

# 2

## Certainty of terms and intention

### Introduction

#### Contractual Certainty

If businessmen are often not overly-concerned with the niceties of offer and acceptance it follows that their contracts may not be complete in every respect. The parties may reach an agreement *in principle* but prefer to rely on experience from previous dealings, business practice and goodwill to determine their respective rights and liabilities, rather than on the precise wording of a formal, written and all-embracing contract. Accordingly, as businessmen tend to record their agreements in ‘crude and summary fashion’, the law’s overall policy is to uphold bargains where possible, rather than being ‘too astute or subtle in finding defects’ (*Hillas & Co. Ltd v Arcos Ltd* (1932) 147 LT 503, 514, *per* Lord Wright).

Nevertheless, the law will expect the parties to fix the boundaries of their own obligations and not paternalistically intervene to *create* a contract on their behalf. In many ways this creates a rebuttable presumption that, if an essential term is missing from an agreement, a court will assume that negotiations remain ongoing, i.e. the parties have not yet shown an intention to be legally bound. For example, in *Baird Textile Holdings Ltd v Marks & Spencer plc* [2001 EWCA 274, [2002] 1 All ER (D) 352 the two parties had established a long-standing relationship of dealing with each other which the defendants had unexpectedly terminated. The claimant argued that the defendants were contractually obliged to purchase garments from them ‘in quantities and at prices which in all the circumstances were reasonable’. However, in the absence of any objective criteria for assessing that quantity or price, the Court of Appeal concluded that no such contract existed (see also *British Steel Corporation v Cleveland Bridge & Engineering Co Ltd* [1984] 1 All ER 504).

In seeking to clarify and enforce agreements the law must therefore tread a middle line, avoiding wanton destruction of agreements on one side or the imaginative creation of bargains on the other (compare *Hillas* (*supra*) with *Scammell (G) & Nephew Ltd v Ouston* [1941] AC 251). At present, in line with the general policy of upholding bargains, the courts have tended to (a) ignore meaningless clauses if they add nothing to an otherwise complete agreement (see *Nicolene Ltd v Simmonds* [1953] 1 QB 543), (b) enforce an agreement where one party is under a duty to resolve the uncertainty (see *David T Boyd v Louis Louca* [1973] 1 Lloyd's Rep 209), (c) refer to previous dealings and trade practices (see *Hillas* (*supra*)), and, (d) resolve vagueness by reference to custom (see *Shamrock SS Co. v Storey & Co.* (1899) 81 LT 413).

The real difficulty arises where parties have attempted to allow for fluctuating economic conditions by introducing a variable provision into their agreement, e.g. date of payment and delivery to be fixed from 'time to time in the future'. Such a provision may be regarded by the courts as 'an agreement to agree' and be so uncertain as to be incapable of enforcement (see *May & Butcher v R* [1934] 2 KB 17n; *Smith v Morgan* [1971] 1 WLR 803). Nevertheless, as the courts are reluctant to strike-down provisions which are intended to have legal effect, they may uphold some 'agreements' even if further terms are to be agreed by the parties (see *British Bank for Foreign Trade v Novinex* [1949] 1 KB 623), especially where they have inserted a binding arbitration clause lest they fail to reach agreement on those terms (see *Foley v Classique Coaches Ltd* [1934] 2 KB 1) and/or agree the criteria for resolving any uncertainty (see *Brown v Gould* [1972] Ch 53). On this latter point, more recent case-law has introduced a certain degree of confusion. In *Sudbrook Trading Estate Ltd v Eggleton* [1983] 1 AC 444 the relevant mechanism for resolving the price within a lease agreement broke down—the price was to be determined by two valuers, one nominated by each side, but the lessor refused to nominate a valuer. By this time a substantial part of the contract had been performed. The House of Lords held that since the nomination of valuers was only a *mechanism* for fixing a fair price (rather than an essential *criterion* for determining the price), the court could substitute its own machinery for calculating a fair price. In truth, separating the process for ascertaining the contract price from the criteria being used in that process is fraught with difficulties as the two so often overlap. Consequently, it is not surprising to find that subsequent courts have sought to distinguish *Sudbrook*. For example, in *Gillatt v Sky Television Ltd* [2000] 2 BCLC 103 the disposal of a shareholding was to occur at 'the open market value . . . as determined by an independent chartered accountant' (who was never appointed). The Court of Appeal held that the machinery was integral and essential to the final determination of price (as there was no definition of 'open market value'); in addition, it had failed because the claimant had not acted in accordance with its terms and so could not thereupon claim that the machinery meant nothing and should be replaced by an assessment of the court. This reasoning was followed by the Court of Appeal in *Infinetland Ltd v Artisan Contracting Ltd* [2005] EWCA Civ 758, [2005] All ER (D) 236.

*Letters of intent* cause problems with certainty. Here the sender of the letter states that he intends to contract with the recipient and the latter may act in reliance on the letter in commencing performance. It is quite possible to establish a certain, binding

contract in such cases (see *Trollope & Colls Ltd v Atomic Power Constructions Ltd* [1963] 1 WLR 333; *Wilson Smithett & Cape (Sugar) Ltd v Bangladesh Sugar and Food Industries Corporation* [1986] 1 Lloyd's Rep 378). Similarly, letters of comfort may be either binding contracts or informal and uncertain assurances resting entirely upon business goodwill (see *Kleinwort Benson Ltd v Malaysia Mining Corporation Berhad* [1989] 1 WLR 379).

Finally, in *Walford v Miles* [1992] 2 AC 128, the House of Lords considered the status of a 'contract to negotiate' the sale of a business in which the parties were 'locked out' from negotiating with any other parties. It was held that no contract existed as there was no specified length within which negotiations were to be concluded (see *May & Butcher, supra*); nor could this uncertainty be resolved by implying a duty to negotiate in good faith as this ran counter to the adversarial nature of contract negotiations. Nevertheless, the argument that the *Walford* decision implicitly recognized that a purely negative lock-out arrangement, for a specific period of time, constituted an enforceable contract was subsequently recognized in *Pitt v PHH Asset Management Ltd* [1993] 4 All ER 961. Moreover, in *Petromec Inc v Petroleo Brasileiro SA Petrobras (No. 3)* [2005] EWCA Civ 891, [2006] 1 Lloyd's Rep 121, where an existing contract already existed, it was held that an express duty to negotiate (in good faith) the additional costs of upgrading the agreed level of performance was enforceable as the contract provided for an explicit right to such upgrading.

### Contractual Intent

As well as the other elements required for the formation of a contract, there must be an intention to create legal relations (ICLR), this being assessed objectively. In commercial contracts there is a presumption of ICLR and the onus is on the party who asserts that no legal effect is intended to rebut the presumption. The parties may expressly deny any intent but, in the absence of such an express denial, rebuttal is extremely difficult (see *Edwards v Skyways Ltd* [1964] 1 WLR 349; *Rose & Frank Co. v J R Crompton & Bros Ltd* [1923] 2 KB 261; *Jones v Vernons Pools Ltd* [1936] 2 All ER 626). The litigation in *Kleinwort Benson Ltd v Malaysia Mining Corporation Berhad* [1989] 1 WLR 379, is important. The first instance decision applied the presumption of ICLR ([1988] 1 WLR 799) but the Court of Appeal's reasoning appeared to allow a circumvention of the presumption rather than its rebuttal by first asking whether the parties had evidenced a *general* intent to create a contract (or, at the very least, a promissory intent). As the court answered that question in the negative, there was no reason to consider the applicability of the general presumption of ICLR regarding commercial agreements.

Conversely, many social and domestic agreements lack sufficient intent to make them legally binding (see *Balfour v Balfour* [1919] 2 KB 571), although this presumption can be rebutted, where spouses have reached an agreement, on proof of the requisite legal intent (see *Pearce v Merriman* [1904] 1 KB 80; *Merritt v Merritt* [1970] 1 WLR 1211). Similarly, other domestic arrangements can involve difficulties of intention (see *Jones v Padavatton* [1969] 1 WLR 328; *Simpkins v Pays* [1955] 1 WLR 975; *Parker v Clark* [1960] 1 WLR 286).

The Court of Appeal has implicitly questioned whether the presumptions regarding commercial and domestic agreements represented the correct starting point, preferring to concentrate on the ‘seriousness’ of any promise as the primary indicator of intent (see *Edmonds v Lawson* [2000] QB 501). Clearly an interesting parallel can be drawn with the earlier decision in *Kleinwort Benson* (see above), which itself is reinforced by *Baird Textile Holdings Ltd v Marks & Spencer plc* (*supra*), in which a long-term supplier relationship was not legally binding as the defendant had deliberately avoided entering into a formal contract.

Finally, a statement inducing a contract may be a ‘mere puff’ and the test is one of intention (see *Weeks v Tybald* (1605) Noy 11; *Carlill v Carbolic Smoke Ball Co. Ltd* [1893] 1 QB 256). Similarly, intention determines whether a statement is a term of the contract or a ‘mere representation’ (see *Heilbut, Symons & Co. v Buckleton* [1913] AC 30).

### Question 1

It is a basic axiom of English law that, although the courts cannot make a contract for the parties, they will strive to uphold a bargain wherever possible.

Discuss.



### Commentary

This question calls for an understanding of certainty of terms and, to a lesser extent, intention to create legal relations. Students must be able to make an accurate analysis of the lengths to which the courts will go in enforcing contracts. The decisions tend to make technical distinctions but students should be aware of the important substantive issues raised in *Kleinwort Benson Ltd v Malaysia Mining Corporation Berhad* [1989] 1 WLR 379 and *Walford v Miles* [1992] 2 AC 128.



### Answer plan

- What is meant by the rule that a contract must have certainty of terms?
- To what extent will the courts strive to uphold a bargain and seek to clarify the terms of the contract?
- To what extent can the parties leave a term of the contract to be agreed upon in the future?
- Do recent decisions adopt a more rigorous approach than formerly in demanding that intent and certainty must unite to forge an intelligible and enforceable undertaking?

## Suggested answer

It is the parties who make their own contract and fix its boundaries whilst the courts enforce the bargain thus created. It follows that if the agreement is uncertain and imprecise the courts will be unable to enforce it and may decide that it also lacks the requisite intention to create legal relations. For example, in *Scammell (G) & Nephew Ltd v Ouston* [1941] AC 251 there was an agreement to acquire goods ‘on hire-purchase terms’ but the House of Lords held that this could not be a binding contract as it was ‘so vaguely expressed that it cannot, standing by itself, be given a definite meaning’ (see also *Jacques v Lloyd D George & Partners* [1968] 1 WLR 625).

Nevertheless, the courts have traditionally sought to uphold bargains where possible and, as Lord Wright emphasized in *Hillas & Co. Ltd v Arcos Ltd* (1932) 147 LT 503, have not been ‘too astute or subtle in finding defects’, even where the commercial agreement has been crudely drafted by businessmen. In *Hillas*, the plaintiffs agreed to buy from the defendants a quantity of Russian softwood timber of a particular quality, the agreement containing an option for the plaintiffs to buy more timber at a later date but with no particulars of size or quality. When the plaintiffs sought to exercise the option, the defendants objected that the clause was vague and indeterminate and provided, at best, a basis for future negotiations. The House of Lords held that, having regard to previous dealings, there was sufficient intention to be bound and the agreement could be rendered certain by referring to the parties’ previous dealings and the normal practice in the timber trade. *Hillas* is illustrative of the courts’ willingness to imply terms that make commercial sense of the agreement, but an alternative method of resolving uncertainty is to delete a meaningless, subsidiary provision, leaving the remainder of the contract complete and enforceable. In *Nicolene Ltd v Simmonds* [1953] 1 QB 543, the defendant agreed to sell a quantity of steel bars to the claimant on terms which were clear except for the statement that ‘we are in agreement that the usual conditions of acceptance apply’. It was held that the words were meaningless but that they did not destroy the contract as they were severable, leaving the core of the obligation intact. As Denning LJ stated, if the opposite conclusion had been reached, defaulters would be ‘scanning their contracts to find some meaningless clause on which to ride free’. However, the *Nicolene* principle cannot function if the meaningless clause is intended to govern an undertaking *central* to the agreement, for then its uncertainty may vitiate the whole agreement.

The courts also look favourably on agreements which, although leaving some issue to be resolved in the future, provide the machinery or criteria for its resolution. Thus, an agreement will not fail simply because it provides for the resolution of outstanding issues by arbitration, and, in *Brown v Gould* [1972] Ch 53, an option to renew a lease ‘at a rent to be fixed having regard to the market value of the premises’ was binding in that it provided a criterion, albeit somewhat elusive, for resolving the vagueness. This approach was extended in *Sudbrook Trading*

*Estate Ltd v Eggleton* [1983] 1 AC 444 where a lease gave the tenant an option to purchase the premises ‘at such price as may be agreed upon by two valuers’ who were to be appointed by each party. The landlord refused to appoint a valuer but the House of Lords held that the option did not fail for uncertainty. The substance of the undertaking was an agreement to sell at a reasonable price, to be determined by valuers, and the extra stipulation that each party should nominate a valuer was ‘subsidiary and inessential’. But a note of caution should be added here. Whilst a court may choose to follow this analysis and substitute its own procedures for resolving uncertainty where the original machinery breaks down (e.g. ascertaining the price with the help of expert evidence—(see *Res Malpas* [1985] Ch 42), the more recent Court of Appeal decisions in *Gillatt v Sky Television Ltd* [2000] 2 BCLC 103 and *Infiniteland Ltd v Artisan Contracting Ltd* [2005] EWCA Civ 758, [2005] All ER (D) 236 suggest that such discretion is severely circumscribed as it is not always easy to separate the process by which an agreed price is to be reached (e.g. *Sudbrook*), from the essential criteria for determining that price (which remain inviolate in accordance with *May & Butcher v R* [1934] 2 KB 17—*infra*).

Finally, the courts have not been deterred from clarifying uncertainty where there is a determinate intention of the parties to form a binding contract but the vagueness in question has related to a fundamental obligation which the parties have deliberately left open-ended. This may occur where both parties are reluctant to enter into a finalized contract for a lengthy period of time, preferring to leave questions such as the price and manner of payment for later consideration and agreement. Are such agreements enforceable? In *May & Butcher v R* [1934] 2 KB 17n, an agreement for the sale of tentage provided that the price, dates of payment and manner of delivery should be agreed ‘from time to time’. On these facts, the House of Lords held that the agreement was incomplete as it amounted to nothing more than an agreement to agree in the future. If the agreement had been silent on these issues, the House thought that s. 8(2) of the *Sale of Goods Act 1893* (now s. 8(2) *Sale of Goods Act 1979*) might have applied meaning that a reasonable price should be paid, but the parties had shown that this was not their intention by providing for a further agreement. However, *May & Butcher* has been distinguished in several cases and, although it is difficult to make generalizations in this area, it seems that if the courts identify substantial agreement between the parties (referring to existing commercial practice where relevant) some points may be left for future resolution without vitiating the agreement. For example, in *Foley v Classique Coaches Ltd* [1934] 2 KB 1, the plaintiff owned a petrol station and adjoining land which he agreed to sell to the defendants on condition that they should agree to buy all the petrol for their coach business from him. The agreement regarding the petrol was executed and provided that it was to be supplied ‘at a price to be agreed by the parties in writing and from time to time’. The land was conveyed and the petrol agreement was acted on for three years but the defendants then repudiated it arguing that it was incomplete in relation to the

price of the petrol. The Court of Appeal held that the agreement was enforceable and that, consequently, the defendants must pay a reasonable price for the petrol. The most influential factors in the decision appeared to be that the contract had been acted upon for several years (see also *Trentham Ltd v Archital Luxfer* [1993] 1 Lloyd's Rep 25) and that the petrol agreement formed part of a linked bargain with the sale of the land, the defendants paying a price for the land which no doubt reflected the fact that they would buy their petrol from the plaintiffs.

However, more recent decisions have cast doubt upon the whole notion that the courts, as described above, will strive to uphold the parties' bargain where possible. In *Kleinwort Benson Ltd v Malaysia Mining Corporation Berhad* [1989] 1 WLR 379 the defendant issued a letter of comfort to the plaintiff in respect of a loan of £10 million to one of the defendant's subsidiary companies. Comfort letters possess varying degrees of formality but here the letter was negotiated between the parties and contained the statement by the defendant that it was its 'policy to ensure that the business of [the subsidiary] is at all times in a position to meet its liabilities to you under the above arrangements'. The defendant argued that neither party intended this statement to be contractually binding. At first instance, it was held that the plaintiff should succeed as: (a) the presumption of intention to create legal relations which applies to commercial contracts had not been rebutted by the defendant; (b) the wording was unambiguous and 'crystal clear'; and (c) the undertaking was of crucial importance and the plaintiff had acted in reliance on it in advancing the loan. The Court of Appeal reversed the decision and held that the wording of the undertaking did not amount to a contractual promise and thus the question of rebutting the presumption of intention to create legal relations never arose. Moreover, the court considered that the statement was only one of present intention in that the defendant's 'policy' could change in the future. The Court of Appeal's reasoning appears to ignore the presumption of intention and, if that presumption has not been rendered redundant by the decision, it is very difficult to ascertain in which circumstances it will apply. The second decision, *Walford v Miles* [1992] 2 AC 128, concerned the enforceability of a contract to negotiate. The plaintiff and defendant were negotiating the sale of the defendant's business and an agreement was reached by which the plaintiff would provide the defendant with a letter of comfort from the plaintiff's bankers confirming that a loan would be granted to the plaintiff. In return, the defendant agreed to terminate any negotiations with third parties and not to consider any alternative offers. The comfort letter was provided but the defendant withdrew from the negotiations and sold the business to a third party. The House of Lords held that the plaintiff's action must fail. The House considered that it was possible to have an enforceable lock-out contract (i.e. an agreement *not* to negotiate with third parties) provided the duration of the 'lock-out' was specified expressly, but that the parties could never be 'locked-in' by such an arrangement to negotiate positively as this would amount to an uncertain and unenforceable contract to negotiate.

*Kleinwort* and *Walford* illustrate perfectly the *laissez-faire* principles of self-reliance and judicial non-interventionism. It is suggested that the decisions ignore English law's basic tenet that agreements should be validated wherever possible and, in so doing, potentially encourage bad faith in commercial transactions. Consequently the recent Court of Appeal decision in *Petromec Inc v Petroleo Brasileiro SA Petrobras (No. 3)* [2005] EWCA Civ 891, [2006] 1 Lloyd's Rep 121 is to be welcomed. The facts involved a provision within an *existing* contract that required the parties to negotiate in *good faith* the costs of upgrading that contract (note that the possibility of upgrading was permitted and acknowledged within the contract). This provision was held to be enforceable. Longmore LJ was not put off by the difficulty of determining the result of 'good faith' negotiations (i.e. in calculating the costs of upgrading) as this would be a relatively easy task. Moreover, whilst withdrawing from negotiations in 'bad faith' (i.e. a potential breach of contract) would be difficult to ascertain, to ignore that possibility would unfairly undermine the expressed and reasonable intentions of the parties. Thus, whilst the traditional notion that courts seek to uphold rather than destroy contracts has, to some extent, come under attack in recent times, the sentiments expressed in the original question still retain great resonance in the law today.

## Further Reading

### Case-notes

*Walford v Miles* [1992] 2 AC 128

Brown, 'The Contract to Negotiate: A Thing Writ in Water' [1992] JBL 353

*Kleinwort Benson Ltd v Malaysia Mining Corp. Bhd* [1989] 1 WLR 379 (CA)

Brown, 'The Letter of Comfort: Placebo or Promise?' [1990] JBL 281

### Articles

Hedley, 'Keeping Contract in its Place—*Balfour v Balfour* and the Enforcement of Informal Agreements' (1985) 5 OILS 391

Hepple, 'Intention To Create Legal Relations' [1970] CLJ 122

Gilliker, 'Taking comfort in certainty: to enforce or not to enforce the letter of comfort' [2004] LMCLQ 219

Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1977) 113 LQR 433