FRUSTRATED CONTRACTS: THE NEED FOR LAW REFORM

The following is in the nature of a postscript to my article, bearing the same title, which was published in the issue of the REVIEW for January, 1945.[1] In that article I ventured to draw attention to the important improvement effected in the law of England by the statute of the United Kingdom entitled the Law Reform (Frustrated Contracts) Act, 1943, and, in order to make some of the relevant material readily available in Canada, I there set out the text of the Seventh Interim Report (Rule in *Chandler* v. *Webster*) of the Law Revision Committee presented to the Parliament of the United Kingdom in 1939, and gave some account of the decision of the House of Lords in *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Limited*,[2] which preceded, and led to the enactment of, the statute of 1943.

In a case like the present one, in which in England an effort has been made to remedy by legislation certain patent defects of the common law, it is obvious that the law of the common law provinces of Canada should not be allowed to lag behind the law of England. It seems worth while therefore to supplement my earlier article by some further observations with regard to the background and scope of the statute of 1943.

The overruling of *Chandler* v. *Webster*[3] in the *Fibrosa* case had remedied one defect in the law of England, but had so to speak created another, in the sense that the House of Lord's decision that the buyer was entitled to the return of his down payment on the ground of total failure of consideration might lead to injustice if the seller had incurred expense in preparing for performance.[4] The statute has afforded a remedy for this injustice by authorizing an allowance to be made to the seller. The statute goes a good deal farther, however, in the direction of enlarging the power of a court to prevent unjust enrichment in various kinds of cases.

The statute has already been the subject of critical analysis in England by two authors — Sir Arnold McNair in a 15-page article,[5] and Glanville L. Williams in a 92-page book.[6] In the

[1] *Supra*, p. 43.
[2] [1943] A.C. 32.
[3] [1904] 1 K.B. 493.
[4] See p. 55, *supra*.
[5] (1944), 60 L.Q. Rev. 160.
[6] THE LAW REFORM (FRUSTRATED CONTRACTS) ACT, 1943: THE TEXT OF THE ACT WITH AN INTRODUCTION AND DETAILED COMMENTARY. Stevens

present article I will not attempt to cover the whole ground of these authors' comments, but will confine myself to an explanation of some of the main features of the statute in the setting of the old English law relating to quasi-contract or unjust enrichment.

Money Had and Received

By the beginning of the eighteenth century it was settled law that in an action of *indebitatus assumpsit,* under a count for money had and received by the defendant to the use of the plaintiff (called for short a count for money had and received), claims might be entertained (1) to recover money paid upon a total failure of consideration, (2) to recover money paid to a person to whom it was not due, and (3) to recover money from a person who had wrongfully taken it. In each of these three cases the cause of action was nominally based on a promise to repay made by the defendant, but this promise was obviously fictitious, the promise being implied in law in order to bring the case within the action of *indebitatus assumpsit.* The defendant was held liable, not in contract, but in *quasi-contract,* that is, as if there were a contract, and the obligation imposed on the defendant was so imposed in order to prevent the unjust enrichment of the defendant at the expense of the plaintiff.[7]

By 1760 actions for money had and received had increased in number and variety, and Lord Mansfield C.J., in a familiar passage in *Moses* v. *Macferlan,*[8] sought to rationalize the action for money had and received, and illustrated it by some typical instances.[9] Recovery of money paid under mistake of fact is an important example, frequently discussed in modern cases, of claims falling within the second class of claims mentioned above, but, for the present purpose, we are concerned primarily with claims falling within the first class, that is, claims for the recovery of money paid for a consideration which has failed. Causes of action of the latter kind "were assumed to be common-place by Holt C.J. in *Holmes* v. *Hall*[10] in 1704".[11]

The quasi-contractual claim for recovery of money on the ground of failure of consideration was limited to the case of

& Sons Limited. London 1944. An instructive review by H. C. Gutteridge appeared in (1945), 61 L.Q. Rev. 97.

[7] See HOLDSWORTH, HISTORY OF ENGLISH LAW, vol. 8 (1926) 92 *ff.* (*The extension of indebitatus assumpsit to remedy cases of unjust enrichment*). For the continuation of the story, see vol. 12 (1938) 542 *ff.*

[8] (1760) 2 Burr. 1005, at p. 1012: see also at p. 1008.

[9] See Lord Wright in the *Fibrosa* case, [1943] A.C. 32, at pp. 61 *ff.* As to Lord Mansfield, see also HOLDSWORTH, *op. cit.*, note 7, *supra.*

[10] (1704), Holt 36.

[11] Lord Wright, [1943] A.C. 32, at p. 61.

total failure of consideration,[12] and in *Chandler* v. *Webster* it was held that the failure was not total in the case of money paid under a contract originally valid but subsequently frustrated, because the parties were only discharged from performance due since the frustration, and that accrued obligations were not affected. The House of Lords held in the *Fibrosa* case that if the buyer had received no part of the benefit of the seller's performance, the failure of consideration was total, and therefore the buyer was entitled in quasi-contract to the return of his down payment.[13]

The first two sub-sections of s. 1 of the Law Reform (Frustrated Contracts) Act, 1943,[14] are as follows:

> 1.—(1) Where a contract governed by English law has become impossible of performance or been otherwise frustrated, and the parties thereto have for that reason been discharged from the further performance of the contract, the following provisions of this section shall, subject to the provisions of section two of this Act, have effect in relation thereto.
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> (2) All sums paid or payable to any party in pursuance of the contract before the time when the parties were so discharged (in this Act referred to as "the time of discharge") shall, in the case of sums so paid, be recoverable from him as money received by him for the use of the party by whom the sums were paid, and, in the case of sums so payable, cease to be so payable:
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> Provided that, if the party to whom the sums were so paid or payable incurred expenses before the time of discharge in, or for the purpose of, the performance of the contract, the court may, if it considers it just to do so having regard to all the circumstances of the case, allow him to retain or, as the case may be, recover the whole or part of the sums so paid or payable, not being an amount in excess of the expenses so incurred.

I have already said something[15] about the introductory words of sub-s. 1 — "Where a contract governed by English law" — which constitute an innovation in legislation, in that the scope of the statute is defined by reference to a rule of the conflict of laws. These words are described by Williams[16] as a "juristic blunder", but Gutteridge[17] says this is "rather strong language in the circumstances." It is true that there is some opinion in favour of the view that in the conflict of laws the law governing remedies for unjust enrichment is the law of the

[12] *e.g.*, *Whincup* v. *Hughes* (1781), L.R. 6 C.P. 78.
[13] See p. 54, *supra*.
[14] For the complete text of the statute, see pp. 56 *ff.*, *supra*.
[15] See pp. 58 *ff.*, *supra*.
[16] *Op. cit.* (*supra.*, note 6) 19.
[17] (1945), 61 L.Q. Rev. 98

place where the alleged unjust enrichment occurs,[18] and therefore might be different from the proper law of the contract. It would appear, however, that if the alleged unjust enrichment results from the frustration of a contract, it is a convenient and desirable rule that the law governing the contract should also be the law governing the question whether there has been unjust enrichment and the extent to which a remedy is available to avoid the consequent injustice.

In effect sub-s 2 has affirmed the doctrine of the *Fibrosa* case, subject to a proviso which is designed to prevent the injustice which, as pointed out in that case,[19] might result if the seller were compelled to return the whole of the down payment.

Sub-s. 2 is not limited, however, to the case of total failure of consideration, and in this respect it notably enlarges the field of remedy for unjust enrichment. If, for example, some small part of the consideration has been furnished by the seller, the injustice of permitting the buyer to retain the down payment is almost as great as in the case of total failure of consideration, but no remedy would be available to the seller under the doctrine of the *Fibrosa* case. The terms of sub-s. 2 seem clearly to cover the case of partial failure of consideration, subject to the proviso. It is also subject of course to sub-s. 1, that is, it applies only to a case in which a contract "has become impossible of performance or been otherwise frustrated", and in other cases the old rule still prevails that there can be no recovery on the ground of partial failure of consideration.

Quantum Meruit

Sub-s. 3 of s. 1 of the Law Reform (Frustrated Contracts) Act, 1943, is as follows:[20]

> 1.—(3) Where any party to the contract has, by reason of anything done by any other party thereto in, or for the purpose of, the performance of the contract, obtained a valuable benefit (other than a payment of money to which the last foregoing subsection applies) before the time of discharge, there shall be recoverable from him by the said other party such sum (if any), not exceeding

[18] The RESTATEMENT OF THE CONFLICT OF LAWS provides:
§ 452. The law of a place where a benefit is conferred determines whether the conferring of the benefit creates a right against the recipient to have compensation.
§ 453. Where a person is alleged to have been unjustly enriched, the law of the place of enrichment determines whether he is under a duty to repay the amount by which he has been enriched.

[19] See p. 55, *supra*.

[20] Governed by sub-s. 1, already quoted.

> the value of the said benefit to the party obtaining it, as the court considers just, having regard to all the circumstances of the case and, in particular,—
>
> (a) the amount of any expenses incurred before the time of discharge by the benefited party in, or for the purpose of, the performance of the contract, including any sums paid or payable by him to any other party in pursuance of the contract and retained or recoverable by that party under the last foregoing subsection, and
>
> (b) the effect, in relation to the said benefit, of the circumstances giving rise to the frustration of the contract.

The foregoing sub-section breaks new ground, in the sense that it relates to a different branch of the law of quasi-contract or unjust enrichment from that which was involved in the *Fibrosa* case. Some historical introduction to the topic of *quantum meruit* would seem to be justified in order to explain the purpose and scope of the legislation.

Early in the seventeenth century the scope of the action of *indebitatus assumpsit*, theretofore limited to claims for liquidated debts unconditionally payable, as expressed in various common counts, was extended to include claims for unliquidated sums, as, for example, for services rendered on request without mention of a specific price (*quantum meruit*) or for goods sold and delivered without mention of a specific price (*quantum valebant*), the defendant's promise to pay being an actual promise implied in fact.[21] Thus what we may call the original meaning of a claim on a *quantum meruit* was a claim for the value of complete performance as regards which the parties had failed to fix the amount to be paid.

On the other hand, as a general rule, a promisee was not[22] entitled to sue on a *quantum meruit* if the defendant had promised to pay a specified lump sum conditionally on complete performance and the plaintiff had only partly performed; that is, a promisor is not under a duty of immediate performance until the condition of his promise has been fulfilled.[23] In some circumstances, however, the plaintiff may be entitled, either in contract or in quasi-contract, to recover the value of his part performance.

If the promisor has received the benefit of part performance and elects to accept that benefit when he might have rejected it he is under a contractual duty to pay for what he has received. An obvious example is the case in which a seller has delivered

[21] See HOLDSWORTH, HISTORY OF ENGLISH LAW, vol. 3 (1923) 446 *ff.*; STREET, FOUNDATIONS OF LEGAL LIABILITY (1906), vol. 3, pp. 185–188.

[22] HOLDSWORTH, *op. cit.*, vol. 8 (1926) 75, 76.

[23] RESTATEMENT OF CONTRACTS, §250, and comment thereon.

goods not complying with the contract description, and the buyer, instead of exercising his privilege of rejecting the goods (the delivery of which *ex hypothesi* does not fulfil the condition of the buyer's promise), elects to accept them and thereby assumes the contractual duty of paying for them, subject to his right of action or counterclaim against the seller for breach of his promise.[24] The buyer is bound by a new implied promise, a promise implied in fact from his acceptance of the goods. In cases other than the sale of goods, and sometimes even in sale of goods cases, it may be impossible for the promisor to reject or restore the benefit received, and in that event some basis for an implied promise to pay for the benefit other than the mere retention of the benefit must be sought.[25] If in the circumstances a promise to pay is implied, it is sometimes said that the plaintiff is entitled to recover on a *quantum meruit*. This use of the expression *quantum meruit* may be described as a secondary, but still contractual, sense, as distinguished from its original sense, already mentioned, in the case of recovery of the value of services rendered or goods delivered under a contract in which no specific price is mentioned.

Passing now over the borderline between contractual *quantum meruit* and quasi-contractual *quantum meruit*, we arrive at the case in which the promisor has prevented or rendered impossible the fulfilment of the condition of his promise. In that event the promisor is obliged to pay the value of what he has received.[26] This is *quantum meruit* in a third sense. In order that the claim against the promisor might be brought within the scope of the action of *indebitatus assumpsit*, the obligation of the defendant was formerly expressed in terms of an implied promise, but this promise was a pure fiction,[27] a promise implied in law as distinguished from the promise implied in fact in the cases already mentioned. The necessity for expressing the defendant's obligation in terms of a fictitious promise having disappeared with the abolition of the ancient forms of action, the obligation

[24] The result is stated in confusing terms in the Sale of Goods Act, 1893, s. 11 (1) (a) (b) (c), in which the word "condition" is used in the novel sense of a promise by the seller, whereas what is meant is a promissory condition of the buyer's promise that is, a condition of the buyer's promise the fulfilment of which is promised by the seller. As to the expression "promissory condition", see Corbin, *Conditions in the Law of Contract* (1919), 28 Yale L.J. 739, p. 745, in SELECTED READINGS ON THE LAW OF CONTRACT (N.Y. 1931) 871, at p. 877, and ANSON ON CONTRACTS (5th American edition, 1930, ed. Corbin) § 358.

[25] *Sumpter* v. *Hedges*, [1898] 1 Q.B. 673.

[26] *Mavor* v. *Pine* (1825), 3 Bing, 285; *Planché* v. *Colburn* (1831), 8 Bing 14.

[27] *Cf.* note 7, *supra*.

may now be expressed as a duty imposed by law for the purpose of preventing the unjust enrichment of the defendant at the expense of the plaintiff. Other examples of quasi-contractual *quantum meruit* are afforded by the cases in which goods are delivered or services are rendered under an unenforceable or invalid contract.[28]

We have now reached the limit of quasi-contractual *quantum meruit* according to English common law. If a contract is frustrated by reason of supervening impossibility of performance not due to the fault of either party, as, for example, by destruction of the subject matter[29] or other circumstances rendering complete performance impossible, the promisor is excused from further performance.[30] So, in the case of a promise requiring personal performance by the promisor, the promisor is excused by disabling illness,[31] and if the promisor dies, his personal representative is excused. But, before the coming into force of s. 1 (3) of the Law Reform (Frustrated Contracts) Act, 1943,[32] English law did not say that a promisor who was excused, by reason of impossibility, from performing his promise, was also excused from performing the condition of the other party's promise so as to become entitled to recover the value of his part performance of the condition. Thus, if *A* promises to pay *B* a lump sum conditionally on *B*'s completing certain work, and *B* dies before completing the work, *B*'s personal representative is not, at common law, entitled to recover for the value of the work done,[33] but, it would appear, might now recover under s. 1 (3) of the statute of 1943. Again, if *A* promises to pay to *B*

[28] *Lawford* v. *Billericay R.D.C.*, [1903] 1 K.B. 772 (contract of non-trading corporation not under corporate seal); *Scott* v. *Pattison*, [1923] 2 K.B. 723 (contract unenforceable under the Statute of Frauds); *Craven-Ellis* v. *Canons*, [1936] 2 K.B. 403 (contract of corporation made by unqualified directors); *cf.* Wright, comment on *Craven-Ellis* v. *Canons* (1936), 14 Can. Bar Rev. 758; *Friedmann, The Principle of Unjust Enrichment in English Law* (1938), 16 Can. Bar Rev. 243, at pp. 250 *ff.*, 378; Denning, *Quantum Meruit: the Case of Craven-Ellis* v. *Canons* (1939), 55 L.Q. Rev. 54.

[29] The case of the frustration of a contract for the sale of specific goods by reason of the perishing of the goods is the subject of a provision of the Sale of Goods Act: see below under the heading *The Excepted Cases*.

[30] *Taylor* v. *Caldwell* (1863), 3 B. & S. 826. The proposition stated in that case that both parties were excused is a "shorthand" way of stating the result that one party was excused by reason of impossibility of performance and the other was excused by reason of total failure of consideration. *Cf.* my review of McELROY, IMPOSSIBILITY OF PERFORMANCE (1942), 20 Can. Bar Rev. 268, at p. 269.

[31] *Robinson* v. *Davison* (1871), L.R. 6 Ex. 269; *Poussard* v. *Spiers and Pond* (1876), 1 Q.B.D. 410.

[32] Quoted above. For the complete context of the sub-section, see the text of the statute, *supra*, pp. 56 *ff.*

[33] *Cutter* v. *Powell* (1795) ,6 T.R. 320.

a lump sum on the completion of work to be done by *B* on *A*'s premises, and after part of the work has been done *A*'s premises are destroyed by fire, *B* is not, at common law, entitled to recover the value of the work done. As Blackburn J., delivering the judgment of the Exchequer Chamber, said:[34]

> —the plaintiffs, having contracted to do an entire work for a specific sum, can recover nothing unless the work be done, or it can be shown that it was the defendant's fault that the work was incomplete, or that there is something to justify the conclusion that the parties have entered into a fresh contract.

The result in the case last mentioned would apparently not be affected by s. 1 (3) of the statute of 1943, because the defendant received no benefit from the plaintiff's part performance, but in other circumstances, for example, if the destruction of the defendant's premises was partial and the defendant received the benefit of the plaintiff's part performance, the plaintiffs might, under the statute, recover the value of the benefit notwithstanding that the plaintiff was unable to complete his promised performance. Again, if the contract had been severable and had provided for payment in instalments as the work was done, the plaintiffs might at common law have recovered the amounts of the accrued instalments,[35] and the statute contains a special provision applicable to these circumstances.[36]

The effect of s. 1 (3) of the statute may be stated more generally, namely, that in any case of frustration of a contract by reason of circumstances rendering it impossible for one party to complete the performance which is the condition of the other person's promise, the latter is obliged to pay the value of the benefit received by him. This is subject, however, to s. 2 (3) of the statute,[37] under which effect is to be given to any provision of the contract which "is intended to have effect in the event of circumstances arising which operate, or would but for the said provision operate, to frustrate the contract, or is intended to have effect whether such circumstances arise or not."[38]

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[34] *Appleby* v. *Myers* (1867), L.R. 2 C.P. 651, at p. 661.
[35] *Stubbs* v. *Hollywell Ry. Co.* (1867), L.R. 2 Ex. 311.
[36] See s. 2 (4), quoted *supra*, p. 58.
[37] Quoted *supra*, pp. 57–58.
[38] A contractual provision of this kind was in question in *Robbins* v. *Wilson & Cabeldu Ltd.* (1944), 60 B.C.R. 542, [1944] 4 D.L.R. 663, [1944] 3 W.W.R. 625, cited by me, *supra*, p. 56, and subsequently discussed by Gordon, *supra*, p. 165, and Tuck, *supra*, pp. 253, 256 *ff.*, 261. As to the "implied term" theory and other theories of the frustration of contracts, discussed by Tuck, see also Wright, review of WEBBER, EFFECT OF WAR ON CONTRACTS, (1941), 19 Can. Bar Rev. 224.

The Excepted Cases

It is provided by the Law Reform (Frustrated Contracts) Act, 1943, as follows:[39]

> 2.—(5) This act shall not apply—
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> (a) to any charterparty, except a time charterparty or a charterparty by way of demise, or to any contract (other than a charterparty) for the carriage of goods by sea; or
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> (b) to any contract of insurance, save as is provided by subsection (5) of the foregoing section; or
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> (c) to any contract to which section seven of the Sale of Goods Act, 1893 (which avoids contracts for the sale of specific goods which perish before the risk has passed to the buyer) applies, or to any other contract for the sale, or for the sale and delivery, of specific goods, where the contract is frustrated by reason of the fact that the goods have perished.

There may be legitimate differences of opinion as to the desirability of some one or more of these exceptions. It is arguable that for the sake of uniformity of legislation they should be accepted and re-enacted *in toto* in the common law provinces of Canada. Some observations on each of the exceptions are, however, added below, chiefly by way of references to the various opinions already expressed in published comments on the statute by English writers. It would appear that the retention of the exceptions, some of them not justified on principle, may possibly furnish the courts with more troublesome problems than would be presented if the whole of sub-s. 5 of s. 2 were omitted so as to compel the courts to struggle with problems of unjust enrichment in the cases mentioned in that sub-section, and to attempt to apply to those cases the remedial provisions of sub-ss. 2 and 3 of s. 1. If the reason for excepting any of the three cases from the operation of the statute is merely that the law is settled in those cases, so as to exclude remedies for unjust enrichment, perhaps the sooner the law is unsettled the better.

Exception (a) adopts the recommendation of the Law Revision Committee[40] in making the statute applicable to the recovery back of hire paid in advance under a time charterparty or under a charterparty by way of demise, but inapplicable to the recovery back of advance or prepaid freight under a voyage charterparty, or to the recovery of freight *pro rata itineris*. The reasons given by the Committee are not especially convincing, as it admits that the settled law which it is unwilling

[39] For the complete text of the statute, see *supra*, pp. 56–58.
[40] Appendix B, *supra*, p. 52.

to disturb is unsatisfactory. The exception is vigorously criticized by Williams,[41] whereas Gutteridge[42] accepts it philosophically because the rule relating to prepaid freight is "perfectly well understood by men of business" and "accepted by them," and McNair[43] merely speculates on the possibility that the exception does something more than to preserve the old-established law as to advance freight and freight payable *pro rata itineris*.

As to exception (b), Williams[44] says that it is "difficult to see why contracts of insurance are excluded," whereas Gutteridge[45] says: "As regards the rule that no part of an insurance premium is recoverable when once the risk has attached there are no grounds for regarding this as inequitable. The insurer has no claim to an increase of premium in case the risk should have become enhanced during the currency of the policy and the assured cannot have it both ways." McNair,[46] without adverse comment, explains the effect of the exception, and his explanation may usefully be read along with his explanation of s. 1 (5) of the statute.[47]

Exception (c) — relating to contracts for the sale of specific goods — is the most troublesome of the exceptions, because the common law background is especially complicated.

McNair[48] gives some examples of cases which appear to be covered by paragraph (c), his introductory explanation being as follows

> The ground for the express exclusion of these contracts, an exclusion which may well be provided *ex abundanti cautela*, would appear to be that the consequences of their frustration are adequately taken care of by the existing law. The exclusion was probably suggested by Viscount Simon's discussion of *Rugg* v. *Minett*[49] in his *Fibrosa*[50] speech.

On the other hand, Williams[51] introduces a terrifying exposition of the existing law and criticism of the statutory exception, as follows:

> *Paragraph* (c). This seems to be a somewhat involved way of saying that the Act does not apply to any contract for the sale of specific

[41] *Op. cit.* (*supra*, note 6) 72–80, elaborately stating the present law.
[42] In a review of Williams' book (1945), 61 L.Q.Rev. 97, at p. 98.
[43] (1944), 60 L.Q. Rev. 170, 171.
[44] *Op. cit.* (*supra*, note 6) 80.
[45] (1945), 61 L.Q. Rev. 99.
[46] (1944), 60 L.Q. Rev. 172.
[47] (1944), 60 L.Q. Rev. 167; *cf.* the explanation of s. 1 (5) by Williams, *op. cit.* (*supra*, note 6) 56–58. The text of s. 1 (5) is quoted, *supra*, p. 57.
[48] (1944), 60 L.Q. Rev. 172, 173.
[49] (1809), 11 East 110.
[50] [1943] A.C. at pp. 48, 49.
[51] *Op. cit.* (*supra*, note 6) 81.

goods that perish, whether the risk passed to the buyer before the date of the perishing or not.

Again this restriction upon the scope of the Act is to be regretted I shall try to show that (i) when the consideration wholly fails or is wholly rendered, the restriction is unnecessary in all cases except one, and that in this one case, and also (ii) where the consideration partially fails, the restriction has the effect of preserving the unsatisfactory features of the previous law. Moreover I shall try to show, in commenting upon specific words and phrases in the paragraph, that the limits of the restriction are ill-defined and are likely to cause difficulty.

Gutteridge,[52] while paying tribute to the depth of Williams' learning and the amazing versatility which he displays, adds that it "is not possible to share all the doubts which are expressed or to appreciate all the difficulties which are adumbrated" in Williams' book. He does admit, however, that paragraph (c) "may possibly prove to be the most fertile source of any litigation which the Act may engender, since those who are debarred from obtaining redress under the Sale of Goods Act may seek to obtain it by resorting to the later statute."

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[52] (1945), 61 L.Q. Rev. 98.