



# 2

part two

## Contract law

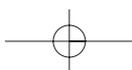
CHAPTER 7: Contract law 1 187

CHAPTER 8: Contract law 2 2

CHAPTER 9: Contract law 3 2

CHAPTER 10: Property law: Mortgages, leases and licences 2

CHAPTER 11: Insurance law 2





# Contract law 1

## Learning objectives

At the end of this chapter you should be able to:

- describe how contracts can be classified
- define contracts according to:
  - validity
  - performance
  - formation
- distinguish formal contracts from simple contracts
- identify the six essential elements required to make a valid contract
- explain how the law determines whether parties to a contract intend to create a legal relationship
- define the term 'offer' and distinguish it from an 'invitation to treat'
- list the rules with respect to offer and acceptance
- explain the rules for offer and acceptance for contracts made by post
- define 'consideration' and state the consequence for a contract lacking consideration
- explain how a contract that lacks consideration can be enforceable if placed in a particular form
- list the rules regarding consideration
- describe the requirements of contracts required to be in writing and of contracts required to be evidenced in writing.

## Summary of contents

This chapter will cover:

- classification of contracts
- sources of contract law
- essential elements required to make a valid contract
- intention to create a legal relationship
  - social and domestic agreements
  - business agreements
- offer and acceptance
- rules with respect to offers
- rules with respect to acceptance
- form and/or consideration
- rules with respect to consideration
- contracts required to be in writing and contracts required to be evidenced in writing.





## Introduction

An understanding of the law of contract is of fundamental importance in the context of business practices. A 'contract' is defined by Trietel in his work *The Law of Contract* (9th edn, Sweet & Maxwell, London, 1995) as 'an agreement giving rise to obligations that are enforced or recognised by the law'. Both the common law and statutory laws have application to contracts.

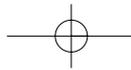
In the next three chapters we will examine the main principles governing contractual relations. We will consider the main elements of a contract, the classification of contracts, and the methods by which they can be discharged and breached. We will also examine the remedies available to a party who has suffered because of a breach of contract.

The following terms are used throughout this chapter:

<b>acceptance</b>	the act of assenting to an offer: an essential element in the formation of a contract
<b>consideration</b>	mutual rights and promises made by the parties to a contract
<b>contract</b>	an agreement between two or more persons that is legally enforceable
<b>counter offer</b>	the rejection of an offer by the putting of an alternative offer
<b>deed</b>	a type of formal contract that requires no consideration
<b>formal contract</b>	a contract not requiring consideration
<b>gratuitous promise</b>	a promise not supported by consideration
<b>illegal contract</b>	a contract where the purpose or the object of the contract is illegal
<b>invitation to treat</b>	an invitation to a person to make an offer
<b>offer</b>	a proposal made by a person to another to enter a legally binding contract
<b>offeree</b>	a person to whom an offer is made
<b>offeror</b>	the person who makes an offer
<b>promisee</b>	the person to whom a promise is made
<b>promisor</b>	the person who makes a promise
<b>simple contract</b>	all those contracts that are not formal contracts
<b>unenforceable contract</b>	a contract that is not able to be enforced
<b>void contract</b>	a contract of no legal effect
<b>voidable contract</b>	a contract that one party is entitled to rescind

## Key terminology





## CLASSIFICATION OF CONTRACTS

Contracts may be classified according to validity, performance and formation.

### Validity

Not all contracts  
need be in writing

Contracts can be classified according to their validity into several categories, which are illustrated in Table 7.1. Very few contracts are required to be in writing, or to be evidenced in writing, in order to be valid. In the latter part of this chapter, we will look at these contracts. Apart from this very small group, contracts made verbally will be valid and enforceable by the law. Obviously, it will be easier to prove the existence and terms of a written contract. Problems will arise when seeking to enforce a verbal contract. It will be necessary to decide which party is telling the truth. For these reasons, it is **recommended** that contracts should be placed in **writing**.

**TABLE 7.1** Classification based upon validity

Type of contract	Enforceability
Valid contract	Enforceable by either party
Void contract	Not enforceable
Voidable contract	Able to be avoided (rescinded) by innocent party
Unenforceable contract	Not enforceable
Illegal contract	Not enforceable

A **valid** contract is a contract in which all elements are present and that is enforceable by law. A **void contract** is one that is of no legal effect. A contract falling into this category cannot be enforced by a party to the contract. A contract is void where, for example, the consideration for the contract is immoral or where a party enters a contract under a mistaken belief—although only certain instances of mistaken belief will make a contract void. They will be discussed in more detail in the next chapter.

One party may  
rescind the contract

A **voidable contract** is a contract that one of the parties is entitled to rescind (i.e. not be bound by the contract). This right is usually given to the injured party. Examples of voidable contracts are those entered into as a result of misrepresentation, duress or undue influence.

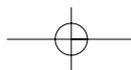
An **unenforceable contract** is one in which all the essential elements are present, but a technicality may make it impossible for the contract to be enforced. For example, a contract for the assignment of copyright has to be in writing (*Copyright Act 1968* (Cwlth)). If the assignment is not in writing, the contract will be unenforceable.

Illegal object or purpose

An **illegal contract** is one in which the purpose or object of the contract is illegal, pursuant either to common law or statute. Contracts that are in restraint of trade are illegal at common law unless reasonable. An example of a contract illegal by statute would be one that involved a restrictive trade practice. For example, price fixing between a wholesaler and a retailer is prohibited by the *Trade Practices Act 1974* (Cwlth).

### Performance

Another way of classifying a contract is according to performance. A contract can be either executed or executory. An executed contract is a contract where one party to the contract has performed its side of the bargain.



## Building on a contract

**A formal, written contract may be your only recourse if your contractor fails to match your home-improvement dreams with reality, writes JANE-ANNE LEE.**

Having your bathroom painted? Tiled? Totally refurbished? Does the cost of labour exceed \$200? If your home or investment property is in NSW, then you are required by law to have a written contract which is designed to diminish disputes between consumers, builders and contractors.

In Victoria, contracts are necessary for work costing more than \$5,000. In Queensland, they are recommended and come in two varieties—one for work less than \$25,000 and another for more than \$25,000. Western Australia requires formal contracts for all work. In South Australia, indemnity insurance and formal contracts are required for work exceeding \$5,000. The ACT does not require formal contracts. And in the Northern Territory and Tasmania, licensing or registration of builders is not a statutory requirement.

The NSW Department of Fair Trading is the first of the States to trailblaze “plain-English” contracts. Launched in May this year, they comprise four contracts: minor works for jobs less than \$5,000; renovation for work costing between \$5,000 and \$25,000; home building for new homes and additions worth more than \$25,000; and swimming pools.

They were designed for use in NSW but could be adapted for use in other States.

By using one of the relevant contracts for that new kitchen, extension or paint job, you have some recourse if it is not up to scratch. Contracts are also available from the Master Builders Association, Home Industry Association, Royal Australian Institute of Architects and Standards Australia.

The Jamesons, of the Melbourne suburb of Brighton, were glad they had taken out a written contract with a builder for their new double garage (even though the job fell under the \$5,000 requisite). Much of the cosmetic work was incomplete so they withheld \$3,000. The builder had no recourse because everything was detailed in the contract.

Oral contracts, on the other hand, can be disastrous. Take the Pavey and Matthews v. Paul case, where a builder and his client had an oral contract. The builder sued his client for \$26,945.50 “for work done and materials provided”. The High Court found that the builder was entitled to the payment as the clients had the benefit of the work.

But not all oral contracts result in a victory for the builder. One couple walked and talked their builder through what they wanted, right down to saying “please put the bathroom here”. No plans were drawn up. Unfortunately, the workmanship was poor. Because the contract was oral, the owners had trouble rectifying the

problems as there was no evidence as to what had been agreed.

The matter went before the NSW Building Disputes Tribunal, which found in favour of the owner.

The tribunal, which deals with about 3,000 cases a year, can hear matters only where orders sought are for less than \$25,000. If the claim is more than \$25,000, the Commercial Tribunal will hear any appeals.

Some of the most common building disputes involve variations to plans—for example, the owners asking the sub-contractor (maybe an electrician) to alter something. In many instances the builder only finds out when he gets a bill from the sub-contractor and then has to charge the client extra.

The NSW contracts are part of reforms to the home-building industry that have resulted in the new Home Building Act. NSW Minister for Fair Trading, Faye Lo Po, says that with consumers in the State spending more than \$7 billion on new dwellings and renovations, the changes to home-building laws will create incentives for better standards of work, and make it harder for sub-standard builders to operate in NSW.

*Source: The Australian Financial Review, 22 August 1997, p. 7, Smart Money Section.*

### Newspaper discussion questions

1. According to the article, what is the benefit of having a written contract?
2. Briefly outline the differences between each State and Territory with respect to contracts between builders and consumers.
3. Explain what makes the NSW Department of Fair Trading unique in Australia.
4. What are the advantages and disadvantages of oral contracts?
5. Identify some of the most common building disputes referred to in the article.
6. Why did NSW adopt relatively tough measures with respect to contracts between builders, consumers and contractors?

### LAW IN ACTION

Tom agrees to sell a book to Nigel for \$15. If Tom delivers the book to Nigel’s home, the contract is said to be executed. Tom has done all he is obliged to do pursuant to the agreement. All that must be done is for Nigel to pay the \$15.





Both parties yet to perform  
contractual obligations

An **executory contract** is one in which both parties to the contract have obligations still to be performed. In the above 'Law in action', if Tom had not delivered the kit, the contract would be executory. Tom would be required to deliver and Nigel would be required to pay the purchase price.

## Formation

This method of classification depends on the way in which a contract is formed. Contrary to what many people think, a contract can exist in the absence of a written agreement. Contracts can be formed expressly or impliedly, or independently of the wishes of the parties by operation of law.

**TABLE 7.2** Formation of contracts

Type of contract	Method of formation
Express contracts	Written or spoken words
Implied contracts	Conduct or actions of parties
Quasi-contracts	By operation of law

### EXPRESS CONTRACTS

Written or spoken

Contracts formed expressly are created by express words, either written or spoken. For example, a contract for the sale of a house for \$300 000 is created by a standard form written contract. An example of an express verbal agreement would be an agreement made by Sandra to paint Peter's portrait for \$750.

### IMPLIED CONTRACTS

Conduct of parties

A contract created impliedly is created not by words, either written or spoken, but by the conduct or actions of the parties. The conduct of the parties leads to the implication that there is a contract.



### EXAMPLE

Suzanne selects a magazine in a newsagency, takes it to the counter and gives the seller money to buy the magazine. Even though no words are spoken, a contract is created impliedly by Suzanne's actions in tendering payment and the acceptance of the payment by the seller.



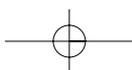
### EXAMPLE

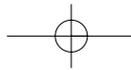
Monica hails a taxi on a street corner. By this act, the law implies that Monica will pay the fare and that the taxi driver will take her to her destination.

### QUASI-CONTRACTS

Contracts may be created by  
operation of law

A third way of creating a contract is to create it independently of the wishes of the parties, by operation of law. The term used for such contracts is **quasi-contracts**. The term 'quasi-contract' refers to the remedy provided by the common law that compels payment of money from one person to another when justice requires. For example, where money has been paid by a person under duress, quasi-contract will allow the person who has paid the money under duress to recover it.



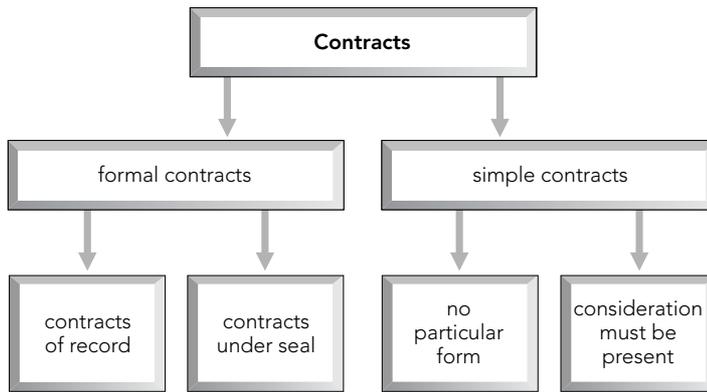


**FORMAL CONTRACTS AND SIMPLE CONTRACTS**

Contracts can also be classified into simple and formal contracts. **Formal contracts** can be further divided into two broad categories: **contracts of record** and **contracts under seal (deeds)**.

Consideration not always required

Formal contracts must be in a particular form but do not have to possess consideration. They are enforceable because of their form. **Simple contracts** are all those contracts that are not formal contracts. They are not required to be in any particular form but are required to have consideration. As the name suggests, simple contracts require few formalities. There is a more detailed discussion of the distinction between formal and simple contracts later in this chapter (see p. xxx). Figure 7.1 illustrates the key differences between formal and simple contracts.



**FIGURE 7.1** Formal and simple contracts

One significant difference between the two forms of contract relates to the rights of enforcement if a contract should be breached. Under a formal contract, contractual rights are enforceable for a longer period of time than is the case for simple contracts. Table 7.3 sets out the respective periods of time imposed by statutes of limitations in each State and Territory.

Rights of enforcement

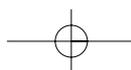
We will discuss the issue of consideration and the distinction between formal and simple contracts in more detail later in this chapter.

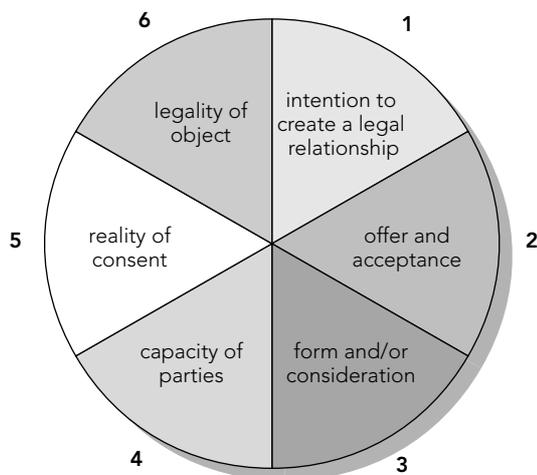
State/Territory	Simple contract (yrs)	Formal contract (yrs)
New South Wales	6	12
Victoria	6	15
Queensland	6	12
South Australia	6	15
Western Australia	6	20
Tasmania	6	12
Australian Capital Territory	6	12
Northern Territory	3	12

**SOURCES OF CONTRACT LAW**

Contract law has its sources in both common law and statute. The rules with respect to the essential elements of a contract are predominantly common-law based, but some have been modified by statute. For example, there are numerous statutes protecting consumers. The majority

Most contract law is common-law based





**FIGURE 7.2** Six elements of a contract

of these are State rather than federal statutes, because the Federal Constitution restricts the law-making power of the Federal Parliament to certain matters. One important piece of legislation that will be discussed at some length in later chapters is the *Trade Practices Act 1974*.

## ESSENTIAL ELEMENTS REQUIRED TO FORM A CONTRACT

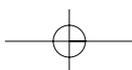
Before the law will regard an agreement as a contract, a number of essential elements must exist. Figure 7.2 illustrates the six elements required to constitute a contract.

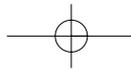
Contract comprises  
six elements

1. *Intention to create a legal relationship*. The parties to the contract must intend their agreement to be legally enforceable.
2. *Offer and acceptance*. There must be a meeting of minds. There must be an offer made by one party and an acceptance of that offer by another.
3. *Form and/or consideration*. Consideration can be defined as a mutual promise. Both parties must provide consideration. A contract lacking consideration may be valid if it is in the form of a deed (i.e. a contract under seal).
4. *Capacity of parties*. The parties to a contract require capacity or ability to contract. Some people are under a disability when it comes to making contracts (e.g. minors); their capacity to contract is restricted.
5. *Reality of consent*. It is necessary that the parties to a contract genuinely consent to the making of a contract. Their consent must be genuine and not given because of misrepresentation, duress or undue influence.
6. *Legality of object*. The purpose or object of a contract must be legal. Contracts can be illegal at common law and by statute.

An easy way to remember the six elements of a contract is to remember the word FROLIC:

<b>F</b>	form and/or consideration
<b>R</b>	reality of consent
<b>O</b>	offer and acceptance
<b>L</b>	legality of object
<b>I</b>	intention to create a legal relationship
<b>C</b>	capacity of parties





We will now consider three of the elements in some detail (the other three elements will be discussed in Chapter 8).

### Intention to create a legal relationship

Not all agreements give rise to legally enforceable obligations. People who make agreements must intend that the agreement made will give rise to a legally enforceable obligation. Figure 7.3 illustrates the factors relevant to this element.

Not all agreements are contracts

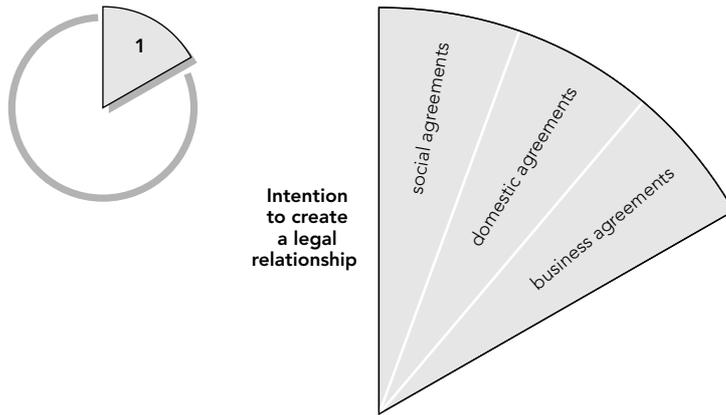


FIGURE 7.3 Types of agreement that may determine if the intention element exists

To determine whether there is an intention to create legal relations, the law looks at the **nature** of the agreement. If an agreement is of a **social** or **domestic** nature, the law has created a presumption that such agreements do not have an intention to create legal relations. A **presumption** is a conclusion or inference about the truth of some fact.

Domestic agreements are presumed not to have intention to create legal relations

#### SOCIAL AND DOMESTIC AGREEMENTS

Social agreements are made between friends. A domestic agreement is one made between members of the same family or household.

#### EXAMPLE

Two friends agree to play tennis next Saturday. If one person fails to arrive at the agreed time, the law presumes that the agreement was not intended to create legal relations. The person who breached the agreement could not be sued for breach of contract.



#### EXAMPLE

A husband agrees to cook dinner for his wife and, in return, she will do the dishes. The husband fails to cook the dinner. The law presumes that this type of agreement is not intended to create legal relations.

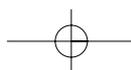


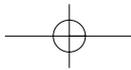
The reason for the existence of this presumption is simple and sensible. The courts would be flooded with litigants if every social or domestic agreement gave rise to a legally enforceable obligation.

#### CASE EXAMPLE

*Balfour v. Balfour* [1919] 2 KB 571

**Facts:** The defendant was a civil servant working in Ceylon. When he was home on leave in England, it was agreed that his wife would not return to Ceylon with him, due to her poor health.





The husband promised to pay his wife £30 per month as maintenance while he was in Ceylon. The defendant breached this agreement and his wife sued him, alleging breach of contract.

**Decision:** The action was unsuccessful. The court held that the agreement was not a contract. This was because there was no intention to create legal relations. Aitkin LJ, in his judgment at 578, explained why this element was missing:

It is quite common, and it is the natural and inevitable result of the relationship of husband and wife, that the two spouses should make arrangements between themselves ... Nevertheless they are not contracts, and they are not contracts because the parties did not intend that they should be attended by legal consequences ... They are not sued upon, not because the parties are reluctant to enforce their legal rights when the agreement is broken, but because the parties, in the inception of the arrangement, never intended that they should be sued upon. Agreements such as these are outside the realm of contracts altogether.

Rebutting the presumption

The presumption can be rebutted or negated by producing evidence that there is a business or commercial flavour to the agreement, even though it is made between family members or friends.

We will now consider some examples where the presumption has been successfully rebutted. The first case deals with a married, although separated, couple, and the following cases deal with agreements between family members.



### CASE EXAMPLE

*McGregor v. McGregor* (1888) 21 QBD 424

**Facts:** A husband and wife had taken out summonses against one another for assault. Before the summonses were heard, the parties agreed to withdraw them and to live apart. The husband agreed to pay the wife an amount each week for maintenance, and the wife agreed to support herself and her children and to indemnify the husband against any debts contracted. The payments fell into arrears and the wife sued the husband for breach of contract.

**Decision:** Mrs McGregor succeeded in her action. The court said that the parties' agreement had intention to create legal relations. It was not an agreement covering the day-to-day arrangements of the marriage but rather an agreement, reached in compromise, of a legal action, and an agreement made to facilitate separation of the parties.



### CASE EXAMPLE

*Todd v. Nicol* [1957] SASR 72

**Facts:** The plaintiffs were the sister and the niece of the defendant's husband. The husband had died prior to the agreement in question being made. Mrs Nicol lived in Adelaide and proposed that the plaintiffs, who lived in Scotland, should join her. She promised that if they came to Adelaide she would change her will so that her house would be given to her sister-in-law and niece, provided that the niece did not marry. Expenses were incurred in the plaintiffs' moving to Adelaide, and the defendant broke her agreement. The plaintiffs sued her for breach of contract.

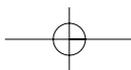
**Decision:** The South Australian Supreme Court held that the parties had made a binding contract, notwithstanding that the arrangement was between family members. Several factors led the court to the conclusion that this was not simply a domestic arrangement but had more of a business flavour. The selling of belongings by the plaintiffs and the expenses incurred to move permanently to Adelaide were factors considered to be important by the court.



### CASE EXAMPLE

*Wakeling v. Ripley* (1951) 51 SR (NSW) 183

**Facts:** Ripley was a bachelor who lived in Sydney. The plaintiffs were Ripley's sister and her husband who was a lecturer at Cambridge University in England. Ripley wrote to his sister



in 1946 to try to convince her to move to Australia. He promised to give the plaintiffs a home and a living if they moved. He also promised to leave all his property to his sister on his death. The plaintiffs agreed. They sold their house and the husband resigned his lectureship. After a year of living together, the parties argued and the defendant reneged on his promise to leave his property to his sister. He sold his house and disinherited the plaintiffs. The plaintiffs sued for breach of contract.

**Decision:** When the court heard the matter for the first time, it said there had been a breach of contract. The defendant appealed, alleging there had been no intention to create legal relations. The court found again in favour of the plaintiffs, deciding that there was a contract. The court said that the agreement had intention to create legal relations despite the fact it was made between family members. Factors considered relevant in coming to that decision were that one of the plaintiffs had left his job and that the plaintiffs had moved to another country.

Contract between family members

## BUSINESS AGREEMENTS

Agreements of a business or commercial nature are treated differently from social or domestic agreements by the law. Business or commercial agreements raise a presumption that there is an intention to create legal relations. Again, this presumption can be rebutted if evidence is produced to show that there was clearly no intention to create a legally binding agreement.

Presumption relating to business agreements

If an agreement is made in the course of business dealings, then in the absence of express words to the contrary, the courts will say that legal relations were intended. This presumption can be rebutted by evidence showing that no intention was envisaged.

Express words to the contrary will rebut the presumption

## CASE EXAMPLE

*Edwards v. Skyways* [1964] 1 WLR 349

**Facts:** During an industrial dispute, an airline company agreed with the British Airline Pilots Association to make an *ex gratia* payment of a specific amount to redundant pilots. When a redundant pilot sued to recover the payment from the company, the company said that they were not obliged to pay on the grounds that no legal relations were intended by the agreement.

**Decision:** There was an enforceable contract between the parties, and the pilot was entitled to recover the payment. The presumption that business agreements intend to create legal relations was not rebutted in this case.



## CASE EXAMPLE

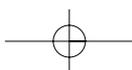
*Rose and Frank Co. v. Crompton and Bros Ltd* [1923] 2 KB 261

**Facts:** A clause in a contract made between the plaintiff and the defendant stated that there was no intention to create a legally binding arrangement. The words used were:

This arrangement is not entered into, nor is this memorandum written as a formal or legal agreement ... but is only a definite expression and record of the purpose and intention of the three parties ... to which they each honourably pledge themselves ... that it will be carried through ... with mutual loyalty and friendly co-operation.

**Decision:** The statement above was considered by the court to indicate the intention of the parties. It was sufficient to rebut the presumption that there was intention to create legal relations.

The presumption was also successfully rebutted in the following case.





## CASE EXAMPLE

*ABC v. XIVth Commonwealth Games Ltd* (1988) 18 NWSLR 540

**Facts:** It was agreed that the ABC should be given the broadcasting rights to the Commonwealth Games. The price was agreed upon, including the amount of the first instalment. A number of matters had not been agreed upon, including sub-licences, radio and television signals and the right to release cassettes.

Draft contracts were exchanged by the parties but before the contracts were signed a higher offer was submitted by a third party. The Commonwealth Games argued it could take up this offer as it did not have a contract with the ABC.

**Decision:** The court said there was no contract between the parties as there was no intention to be immediately bound contractually. No agreement had yet been reached on a number of important issues. The court held the parties were still negotiating a contract.

Clauses like these are often included in the conditions of entry of competitions. The following case illustrates this point.



## CASE EXAMPLE

*Jones v. Vernon Pools Ltd* [1938] 2 All ER 626

**Facts:** The plaintiff sued to recover money on a football pools coupon that he alleged he had posted and the defendants had lost. A clause on the pools coupon was relied upon by the defendant to deny liability. The clause said:

... and this coupon and any agreement or transaction ... shall not ... give rise to any legal relationship ... or be legally enforceable ... but all such arrangements, agreements and transactions are binding in honour only.

**Decision:** The insertion of this clause meant that the agreement was not intended to give rise to a legally binding contract. The plaintiff therefore could not sue for breach of contract.



## CASE EXAMPLE

*Sindel v. Georgiou* (1984) 154 CLR 661

**Facts:** The parties entered into a contract for the sale of land. The vendor later sought to avoid specific performance of the contract on the grounds that the documents exchanged with the purchaser, which purported to evidence the agreement, were not identical.

**Decision:** The agreement bound the parties. Although the documents signed by each party were not identical in terms, the intention of the parties was the paramount consideration. The High Court of Australia found that the parties had agreed on terms and exchanged signed documents. This was an indication that the parties intended to create a binding agreement. The differences between the two documents were rectifiable and therefore the vendor and purchaser were bound by the terms of the contract.

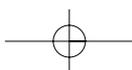
## Check your progress 7.1

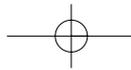


Interactive version at  
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Place a tick in the appropriate box.

1. Contracts may be classified according to:
  - (a) offer, acceptance and performance
  - (b) formation, validity and performance
  - (c) agreement, intention and consideration
2. A contract that one of the parties is entitled to rescind is:
  - (a) an illegal contract
  - (b) an unenforceable contract
  - (c) a voidable contract





3. The two major categories of formal contracts are:
  - (a) contracts of record and contracts under seal
  - (b) contracts under seal and contracts requiring consideration
  - (c) contracts of record and contracts of service
4. The major source of contract law is:
  - (a) UK statute law
  - (b) common law
  - (c) Australian and UK statute law
5. Agreements classified as 'social' or 'domestic' are presumed:
  - (a) not to intend to create legal relations
  - (b) to intend to create legal relations
  - (c) to be enforceable if they are made expressly
6. Business or commercial agreements:
  - (a) raise a presumption that the parties intend to create legal relations
  - (b) raise an irrebuttable presumption that legal relations are intended
  - (c) have the same legal status as social or domestic agreements

### Offer and acceptance

The second element required to create a valid contract is an offer and an acceptance of the offer. An offer is a **proposal**. When it is accepted, it creates a legally binding agreement—a contract. Figure 7.4 illustrates the relationship between the offeror and the offeree, and Figure 7.5 illustrates the factors relevant to this element.

What is an offer?



FIGURE 7.4 A contractual relationship

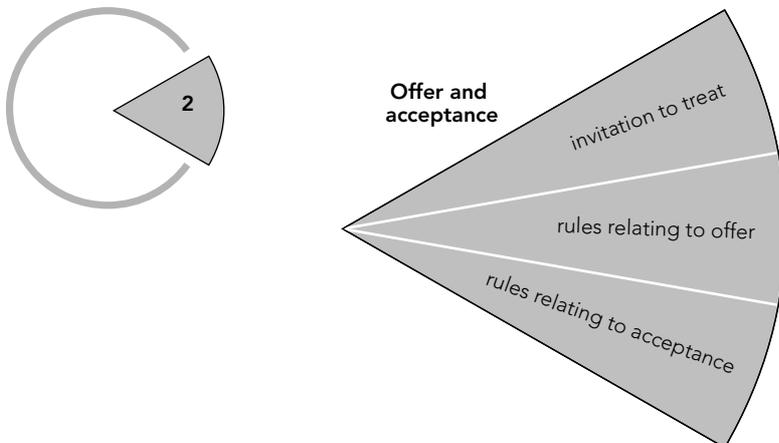
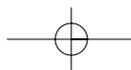
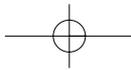


FIGURE 7.5 Factors relevant to offer and acceptance element





Invitation to treat  
distinguished from offer

## INVITATION TO TREAT

An 'offer' must be distinguished from an 'invitation to treat'. An invitation to treat invites people to make offers. The main difference between an offer and an invitation to treat is that a person making an offer intends to be bound, whereas a person making an invitation to treat does not intend to be bound. An item that appears in a shop window with a price tag on it is an invitation to treat. For example, a pair of trousers with a price tag of \$75 (or an item in an advertising catalogue) is regarded by the law not as an offer but as an invitation to treat. This is an invitation for persons interested in buying the article to make an offer to purchase. In the above example, if a person takes the trousers to a counter in order to purchase them, then that person is making an offer to purchase. The offer can be either accepted or rejected by the seller.

In *Pharmaceutical Society of Great Britain v. Boots Cash Chemists (Southern) Ltd* [1952] 2 QB 795, Lord Goddard CJ, at 802, made the following comment regarding whether an item in a shop was an offer:

I am quite satisfied it would be wrong to say that the shopkeeper is making an offer to sell every article in the shop to any person who might come in and that that person can insist on buying any article by saying 'I accept your offer' ... There is no contract by the shopkeeper to sell until the customer has taken the book to the shopkeeper or his assistant and said 'I want this book' and the shopkeeper says 'yes'.

Today, goods on display in a shop still constitute an invitation to treat. Sophisticated retailing has not changed this principle.



## EXAMPLE

In the sale bin at Harrads Department Store, Michael discovers a pair of shoes that are cheaper than elsewhere in the store. Upon presenting the shoes at the counter the sales attendant discovers that the wrong price tag has been placed on the item. Harrads Department Store can refuse to sell the shoes because Michael is simply making an offer. Harrads are entitled to reject the offer on discovering the mistake on the price tag. No contract is formed in the absence of acceptance.

Advertisements usually  
invitations to treat

Advertisements are usually regarded as invitations to treat, whether they appear in a newspaper or a catalogue. In some cases, however, an advertisement can be an offer if that is the intention of the person advertising. This point is illustrated well by the case of *Carlill v. Carbolic Smoke Ball Co.*, discussed on pp. xxx and xxx.

## Circulars

If a circular contains a request for a person to send money it may be regarded as an offer, as illustrated by the following case example.



## CASE EXAMPLE

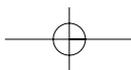
*re Mount Tomah Blue Metals* (1963) 4 FLR 478

**Facts:** A circular requested shareholders in a company to subscribe money for conduct of the company's business and the discharge of its liabilities.

**Decision:** The court held that this was a request that would result in the performance of an act—the act being acceptance by shareholders. Therefore, it was an offer and not an invitation to treat. The company was requesting a loan and offering debentures to those who sent money to the company.

## Auctions

When an auctioneer calls for bids at an auction, this is only an invitation to treat. He or she is inviting those present at the auction to make an offer. A bid is regarded as an offer. It is



then up to the auctioneer to either accept or reject that bid. When there is no reserve price, the auctioneer will accept the highest bid and, once the hammer has fallen, a contract has been made.

### Tenders

An advertisement for tenders (see Figure 7.6) is usually considered to be an invitation to treat. Any tender received following the advertisement will amount to to be an offer. A binding contractual obligation may arise if the invitation to tender specifies the exact needs of the person placing the tender and their tender is then accepted by the person who invited tenders to be submitted.

Tenders usually invitations to treat

**SOUTH AUSTRALIA**

**Department for Administrative and Information Services**  
Supply SA

**Sale Tenders**

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**CLOSING MONDAY 3 JANUARY 2000**

**S42/98** – Purchase, dismantle and remove Atco hut building No 7, 10x3M, Demac building 16x19M. Inspect by arrangement with Officer in Charge, West Beach Railway Station, tel (08) 8226 9999, Monday to Friday, 9am to 4pm. AH John Citizen 0418 8226 9999.

**Closing date: 5:00pm Monday 3 January 2000**

**Tender documents are available from:**

Supply SA, Level 12, 30 Wakefield Street,  
ADELAIDE SA 5000  
Telephone (08) 8226 9999  
Facsimile (08) 8226 9999

**FIGURE 7.6** Example of an advertisement calling for tenders

### Standing offers

Sometimes tenders are called for in respect of the supply of goods or material that may or may not be required. If a tender is submitted to supply goods on an 'if required' basis it is called a 'standing offer'. If orders are placed for the supply of goods they will be regarding as separate contracts for each order made.

### RULES WITH RESPECT TO THE MAKING OF AN OFFER

The following rules apply to the making of an offer:

- An offer is not required to be in any particular form. It can be written, verbal or made by action.
- The person who makes the offer is called the **offeror**; the person to whom the offer is made is the **offeree**.
- An offer can be made to one or more persons, even to the whole world.

An offer can be made to one or more people

### EXAMPLE

Ryan may offer to sell his car to Linton for \$7000, or he may offer to sell his car to anyone at the place of his employment.





## CASE EXAMPLE

*Carlill v. Carbolic Smoke Ball Co.* [1893] 1 QB 256

**Facts:** An advertisement was placed in several magazines by the defendant company. The company manufactured a carbolic smoke ball that allegedly prevented the user from contracting influenza or a cold provided it was used as directed. An offer of £100 was made to any reader who contracted a cold or flu after using the smoke ball three times a day for a period of two weeks. This offer was made to any person who read the advertisement. Conceivably, the offer could be made to the whole world if the advertisement were published in magazines throughout the globe.

Cannot accept an offer you are not aware of

An offer must be communicated to the offeree. Therefore a person cannot accept an offer unless they are aware of it.



## LAW IN ACTION

Anton loses his watch in the school yard and places a notice in the school magazine advertising a reward of \$20 to any person who finds it. Catherine (a friend) finds the watch and returns it to Anton without being aware of the reward. Catherine is unable to claim the reward, as the offer of the reward was not communicated to her. The act of returning the watch was not an acceptance of an offer. She cannot accept the offer as she had no knowledge of it.

A person, when accepting, must be doing so in reliance on the offer and not for some other reason.



## CASE EXAMPLE

*R v. Clarke* (1927) 40 CLR 227

**Facts:** A reward of £1000 was offered for information that would lead to the arrest and conviction of the person or persons responsible for the murder of two police officers.

On 6 June, two persons, X and Y, were arrested and charged with the murder of one of the officers. On 10 June, Y gave evidence that led to the conviction of X and another person, Z, for the murder of the officer. Y was released from custody and, on release, he claimed the £1000 reward.

Acceptance must be in reliance of an offer

**Decision:** The court found that Y (whose name was Clarke) had only provided the information to the police in order to escape a charge of murder. Y did not act in reliance of the offer when he gave the information and therefore there could be no acceptance of the offer. The court said that he was not entitled to the reward. Although Clarke had been aware of the reward (the offer) at the time he gave information to the police, he hadn't relied on the offer.

Communication of all terms of an offer required

All the **terms** of the offer must be communicated to the offeree. For example, a condition may be that the offer will only remain open for a specified period. An offer may specify conditions to be followed by the offeree. For example, an offer may specify that acceptance must be made in writing to the offeror.

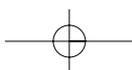
## TERMINATION OF AN OFFER

There are several ways in which an offer can be terminated (see Figure 7.7).

### An offer may be terminated due to:

- lapse of an offer
- revocation of an offer
- rejection of an offer
- death of the offeree or offeror
- non-occurrence of a condition

**FIGURE 7.7** Methods of terminating an offer



### Lapse of an offer

An offer will lapse or disappear if certain events occur:

- if acceptance is not made within the time stated
- where no time is stated, if the acceptance is not made within a **reasonable time**
- if a counter offer is made.

The meaning of a 'reasonable time' will be considered objectively.

### EXAMPLE

If perishable goods are the subject matter of a contract, then a 'reasonable time' will be far less than for goods that are not perishable.

### CASE EXAMPLE

*Ramsgate Victorian Hotel Co. v. Montefiore* (1866) LR 1 Ex 109

**Facts:** The defendant applied for shares in the plaintiff company in June. He heard nothing until November when the company informed him that shares had been allotted and that the balance subscription moneys were due. Montefiore refused to accept the allotment or to pay the money, alleging that his offer to buy had lapsed through expiry of time.

**Decision:** The court said that Montefiore's refusal to accept the allotment was justified. The acceptance of his offer was too late. The delay of five months between offer and acceptance was unreasonable. The court said that if there is no time prescribed within which offers must be accepted, they must be accepted within a reasonable time.

It is permissible for an offeror to say that an offer will remain open for a certain time and then to withdraw the offer before the expiry of that time. This is allowed as long as no acceptance has been made.

If a **counter offer** is made, the original offer will lapse. A counter offer is a rejection of an offer by the putting of an alternative offer.

### EXAMPLE

Paul offers to sell his car to Bob for \$5000. Bob says he will buy it for \$4500. This is a counter offer. The original offer lapses: it is no longer in existence and cannot be accepted.

### CASE EXAMPLE

*Hyde v. Wrench* (1840) 3 Beav 334; 49 ER 132

**Facts:** The defendant offered to sell his estate to the plaintiff for £1000. The plaintiff replied with an offer of £950, which the defendant refused. The plaintiff then agreed to pay the £1000 that was originally asked. The defendant, although he had not withdrawn his offer at this stage, neither assented to nor rejected this proposal, but he subsequently refused to go through with the sale. The plaintiff sued.

**Decision:** The court said that the plaintiff's actions showed that he intended to reject both the defendant's offers and this meant he was no longer able to revive them by changing his mind and making a subsequent acceptance. Once a counter offer is made, the original offer lapses.

If either party loses its contractual capacity, this will also cause an offer to lapse. For example, if a person were declared bankrupt or were to become insane, this could result in that person losing their contractual capacity, thus causing an offer to lapse.

### Revocation of an offer

A general rule is that an offer can be revoked by the offeror at any time before acceptance. There are exceptions to this general rule: if the offer is made in the form of an option or made under seal (in the form of a deed).



Reasonable time to accept an offer if no time is stated

Withdrawal of offer before acceptance



Counter offer causes original offer to lapse



## CASE EXAMPLE

*Payne v. Cave* (1789) 3 Term Rep 148

**Facts:** Cave bid £40 for goods being auctioned, but before they were knocked down to him, he withdrew the bid. Payne maintained that he could not withdraw in this fashion.

**Decision:** A bid is only an offer that can be withdrawn at any time before acceptance. This is called revocation. At an auction, acceptance takes place on the fall of the hammer. As the defendant had withdrawn his bid before the hammer fell, his offer was terminated.

Revocation must be communicated to offeree

For the revocation to be effective, it must be **communicated** to the offeree. It does not have to be communicated by the offeror personally; it can be done by another person on behalf of the offeror or it may happen unintentionally. The offeree is bound by a notice of revocation.



## CASE EXAMPLE

*Dickinson v. Dodds* (1876) 2 Ch D 463

**Facts:** On a Wednesday, Dodds offered, by letter, to sell Dickinson some houses for £800. The letter stated that the offer was 'to be left over until Friday, 9 a.m.'. Despite this, Dodds sold the houses to a third party on the Thursday. Dickinson heard of this sale from a fourth person on Thursday evening. Before 9 a.m. on Friday morning, Dickinson attempted to accept Dodd's offer by handing him a formal acceptance.

**Decision:** This was not a valid acceptance. An offer can be revoked without the offeror having to give notice of it personally. If the offeree becomes aware that the offer has been revoked from a reliable source then that is sufficient. The offer had been validly revoked before acceptance because Dickinson had received notice of it from the fourth person.

Following termination offer cannot be accepted

### Rejection of an offer

If an offeree rejects an offer, then this will have the effect of **terminating** the offer. It is not possible for the offeree to try to accept the offer at a later time. A new offer must be made before acceptance can occur.

An offer is rejected if a counter offer is made.

### Death of the offeree or offeror

The death of the offeree or offeror may terminate an offer. If an offeror dies, an offeree cannot accept an offer after notice has been received of the offeror's death. Notice of death will terminate the offer. The death of the offeree before acceptance will also terminate an offer.

If acceptance has been made before death occurs, it may be possible to proceed with the contract, which will then be carried out by the personal representative of the deceased (e.g. the executor). This is not possible if a contract is for personal services—that is, an employment contract.



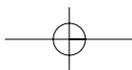
## CASE EXAMPLE

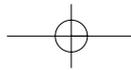
*Carter v. Hyde* (1923) 33 CLR 115

**Facts:** Carter gave Hyde an option to buy certain premises within a period of three months. Hyde died, but his executors exercised the option before the three months had expired. Carter claimed they were not entitled to do so, saying that the offer had lapsed on Hyde's death.

**Decision:** The option was not intended to be one that was personal to Hyde and so it could be exercised by his executors for the benefit of the estate. The offer had not lapsed on Hyde's death.

If the offeree learns of the offeror's death prior to acceptance of an offer the purported acceptance will be ineffective. The following case example illustrates this point.





## CASE EXAMPLE

*Fong v. Cilli* (1968) 11 FLR 495

**Facts:** Fong owned land. Cilli and another person signed a contract of sale in respect of the land. Before the second purchaser signed the contract, Fong died. Despite received notification of Fong’s death, the second purchaser still signed the contract and an attempt was made to make Fong’s estate liable for the promise made prior to his death.

**Decision:** The second purchaser knew of the death of the offeror before signing the contract. He could not, therefore, accept the offer; it had already lapsed.

### Non-occurrence of a condition

If a condition is attached to an offer and it is not met, then the offer will be terminated (e.g. an offer to purchase a house on the condition that the purchaser has a loan approved by a financial institution). This is called a **condition precedent**. If the loan is not approved, then the condition has not been met and no contract has been made.



Failure to satisfy a condition precedent

## RULES OF ACCEPTANCE

An acceptance occurs when the offeree agrees to the proposal of the offeror on the terms required by the offeror. For acceptance to occur, there are a number of rules or requirements that must be met.

### Communication of acceptance

An acceptance will only be valid if it is communicated to the offeror. It may be verbal or in writing. Acceptance of an offer can only be communicated to the offeror by the offeree or by the offeree’s authorised agent. The offeror must know that the offer has been accepted. Figure 7.8 illustrates the relationship between the offeror and the offeree, and the offeree’s agent.

Acceptance may be verbal or in writing but must be communicated to offeror

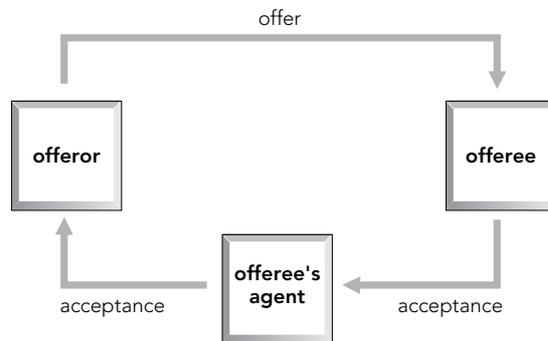


FIGURE 7.8 Acceptance of an offer by offeree’s agent

## CASE EXAMPLE

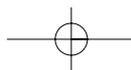
*Powell v. Lee* (1908) 99 LT 284

**Facts:** The plaintiff applied for a job as a headmaster of a school. The managers of the school considered his application and decided to appoint him. One of the managers, without the permission of the others, telegraphed him advising that his application had been successful. A further meeting of managers was held in which the decision was overturned and another person was appointed to the position. Powell sued for breach of contract.

**Decision:** Powell failed in his action for breach of contract. Acceptance of an offer will only be effective if it is communicated by the acceptor or the acceptor’s authorised agent. In this case, the manager who sent the telegram was not authorised and therefore there was no valid acceptance—and no contract.



Acceptance must be communicated by an authorised person





The same question was before the court in the next case example. However, the decision of the court was different from that in *Powell v. Lee*.



### CASE EXAMPLE

*Northern Territory of Australian v. Skywest Airlines Pty Ltd* (1987) 48 NTR 20

**Facts:** The Northern Territory Government called for tenders for the supply of aerial medical flight services. Skywest was the successful tenderer. The validity of the contract was challenged by a competitor who alleged the Tender Board was not properly constituted and/or that the officer who signed the telex of acceptance did not have the authority to do so.

**Decision:** The officer who sent the telex notifying of acceptance regularly performed this task. The court held that it could be assumed the officer did so with the knowledge and approval of the Tender Board. The court held therefore, that the Tender Board had validly accepted Skywest's offer and that acceptance had been validly communicated to Skywest.

**Silence cannot amount to acceptance.**



### CASE EXAMPLE

*Felthouse v. Bindley* (1862) 11 CB (NS) 869; 142 ER 1037

**Facts:** The plaintiff's uncle sent a telegram to the plaintiff (his nephew). The telegram stated: 'I will buy your horse for £30 15s and if I hear no more I will consider it mine.' The nephew never replied and subsequently sold the horse to another person. The question that arose was whether the offer had been accepted by the nephew.

**Decision:** The court held there was no acceptance, as silence could not constitute acceptance. Acceptance needed to be communicated to the offeror. The court said that a mere 'mental acceptance' was insufficient.

Mental acceptance insufficient

Acceptance does not always  
need to be communicated

There are several **exceptions** to the rule that the acceptance of an offer must be communicated. For example, communication of acceptance is not required where the offeror's right to receive notification of acceptance is expressly or impliedly waived by the offeror or the offer is made 'to the world'.



### CASE EXAMPLE

*Carlill v. Carbolic Smoke Ball Co.* [1893] 1 QB 256

**Facts:** The facts of this case were discussed on p. xxx.

**Decision:** It was not necessary for all persons undertaking the conditions of using the smoke ball to notify the company that they were doing so. This would not have been practical.

Conduct may amount  
to acceptance

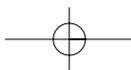
The rule regarding communication of acceptance will often be waived when the offer in question can be accepted by the doing of an act. For example, the return of property pursuant to a reward is an acceptance. It is not necessary for the finder to notify the offeror that they intend to accept the offer; it is necessary only that the finder acts in the knowledge that the offer had been made. Acceptance may be inferred from the conduct of the parties.



### CASE EXAMPLE

*Empirnall Holdings Pty Ltd v. Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523

**Facts:** The offeree was a developer who had not signed a printed contract but had commenced work under its terms. The offeree subsequently sought to avoid being bound by the terms of the contract, relying on the absence of any formally executed contract between the parties.



**Decision:** The New South Wales Court of Appeal found that acceptance could be inferred from the conduct of the offeree, which was consistent with the terms contained in the printed contract. Although the offeree had not signed the printed contract, their conduct indicated that they had submitted to the terms of the contract.

### Contracts by post

Special rules apply where an acceptance is to be made through the postal system. An acceptance that is made through the post is effective when the letter of acceptance is placed in the postbox. Provided the letter has had its postage fees paid and is addressed correctly, **acceptance occurs on posting**. This is the case even if the letter is mislaid and never reaches the offeror. This rule is called the **postal rule**.

The postal rule developed in England in the late 1800s when the postal system was the principal means of communication. There were no instantaneous communication systems such as telexes, facsimile machines and email.

The postal rule applies only if the postal system is contemplated as a mode of acceptance of an offer. This will usually be the case if the offer itself was posted.

It is possible to exclude the operation of the postal rule. The offeror can specify that acceptance will not take place until actual receipt of the notification of acceptance occurs. The postal rule only applies to **acceptances**, not to offers. An offer made through the post will not be effective until it is received and read by the offeree.

Acceptance occurs when letter placed in postbox

Postal system must be contemplated

### EXAMPLE

Sally writes to Michael: 'I offer to sell you my tennis racquet for \$75.' She posts the letter on 1 May 2002. Michael receives the letter on 3 May 2002 and decides to accept. Michael posts a letter of acceptance on 4 May 2002.

In this example:

- The offer is not communicated to Michael until he receives the letter on 3 May 2002.
- As the offer has been made in writing and was sent via the postal system, it is contemplated that acceptance can be made by post.
- Acceptance of the offer occurs immediately Michael places his letter into the postbox on 4 May 2002.

It is possible for an offer made by post to be revoked by the offeror. However, revocation will be ineffective unless it is communicated to the offeree *before* the letter of acceptance is posted. Using the above example, if Sally wishes to revoke her offer, she must communicate this to Michael *before* he posts his letter of acceptance. There would be insufficient time for her to give written notification. However, she could revoke her offer by speaking to Michael personally or by telephone.



Revoking an offer made by post

### CASE EXAMPLE

*Elizabeth City Centre Pty Ltd v. Corralyn Pty Ltd* (1994) 63 SASR 235

**Facts:** Corralyn Pty Ltd sought to renew its sub-lease of shop premises by sending a letter of acceptance to Elizabeth City Centre Pty Ltd within the time specified by the Centre management. The letter was allegedly never received by the company and the sub-lease was not extended. The sub-lease provided that a notice sent by certified or registered mail was deemed to be 'served' on the third business day next, following the day on which it was posted.

**Decision:** The clause governing notification by mail had the effect of impliedly excluding the operation of the postal acceptance rule. The notice had not been received by Elizabeth City Centre Pty Ltd and therefore Corralyn Pty Ltd had not exercised its option to renew the sub-lease. The court said that the postal acceptance rule will be excluded where an uncommunicated acceptance was not intended by the parties.





Actual communication required

**Instantaneous communications**

The postal rule does not apply to means of communication that are virtually instantaneous (e.g. telex, telephone, facsimile machines or email). Unless there is **actual** communication, no contract will be created. The postal rule does apply to telegrams, which are treated as letters and not as instantaneous communications.

**CASE EXAMPLE**

*Proton Investments Pty Ltd v. Vehekin Pty Ltd* (1989) NSW Conv R 55-452

**Facts:** Proton argued that a communication by facsimile (in this case a termination of contract) was ineffective because it was received by a machine in an office that adjoined the office of Proton's solicitor.

**Decision:** The New South Wales Court of Appeal found that notice had been effectively served on Proton's solicitors. It was the normal practice of the solicitor to use the facsimile machine in the adjoining office that he nominated as his own. The facsimile notice amounted to an instantaneous communication.

Acceptance by facsimile

By implication it would appear that the reasoning of the New South Wales Court of Appeal in the above case could be extended to support the use of the facsimile as an effective means of instantaneously communicating the acceptance of an offer.

**CASE EXAMPLE**

*Byrne & Co. v. Leon Van Tienhoven & Co.* (1880) 5 CPD 344

**Facts:** The defendant Leon Van Tienhoven & Co. in Cardiff wrote to the plaintiff Byrne & Co. in New York a letter dated 1 October, offering them goods for sale. Byrne & Co. received the letter of offer on 11 October. They accepted the offer by telegram on 11 October. They also wrote a letter, dated 15 October, accepting the offer. On 8 October Leon Van Tienhoven & Co. posted a letter to the plaintiff withdrawing their offer. This letter was not received by the plaintiff company until 20 October. The issue was whether this was a valid revocation of the offer.

**Decision:** The letter of withdrawal was not effective. The contract was made on 11 October when the telegram was sent. At this point the plaintiff had no notice that the offer of 1 October had been revoked. Revocation, to be effective, would have had to reach the plaintiff company before they sent their telegram to the defendant company (i.e. before 11 October).

**Acceptance must be in reliance of an offer**

A person cannot accept an offer unless they are aware of it.

Acceptance will occur simply by the doing of an act—for example, returning property pursuant to a reward. If the person returning the property to its owner has no knowledge of the reward, they therefore have no knowledge of the offer. Their action of returning the item cannot amount to acceptance as this act was not done in reliance of the offer.

Sometimes a person may accept an offer, but their act of acceptance is not in reliance of the offer. It may have been made for some other reason. This is well illustrated earlier in this chapter by the case of *Crown v. Clarke* (see p. xxx).

**Acceptance must be unqualified**

To create a valid contract, an offer must be accepted without qualifications. If acceptance is qualified, the law will generally regard it as a counter offer.

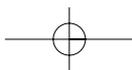
**Discussion question**

Do you think the postal rule should still operate today, given that it was created at a time when there were no instantaneous means of communication?

Knowledge of the offer

**EXAMPLE**

If Ian offers to sell his refrigerator to Francesca for \$300 and she accepts but says she can only make payment in three instalments of \$100, then this is a qualified acceptance. It will be regarded as a counter offer.



### Conditional acceptance

A conditional acceptance is not an effective acceptance unless the offeror agrees to the condition. A common condition is for the acceptance to be subject to obtaining finance. If finance is subsequently arranged, the condition will be satisfied and a contract will be created. In Chapter 9 we will discuss conditions in more detail, in particular the distinction between conditions precedent and conditions subsequent.

A tentative agreement between parties is a form of conditional acceptance. Often the expression 'subject to contract' is used (i.e. the party agrees subject to a contract being drawn up). Whether a binding contract exists depends on the intention of the parties as disclosed by the language used.

Offeror must agree to condition

### CASE EXAMPLE

*Masters v. Cameron* (1954) 91 CLR 353

**Facts:** The defendant owned a farm and made an agreement with the plaintiff to sell. The agreement was made 'subject to the preparation of a formal contract of sale which shall be acceptable to my [the defendant's] solicitors on the above terms and conditions'. The purchaser was in financial difficulties and argued that there was no binding contract. The court had to decide if there was a binding contract.

**Decision:** Tentative agreements were discussed by the court and were divided into three broad categories:

1. agreements where the parties have arranged all the terms of the bargain and intend to be immediately bound by the terms, but want the terms placed in a restated form
2. agreements where the parties have agreed on all terms but have nevertheless made performance of one or more of the terms conditional upon the execution of a formal document
3. agreements where the parties intend not to make a concluded arrangement, unless and until they execute a formal contract.

Cases falling within the first two categories indicate a contract has been formed. Cases falling within the third category indicate that no contract has been formed. The court held that this contract fell into the third category; therefore, there was no contract.

Acceptance must comply with any special conditions stated in an offer. For example, the offer may state that acceptance must be given in writing and be hand-delivered to the offeror. Acceptance will not be effective unless this occurs.

Special conditions

### Acceptance can only be made by a party to the contract

Acceptance can only come from an offeree—that is, a person who has received an offer. For example, if Amy makes an offer to Boris, it is not possible for Craig to accept the offer as the offer was not made to him.

### Revocation of acceptance

An acceptance, once given, cannot be revoked unless the offeror consents. This is because a bargain has been concluded—that is, a contract has been made, provided the other essential elements required to form a contract are present.

The contract will be regarded as discharged by mutual release. See p. xxx for a discussion of this method of discharging a contract.

Generally acceptance cannot be revoked

### Time

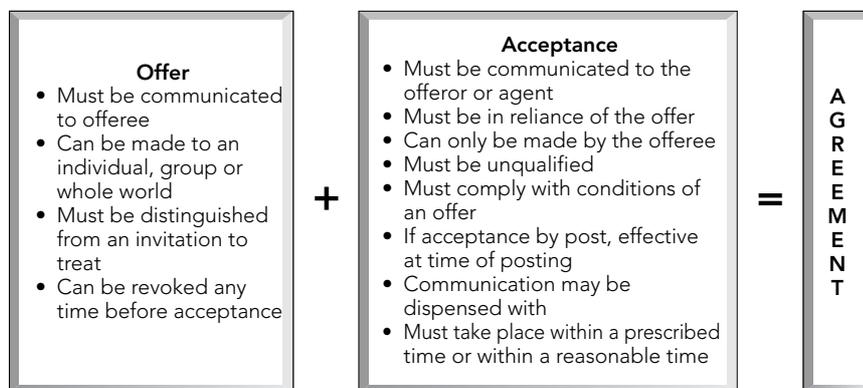
Acceptance must take place within a prescribed time. If no time is prescribed, then acceptance must take place within a reasonable time.





### SUMMARY OF RULES OF OFFER AND ACCEPTANCE

Figure 7.9 summarises the rules governing offer and acceptance. If these rules are satisfied, a valid agreement will exist. A valid contract, however, requires the remaining elements also to be established.

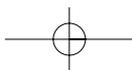


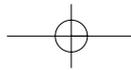
**FIGURE 7.9** The rules of offer and acceptance

## Check your progress 7.2

Place a tick in the appropriate box.

1. A person making an invitation to treat:
  - (a) intends to be bound
  - (b) does not intend to be bound
  - (c) will be presumed by law to be bound
2. At an auction where no reserve price has been set, the highest bid:
  - (a) is an offer that must be accepted
  - (b) is an offer that may be accepted or rejected
  - (c) is acceptance of the vendor's offer
3. An offer will lapse if:
  - (a) it is revoked before acceptance
  - (b) it is made verbally
  - (c) it is not accepted within the time stated
4. If the offeree dies after acceptance of an offer:
  - (a) the contract will be automatically terminated
  - (b) the contract may be performed by the executor of the offeree's estate
  - (c) the contract must be performed if it is a contract for personal service
5. An acceptance that is made through the post is effective when:
  - (a) it is placed in the postbox
  - (b) it is read by the offeror
  - (c) it arrives at the offeror's postal address
6. Instantaneous communications are an exception to the postal acceptance rule.
  - (a) True
  - (b) False





7. Once given, acceptance of an offer:

- (a) can never be revoked
- (b) cannot be revoked unless the offeror consents
- (c) can be revoked within two clear working days

## FORM AND/OR CONSIDERATION

For an agreement to be regarded as a contract, it must either be supported by consideration or be a formal contract. This is the third essential element required to form a valid contract.

### CONSIDERATION

Consideration can be regarded as something done or promised by one party in exchange for something done or promised by the other party. Mutual promises are the basis of consideration. Consideration can be described as an exchange of value for value. Figure 7.10 illustrates the factors relevant to the element of consideration.

Value for value

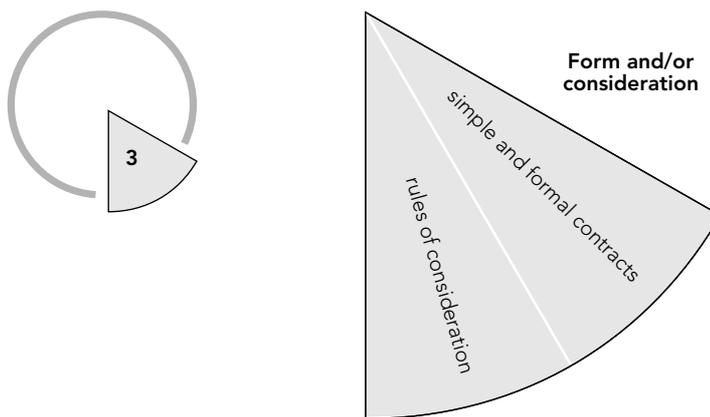


FIGURE 7.10 Factors relevant to form and/or consideration

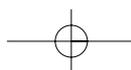
The terms ‘promisor’ and ‘promisee’ are used to describe the parties to a contract in which consideration is present. The **promisor** is the person undertaking to perform the consideration; the **promisee** is the recipient of the consideration. In contracts where both parties provide consideration, each party will be both a promisor and a promisee. Consideration can be classified as ‘executory’ or ‘executed’. Consideration that is still to be performed is termed **executory**. Consideration that has already been performed is said to be **executed**.

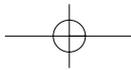
The following are examples of consideration:

- Martin agrees to mow John’s lawn and John agrees to pay Martin \$15.
- Bill agrees to fix Anton’s lawnmower if Anton services his car.
- Tim agrees to discontinue legal proceedings against Linton if Linton pays money owing to Tim.

Promises that are not supported by consideration are called **gratuitous promises**. They are gifts and are not enforceable unless they are in a particular form—that is, a deed. We will consider the form they must take later in this chapter.

Absence of consideration





Deed does not  
require consideration

## EXAMPLE

Raymond agrees to give Paul \$500 and Paul promises nothing in return. This promise will be unenforceable by Paul.

### The significance of the distinction between formal and simple contracts

If a contract is in a particular form, consideration is not required. Formal contracts do not require consideration. Formal contracts take two forms: **contracts of record** and **contracts under seal** (deeds). An example of a contract of record is a judgment of a court. Contracts under seal (deeds) must be in writing. A deed is a formal written contract that does not require consideration.

Simple contracts are all those contracts that are neither under seal nor contracts of record. Simple contracts may take any form—verbal, written or implied—but they *must* have consideration to be valid.

### Rules with respect to consideration

Consideration is essential to every simple contract. There are a number of rules with respect to consideration (see Figure 7.11).

#### Consideration:

- can be present or future, but not past
- must be of some value but need not be adequate
- must be definite, not vague
- must be capable of being performed
- must not be illegal or unlawful
- must be more than a person is already required to do
- must move from the promisee
- cannot be satisfied by part payment of a debt

**FIGURE 7.11** Rules relating to consideration

### *Consideration can be present or future, but not past*

Past consideration  
is no consideration

**Present consideration** exists where the promise or act that is the consideration is performed when the contract is made. **Future consideration** exists where the act that is the consideration is to be performed at a time after the contract is made. **Past consideration** exists where the act that is the consideration was performed before the contract was made. Generally, it is not possible to rely on an act or promise that has already been performed. It is not usually appropriate to create new rights and obligations for matters that have occurred in the past.

There is an exception to the past consideration rule not being adequate consideration. The following case illustrates this exception.



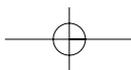
## CASE EXAMPLE

*Pao On v. Lau Yiu Long* [1980] AC 614

**Decision:** The Privy Council at p. 615 said:

An act done before the giving of a promise to make a payment or to confer some other benefit can sometimes be consideration for the promise. The act must have been done at the promisor's request, the parties must have understood that the act was to be remunerated either by a payment or the conferment of some other benefit, and payment, or the conferment of a benefit, must have been legally enforceable had it been promised in advance.

The types of consideration are set out in Figure 7.12.



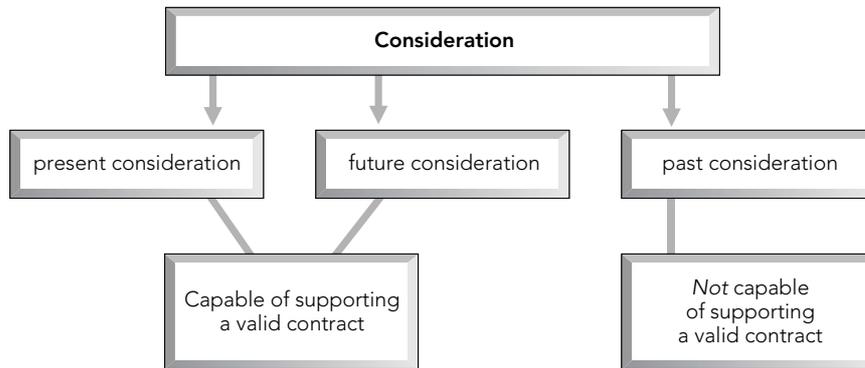


FIGURE 7.12 Types of consideration

## LAW IN ACTION

Lee agrees to sell his bicycle to Mario, who agrees to pay \$150. If Mario pays the money in return for the bicycle at the time the contract is made, then this is present consideration. If the payment and the transfer of possession of the bicycle are to take place at a time after the contract is made, then the consideration is future consideration.

If Mario is to purchase Lee's bike for \$150 and Lee is to rely on work that Mario performed for Lee last week, then consideration is past consideration. The act that is the consideration is already past.

## CASE EXAMPLE

*Roscorla v. Thomas* [1842] 3 QB 234

**Facts:** Roscorla purchased a horse from Thomas. After the contract was completed, Roscorla demanded a promise from Thomas that the horse was sound and free from vice. The promise was given and subsequently it was found that the horse was vicious. Roscorla sued for breach of contract.

**Decision:** There was no breach of contract as Roscorla had provided no consideration for Thomas's promise about the horse. The contract had already been completed when the promise was made and therefore it was past consideration. As a general rule, past consideration cannot support a valid contract. Consideration must be present or future.

### *Consideration must be of some value but need not be adequate*

Consideration can be nominal or trivial. The courts only require that there is *some* consideration present.

## CASE EXAMPLE

*Chappell & Co. Ltd v. Nestlé Co. Ltd* [1960] AC 87

**Facts:** The defendant company promoted chocolate bars they made by offering a choice of records in return for a set payment plus the wrappers of three chocolate bars. There was a dispute with the owner of the copyright of one of the tunes on one of the records. The dispute centred around whether the selling price (on which the royalties were calculated) included the value of three empty wrappers. The owners of the copyright claimed the wrappers doubled the value upon which the royalties were calculated. Nestlé argued that the sending in of the wrappers was simply a condition that had to be met in buying the records, since the wrappers were of no value to Nestlé.

**Decision:** The empty wrappers were part of the selling price of the records. The fact that the wrappers were of no value to Nestlé was irrelevant. The consideration for the contract was the money and the value of the three chocolate bars. A person could not get the records without sending three chocolate wrappers and the money.



Consideration must be definite

***The nature of the consideration must be definite, not vague***

If the consideration is too vague there will be no contract.



**CASE EXAMPLE**

*Shiels v. Drysdale* (1880) 6 VLR Eq 126

**Facts:** A daughter promised to look after her elderly mother and father for as long as they lived. In consideration for the daughter's promise, the father promised to transfer to her his interest in 'some' of his property.

**Decision:** The court held that this agreement was void because the consideration was not definite. No particular property was indicated in the agreement and therefore it was too vague and not legally enforceable.

***Consideration is not permitted to be so vague that it is illusory.***

This is illustrated by the following case example.



**CASE EXAMPLE**

*Placer Development Ltd v. Commonwealth* (1969) 121 CLR 353

**Facts:** In 1952 the parties entered a written agreement whereby it was agreed that Placer Developments would establish an overseas timber company to produce plywood and other timber products. These products would subsequently be imported into Australia.

The following clause was included in the agreement:

If customs duty is paid upon the importation into Australia of the Plywood ... and other products of the timber company, and is not remitted, the Commonwealth will pay to the timber company a subsidy upon the exportation of these products ... for entry into Australia of an amount or at a rate determined by the Commonwealth from time to time, but the amount of the subsidy paid shall not exceed the amount of customs duty paid and not remitted ...

No remittance was received by the company from 1959 to 1963 despite the fact that it had imported timber into Australia on which it had paid customs duty. The court had to decide if the above clause was valid.

**Decision:** The court held that clause was not binding on the Commonwealth. It was held that a promise of a government subsidy was meaningless if there was no specification of some amount or some basis of calculation. No contractual obligation was created by the clause.

***Consideration must be capable of being performed***

It is not possible to enforce a promise that cannot be performed.



**EXAMPLE**

Angela agrees to sell a bicycle to Peter but she is not the owner of the bike.

***Consideration must not be illegal or unlawful***

Consideration is not valid if the act that is the consideration is in any way illegal or unlawful. Consideration also must not involve a breach of the civil law or public duty.



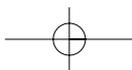
**EXAMPLE**

An agreement to pay a person to commit a robbery would not be valid consideration.

***Consideration must be more than a person is already obliged to do***

A person who is already obliged to perform an act or duty will not be able to rely on that act or duty as appropriate consideration to support a contract. A person may already be under an obligation to perform an act by virtue of an existing contractual term. Such an act cannot support a new contract, as there is no new consideration.

Existing obligations and duties



## CASE EXAMPLE

*Stilk v. Myrick* (1809) 2 Camp 317; 170 ER 1168

**Facts:** The plaintiff (sailors) contracted to crew a ship on a voyage for a fixed amount of money. During the voyage, two crew members deserted. The captain of the ship promised to divide the deserters' wages among the remaining crew if they completed the voyage. On the completion of the voyage, the captain refused to pay the additional money to the remaining crew.

**Decision:** The court agreed with the captain's decision. The reason the remaining crew were not entitled to extra money was because when the crew initially contracted for their wages, they agreed to complete the journey, even if others deserted. The promise by the captain to pay additional money was not supported by consideration. The sailors were doing nothing more than they were already obliged to do pursuant to their contract.

## CASE EXAMPLE

*Williams v. Roffey Bros and Nicholls (Contractors) Ltd* [1990] 1 All ER 512

**Facts:** The defendant was a building contractor who had contracted the plaintiff to do carpentry work on a particular project. The plaintiff experienced financial difficulties because he had underquoted. The defendant ran the risk of a penalty clause in the building contract being imposed for late completion, and he offered Williams an additional payment to complete the work. Williams made some further progress and was paid a further small sum, but the job was still not completed.

When the defendant failed to pay more of the sub-contract price, Williams stopped work and claimed the balance owing under the original contract plus the additional payment. The defendant's defence was that the additional promise was unsupported by consideration of the plaintiff as the plaintiff was already under a contract with the defendant.

**Decision:** The court found that the commercial benefit derived from having the work completed on time amounted to sufficient consideration. The alternative course open to the contractor was less practical, requiring a replacement sub-contractor to be found and risking liability for failing to complete the requirements of the head contract on time.

The court decided that the mutual advantages to both parties were held to amount to sufficient consideration to support the defendant's second agreement to pay an additional amount to the plaintiff.

When a party under a pre-existing contractual obligation promises to do something beyond its existing obligation in exchange for payment, this amounts to consideration. The new agreement will be enforceable.

Additional promise may amount to consideration

## EXAMPLE

Nino agrees to mow Svetlana's lawn for \$15. If Nino is then asked to clip Svetlana's hedge, this would be regarded as additional to his existing obligations.

A person cannot seek to rely on an act as consideration for a contract if they are already under a legal duty to perform that act.



## CASE EXAMPLE

*Foakes v. Beer* (1884) 9 App Cas 605

**Facts:** Beer obtained a judgment against Foakes. Foakes agreed to settle the debt by the payment of £1000 immediately and the balance by instalments. Beer agreed not to take any further action on the judgment. All judgments bear interest from the date of judgment, and after Foakes paid the first instalment, Beer sued for the interest. Foakes claimed he was not liable to pay any interest because of the agreement.



Existing legal obligation will not be sufficient consideration



**Decision:** Beer was entitled to recover the interest because the payment of a lesser sum is not consideration for the promise to take no further action on the judgment. Foakes's promise to pay the judgment, which included the interest component required by law, was a promise to do no more than he was legally obliged to do.



## CASE EXAMPLE

*Collins v. Godefroy* (1831) 1B & Ad 950; 109 ER 1040

**Facts:** A person was subpoenaed to give evidence in court. The plaintiff also entered an agreement with the defendant that this person would be paid for giving his evidence.

**Decision:** The court held that a person who is subpoenaed to give evidence in court, and who receives a witness fee, cannot enforce an agreement to be paid for attending court. Such an agreement is not supported by consideration. The person is already obliged by law to perform the act that is the consideration.

### *Consideration must move from the promisee*

Payment for the promise

The 'promisor' is the person making the promise. The 'promisee' is the person to whom the promise is made. The promise of the promisor will not be supported by consideration and be legally enforceable unless supported by consideration from the promisee. Another way of expressing the same idea is to say that for a promise to be enforceable, it must be paid for.

A promise can be made to two or more persons jointly, with only one of them providing consideration. The party not providing any consideration can still enforce the agreement.



## CASE EXAMPLE

*Coolls v. Bagot's Executor and Trustee Co. Ltd* (1967) 119 CLR 460

**Facts:** A husband granted the right to a mine to a company. In return, a royalty was to be paid to himself and his wife jointly. The wife provided no consideration for this agreement. The husband died and the wife sought to enforce the agreement.

**Decision:** The High Court held that the wife should succeed in her claim. The court regarded the husband and wife as joint promisees. A promise was made to them jointly in respect of the royalties. It was sufficient for one of the promisees (the husband) to provide the consideration on behalf of them both.



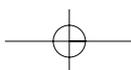
## CASE EXAMPLE

*Dunlop Pneumatic Tyre Co. Ltd v. Selfridge & Co. Ltd* [1915] AC 847

**Facts:** The plaintiff company agreed with a motor accessory dealer to sell tyres to the dealer. The dealer agreed to allow a discount of 10 per cent from the plaintiff's price when reselling the tyres to traders. The dealer agreed to obtain written undertakings that these traders would observe the plaintiff's prices. The defendant was a trader who gave such an undertaking but then sold below the listed price. The plaintiff sued for breach of the agreement between the dealer and the defendant.

**Decision:** The court held that the agreement was unenforceable, as only those who are parties to a contract may sue on the contract. If a person wished to sue on the contract, consideration must have been given to them by the promisor. There was no consideration moving from the plaintiff in this case and therefore the plaintiff had no right to claim a breach of contract.

Although consideration must move from the promisee it does not have to move to the promisor. The promisor can specify that another person is to receive the benefit that is derived from the promisee's action.



## EXAMPLE

Alannah promises to pay Anne \$2000 if Anne paves Margaret's driveway.

In the above example, Alannah is not receiving any direct benefit from Anne's consideration, but Margaret is. The consideration is moving from the promisee (Anne), but not to the promisor (Alannah). Despite this, Anne can enforce the agreement against Alannah irrespective of who derives the benefit of her consideration, as long as the promisor's directive is met.

### *Part payment of a debt will not be adequate consideration*

Generally, part payment of a debt will not be adequate consideration to discharge a debt.

## EXAMPLE

Ian owes Diana \$150. Diana agrees to accept \$100 from Ian in full satisfaction of the debt. Ian may argue that Diana cannot later sue him for the outstanding \$50. Legally this argument would be unsuccessful. There is no consideration passing from Ian to Diana in return for her promise not to sue.

The law has created several exceptions to this rule. They are:

- Payment of a smaller sum along with something else (e.g. agreement to perform labour) will discharge the debt.
- Payment of a smaller sum before the debt is due will be enforceable.
- Payment of a smaller sum at a different place or in a different currency can operate as a legally enforceable discharge of a debt.
- Signing a deed of release may discharge the debt.
- Payment may be made by a third party who is not bound by the contract.
- Agreeing to perform any other act that the debtor is not bound by the contract to perform may result in a legally enforceable discharge.
- By relying on the defence of promissory estoppel, in some circumstances a contract can be altered despite a lack of consideration being provided for the altered promise. This is due to the doctrine of promissory estoppel (see the definition below) that requires several elements to be satisfied:
  - The promisee has altered their position in reliance on a new promise.
  - It would be impossible for the promisee to return to their original position without detriment.
  - It would be unfair for the promisor to renege.

The doctrine of promissory estoppel was developed in the following case.

## CASE EXAMPLE

*Central London Property Trust Ltd v. High Trees House Ltd* [1947] KB 130

**Facts:** In 1937 in England, the plaintiff leased a block of flats to the defendant for ninety-nine years at £2500 per annum. War broke out and it became difficult to fill all the flats. The plaintiff agreed to reduce the rent to £1200 for the duration of the war. When the war ended, the rent reverted to £2500, but the plaintiff claimed the full rent for the whole period.

**Decision:** The court held that the plaintiff was not entitled to claim the full rent for the whole period (including the war years), despite the fact that the defendant had given no consideration for the plaintiff's promise not to demand the full rent entitlement.

Where one party to a contract, by its behaviour, leads the other party to the contract to believe a certain state of affairs exists between them, the courts will support that state of



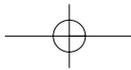
Part payment of a debt



Exceptions to rule



Promissory estoppel



affairs rather than the terms of the contract. It is not possible at a later time for one party to seek to deny the state of affairs. This is called the doctrine of promissory estoppel. The High Court of Australia confirmed the doctrine applied in Australia in *Legione v. Hateley* (1983) 152 CLR 406. The doctrine was extended by the High Court of Australia in *Waltons Stores (Interstate) Ltd v. Maher* (1988) 164 CLR 387.



## CASE EXAMPLE

*Waltons Stores (Interstate) Ltd v. Maher* (1988) 164 CLR 387

**Facts:** Maher and Waltons entered into negotiations whereby Maher would lease commercial property to Waltons. Under the terms of the proposal Maher was required to demolish an existing building and erect and fit out a new building. This work was to be completed by a specified date. Maher indicated that the work would not commence until final agreement had been reached. Subsequently, Maher received documents from Waltons' solicitors incorporating changes requested by Maher. Waltons had not yet approved the amendments. Waltons' solicitors advised Maher that he would be notified the following day if Waltons objected to any of the changes incorporated at Maher's request. Thereafter Maher was required to sign the documents and return them to Waltons' solicitors. Several days later no word had been received from Waltons' solicitors. Maher signed the documents 'by way of exchange' and returned them to Waltons' solicitors.

Although Waltons' solicitors did not acknowledge receipt of the signed documents for almost eight weeks, Maher, believing an agreement had been reached, proceeded to demolish the building on the site in question. A substantial amount of work was undertaken on the new building, and Maher anticipated that the work would be completed by the date specified in the agreement he had signed. Then Maher was notified by Waltons' solicitors that the building would not be required and that, in their view, no contract had been formally created. Maher sued, seeking specific performance of the contract.

**Decision:** Although no contract had been formally created, Maher had relied to his detriment on the assumption that Waltons was proceeding with the project. Waltons' failure to notify Maher that it had decided not to proceed with the project amounted to unconscionable conduct. As a result Waltons were estopped from escaping their obligations under the agreement.



## CASE EXAMPLE

*Commonwealth v. Verwayen* (1990) 95 ALR 321

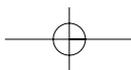
**Facts:** The Commonwealth provided a written assurance that it would not challenge legal actions arising out of the sinking of the HMAS *Voyager* in 1964 on the grounds that the action was out of time. The Commonwealth subsequently sought to rely on the relevant statute of limitation when Verwayen brought an action seeking damages connected to the sinking.

**Decision:** The High Court of Australia found that Verwayen had relied on the assurance provided by the Commonwealth to his detriment. He had continued legal proceedings without considering other forms of dispute resolution and this had caused him to experience stress and anxiety (in addition to the inevitable legal costs of the action). The Commonwealth was estopped from relying on the statute of limitation.

## FORM

Valid contracts in the  
absence of consideration

An agreement that lacks consideration may still be an enforceable agreement if it is created in a particular way or form. Simple contracts require consideration to be valid. If consideration is missing, the contract can only be enforced if it is created in a particular form—it must be created under seal by deed. A **gratuitous promise** is a promise made without consideration. To be enforceable, it can be put in the form of a deed. A deed is a



written document that is signed by the parties; in ancient times, it was 'signed, sealed and delivered'. A deed without consideration is enforceable. Common law and statutes require some contracts to be in the form of a deed. These include:

- the transfer of ownership of a British ship or share in such a ship
- the appointment of an agent where the agent will be contracting by deed (such a document is known as a power of attorney).

Some contracts will not be valid unless they are in a particular form. Some contracts are required to be either in writing or evidenced in writing.

#### Contracts required to be in writing

A contract falling into this group implies that all the terms of the agreement must be contained in one written document. The following kinds of simple contracts are required by statute to be in writing:

- bills of exchange and promissory notes (*Bills of Exchange Act 1909* (Cwlth))
- cheques (*Cheques Act 1986* (Cwlth))
- assignments and mortgages of life insurance policies (*Life Insurance Act 1945* (Cwlth))
- assignment (transfer) of copyright (*Copyright Act 1968* (Cwlth))
- contracts for marine insurance (*Marine Insurance Act 1909* (Cwlth)).

If these contracts are not in writing, the general effect is that the contract is void.

Statutes require some contracts to be in writing

## Check your progress 7.3

Place a tick in the appropriate box.

1. Consideration that is still to be performed is termed:
  - (a) future consideration
  - (b) executed consideration
  - (c) executory consideration
2. Simple contracts:
  - (a) must have consideration to be valid
  - (b) must have consideration and be in writing to be valid
  - (c) can take any form and do not require consideration to be valid
3. Consideration can be:
  - (a) present, future or past
  - (b) present, future, but not past
  - (c) present, past, but not future
4. If a promise is made to two or more persons jointly:
  - (a) consideration must be provided by both persons
  - (b) consideration may be provided by only one person
  - (c) consideration may be provided by only one person but the other person cannot enforce the agreement
5. Consideration must be:
  - (a) the equivalent of market value
  - (b) adequate
  - (c) of some value
6. Consideration must move from:
  - (a) the promisee
  - (b) the promisor to the promisee
  - (c) the defendant to the plaintiff



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7. A 'gratuitous promise' is a promise made without consideration:
- (a) true
- (b) false
8. Bills of exchange and cheques are examples of contracts that:
- (a) must be in writing
- (b) require no consideration
- (c) may be made verbally or expressly

### Contracts required to be evidenced in writing

Written evidence of the contract may be found in several documents

These contracts require some written evidence that a contract exists. It is usual for this evidence to be found in several written documents. The written documents are not the contract itself but written evidence of the contract. In most States and Territories, legislation requires contracts for the sale of land or other interests in land to be evidenced in writing. Examples of interests in land other than a sale include a lease or mortgage of land. Written evidence of all of the matters set out in Figure 7.13 must be produced.

- The names of the parties
- The subject matter
- The consideration
- A signature of the person against whom the contract is sought to be enforced

**FIGURE 7.13** Matters that must be evidenced in writing

The documents evidencing a contract for the sale of land might include letters passing between the parties, a receipt for the deposit, and a cheque signed by the purchaser. These documents, collectively, are written evidence of the contract. A failure to produce written evidence does not render the contract void, but simply unenforceable.

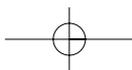
Reason behind written evidence requirement

The historical origin of the requirement for contracts to be evidenced in writing was s. 4 of the English *Statute of Frauds* passed in 1677. The rationale behind the requirement of written evidence was to reduce fraud and ensure enforceability of an agreement that had substance. Section 4 of the *Statute of Frauds* was embodied in many statutes passed in Australia. However, in recent years, this requirement has been removed with respect to some transactions, notably contracts for the sale of goods. This is the case in New South Wales, Victoria, Queensland, South Australia and the ACT. In the Northern Territory the requirement applies to contracts for the sale of goods for a value of \$50 and upwards.

Part performance of a contract

A verbal contract for the sale of land may be enforceable despite the lack of written evidence. Reliance can be placed on the equitable doctrine of part performance. A person can enforce a contract if it can be shown that they have performed certain acts that are in reliance upon promises made by the other party to the contract. Several criteria must be satisfied before the doctrine can operate:

- The acts of part performance must be such that they have been performed in reliance on the contract alleged and not on another arrangement.
- The acts must be such as to render it a fraud if the defendant were to take advantage of the contract not being in writing (i.e. it would be a fraud (and inappropriate) for the defendant to say that there was no contract because there was nothing in writing).
- The contract that the acts refer to must be a contract that, by its nature, can be enforceable by the court.
- There must be parol (i.e. verbal) evidence of the contract that is allowed into evidence by the acts of part performance.

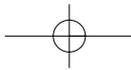


The **parol evidence rule** provides that where a contract is wholly in writing, the courts are reluctant to go beyond the document itself to show the meaning of the words. It will not be admissible for parol or oral evidence to add words to, or alter the words of, a written document. This rule is subject to qualifications and exceptions, but they are outside the scope of this book.

## Chapter overview

The main points made in this chapter are:

1. A 'contract' is an agreement made between two or more persons that the law will enforce.
2. Contracts can be classified according to formation, validity and performance.
3. Contracts classified according to formation can be express, implied or quasi-contracts.
4. Contracts classified according to validity can be void, voidable, unenforceable or illegal. A void contract is one that is of no legal effect. A voidable contract is one that can be avoided (rescinded) by one party. An unenforceable contract is one that cannot be enforced, due to a technical fault. An illegal contract is one where the purpose or object of the contract is illegal or unlawful.
5. Contracts classified according to performance can be either executed or executory. Executed contracts are those where one party to the contract has performed all of its contractual obligations. Executory contracts are those where both parties to the contract have contractual obligations still to be performed.
6. The law of contract is derived from both common law and statute.
7. Six essential elements must be present to form a valid contract. They are: an intention to create legal relations, an offer and acceptance, form and/or consideration, capacity of parties, reality of consent, and legality of object.
8. The law presumes that there is an intention to create legal relations in business agreements. This presumption can be rebutted by showing evidence to the contrary. Conversely, social and domestic agreements are presumed not to have an intention to create legal relations. Again, this presumption can be rebutted by producing contrary evidence.
9. An 'offer' is a proposal made by a person to enter a contract. If the offer is accepted, a valid contract may exist.
10. An offer must be distinguished from an invitation to treat. Items displayed in a shop window or pictured in a catalogue are invitations to treat. They invite offers to be made that can be either accepted or rejected.
11. The person who makes an offer is called the 'offeror'; the person to whom the offer is made is called the 'offeree'.
12. An offer need not take a specific form. Offers can be made expressly (by spoken or written words) or impliedly (by conduct).
13. An offer can be made to one or more persons. It is possible for an offer to be made to the whole world.
14. To be effective, an offer (including all of its terms and conditions) must be communicated to the offeree. A person cannot accept an offer if they are not aware of its existence.
15. An offer can be terminated in several ways: revocation by the offeror, lapse of time, rejection, death of the offeree or offeror, the making of a counter offer, or a condition remaining unfulfilled.
16. An offer can be revoked at any time before acceptance. An acceptance occurs when the offeree agrees to the offer made by the offeror. An acceptance must be communicated to the offeror. Silence will not be effective. There are several exceptions to this rule—that is, where an acceptance will be valid even though it has not been communicated to the offeror. Examples are where the offeror waives the right to receive notification of acceptance, and where contracts are made by post (postal rule).
17. The postal rule applies when an acceptance of an offer is to be made through the postal system. An acceptance will be effective when the letter of acceptance is posted. This is so even if the letter is delayed or never reaches the offeror.

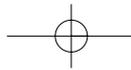


18. Postal offers will only be effective once the letter containing the offer reaches the offeree, and the offeree reads the letter.
19. A postal offer can be revoked, but it must be revoked before acceptance (i.e. before the letter of acceptance is posted).
20. Acceptance of an offer can be made only if the person accepting is aware of the offer.
21. An acceptance must be unqualified. If it is qualified, the law will regard it as a counter offer. A counter offer is an acceptance that involves some alteration to the existing offer, which will then lapse.
22. A conditional acceptance will be ineffective unless the offeror agrees to the conditions and the conditions are satisfied. There may be a question as to whether the parties have reached a final agreement, especially if the term 'subject to contract' is used.
23. An acceptance must take place within a prescribed time or, if no time is stated, within a reasonable time. An acceptance, once made, cannot be revoked unless the offeror consents.
24. A contract needs to be supported by consideration or to be in a particular form.
25. 'Consideration' is the act or promise of a party to a contract. Consideration can be classified as 'executory' or 'executed'. The former is consideration yet to be performed, whereas the latter is consideration that has been performed.
26. Promises not supported by consideration are called 'gratuitous' promises.
27. Consideration is essential to every simple contract: it can be present or future, but not past.
28. Consideration must be: of some value but need not be adequate; definite; capable of being performed; legal; sufficient; and an obligation that has not already been performed.
29. Part payment of a debt will not discharge a debt. Exceptions to this rule are: payment of a lesser amount if given along with something else; payment before the due date; payment in a different currency; and payment at a different place.
30. An agreement lacking consideration may be enforceable. It will be enforceable if it is placed in a particular form called a 'deed'.
31. A 'deed' is a contract under seal, in writing. Some contracts must be in the form of a deed to be enforceable (e.g. a gratuitous promise).
32. Some contracts may need to be either in writing or evidenced in writing. A contract in writing implies that all the terms of the agreement are contained in one written document. If this condition is not fulfilled then the contract will be void.
33. Contracts evidenced in writing require written evidence of the names of the parties, the subject matter, consideration, and a signature of the person against whom the contract is sought to be enforced. This evidence will usually be contained in several written documents. If this requirement is not fulfilled, the contract will be unenforceable.
34. The doctrine of part performance may in certain circumstances be relied upon to enforce a contract that is not in writing but is required to be evidenced in writing.

## Consolidation questions

1. Outline the six essential elements required to form a contract.
2. If a domestic agreement is made between members of a household and is subsequently breached, is a contract presumed? Explain your answer.
3. Define an 'invitation to treat'.
4. What is the difference between an offer and an invitation to treat?
5. Is it possible for an offer to be accepted through the post? Explain the 'postal rule'.
6. Explain under what circumstances an offer may lapse.
7. State three rules of consideration.
8. Explain the difference between a contract evidenced in writing and a contract that is in writing.





9. What is a 'gratuitous promise'?
10. When can an offer be revoked?
11. When can an acceptance be revoked?
12. Define a 'deed'.
13. Explain the doctrine of promissory estoppel.
14. Under what circumstances can a contract be:
  - (a) void
  - (b) unenforceable.
15. Briefly explain the doctrine of part performance and explain under what circumstances it may be important.

## Case study questions

1. Rufus is the father of Robert. Robert's marks at university leave him on the brink of failure. One day Rufus makes an agreement with his adult son. Rufus will give up his life-long habit of smoking if Robert passes all of his subjects. Robert completes his part of the bargain but Rufus refuses to give up smoking. Could Robert sue Rufus for breach of contract? Would he succeed?
2. Michael and Jo are very keen to secure a cheap airfare to London. After weeks of searching for the right fare, they pass a travel agent advertising a direct flight to London for \$650. They immediately withdraw \$1300 and return to the travel agent in order to secure the bargain airfare. They advise the agent that they wish to purchase two tickets. The agent says there has been a mistake and the tickets are \$750 each, not \$650. Michael and Jo are furious and are not willing to pay for additional tickets. Is the travel agent entitled to refuse to sell the tickets for \$650 each?
3. Stuart purchased a Triumph 'Spitfire' sports car from Tim who claimed that the car was part of a limited series released in the mid-1960s. At a Triumph car show Stuart is advised by a number of experts that the Triumph is a later model with some of the trimmings associated with the earlier model. Stuart wishes to know whether the elements necessary to give rise to a valid contract are present. Advise Stuart on this point and outline his potential options.
4. James is a medical student. While undertaking a placement within a hospital, James misplaces his stethoscope. He places a reward notice on the hospital noticeboard. Toby, a fellow medical student, finds the stethoscope and returns it to James. Toby was not aware of the reward notice on the hospital noticeboard. Can Toby claim the reward?
5. Irene offers to sell her sewing machine to Dora for \$200. Dora is a pensioner and is unwilling to pay \$200. Dora says she will pay \$150. Irene refuses to accept this proposal. Dora then decides to accept Irene's original offer of \$200. Can Dora accept this offer?
6. While running late for work, Corey drives through a red light and is detected by a red light camera. Through the post he receives a fine and notification that the driver of the motor vehicle will lose driving points. Corey will lose his licence if he loses any further points. Corey offers his friend Kenny \$1000 if he agrees to notify police that he was the driver of the motor vehicle when it was detected passing through the red light. Kenny agrees and thereafter duly notifies the police that he was the driver of the motor vehicle at the relevant time. The police accept this and Corey does not lose any licence points. Kenny seeks payment of the \$1000 and Corey refuses to pay. Will Kenny succeed in suing Corey for breach of contract for this amount?
7. Graham has agreed verbally to pay \$15 000 for Tom's rare collection of Australiana literature. Before the matter can proceed any further Tom is involved in a serious car accident that results in him entering a coma. It is uncertain whether Tom will regain consciousness. Worried about Tom but still eager to purchase the Australiana literature, Graham consults you to ascertain what essential elements required to give rise to a valid contract are present. Advise Graham on this point and explain what facts may prevent the existence of a valid contract.

