, is by no means a bad result. Otherwise it might follow that agreements which were expressed as contracts, had the appearance of contracts, and, in a sense, were meant to be contracts, would have to be contrued by the courts as not contracts at all, merely 'honourable' bargains, incapable of any legal enforcement, and unproductive of any legal remedy in the event of some alleged grievance. To welcome, rather than deplore, this interpretation of the *Suisse Atlantique* case is not to support judicial interference with contract at the expense of the parties' freedom. It is to recognize that only in this way can freedom of contract properly attain fulfillment. There is clearly a difference between freedom and utter irresponsibility. A proper judicial understanding and treatment of exclusion clauses can help to define and demarcate the boundaries of such freedom.