LAW REFORM COMMISSION OF BRITISH COLUMBIA

REPORT ON THE NEED FOR FRUSTRATED CONTRACTS LEGISLATION IN BRITISH COLUMBIA

(PROJECT NO. 8)

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TO THE HONOURABLE LESLIE R. PETERSON, Q.C.
ATTORNEY-GENERAL FOR BRITISH COLUMBIA

The Law Reform Commission of British Columbia has the honour to present the following:

REPORT ON THE NEED FOR FRUSTRATED CONTRACTS LEGISLATION IN BRITISH COLUMBIA

(Project No. 8)

This Report completes the Commission's Study on Frustrated Contracts Legislation, which is Project No. 8 in the Commission's Approved Programme.

Under the common law doctrine of frustration, contracts that become impossible to perform will in certain circumstances be regarded as terminated and the parties relieved from performing further obligations. However, the common law does little to provide redress to a party who performed obligations before the contract was frustrated and who received insufficient consideration in return to compensate him for what he has done.

Legislation was enacted in England in 1943 in an attempt to provide a statutory solution to the problems created by the application of the doctrine. The English legislation was adopted, with some minor modifications, as a model Act by the Conference of Commissioners on Uniformity of Legislation in Canada in 1948. Since then, a number of Canadian jurisdictions have enacted it.

In 1959, the then Attorney-General of this Province, the Honourable R.W. Bonner, Q.C., introduced in the Legislature a bill containing the provisions of the *Uniform Act*. It was apparently his intention not to proceed with the bill until there had been an opportunity to receive comment on it, particularly from the legal profession. Little comment was received and the proposed legislation was never proceeded with.

Although the need for frustrated contracts legislation may not appear to be as pressing as a good many other matters requiring reform, the Commission felt that, since this subject had already been the subject of draft legislation in this Province, this piece of "unfinished business" could well be included in its programme. It appeared to be a subject which could be studied and reported on reasonably readily while our major studies in other areas were getting under way.

Preliminary study suggested, however, that the *Uniform Act* has shortcomings in principle and that its provisions, while a slight improvement on the English legislation, are inclined to be obscure. While generally a strong argument can be made in favour of uniformity, the Commission felt there was so much room for improvement that it should tackle the problem of suitable legislation afresh.

In this Report, the Commission recommends a statutory solution based on principles of restitution and apportionment of loss. A draft enactment is included.

CHAPTER I INTRODUCTION

1. *The Need for Legislation*

The purpose of frustrated contracts legislation is to provide a fair system of rules for sorting out the positions of the parties to a contract that has been prematurely brought to an end by the application of the common law doctrine of frustration.

Contracts may become impossible to perform for a variety of reasons beyond the control of the contracting parties. War, the destruction of the subject-matter of the contract by fire, the enactment of legislation making performance of the contract illegal, a labour dispute, and the restriction of credit, are examples of events that may prevent parties, through no fault of their own, from performing obligations under their contracts.

Express provision may be made in a contract to deal with the position of the parties should such events occur. On the other hand, the contract may be silent. It is then that what is called the common law doctrine of frustration may come into operation. In certain circumstances, and not necessarily in all the illustrations given above, the contract will be regarded as coming to an end. Where the doctrine applies to a contract, the parties are excused from performing obligations which were due to be performed after the occurrence of the frustrating event. The contract is void from the time of frustration.

Once a contract is frustrated, questions arise as to how the parties should be treated with respect to what has gone on before the frustrating event occurred. What should happen when one party has paid the full, or part of, the contract price? What should happen where the other party has carried out a substantial part of his obligations - say, for the construction of a building, the manufacture of machinery, or the sale or carriage of goods?

The common law, as it has developed in England and the other Commonwealth jurisdictions, has not provided satisfactory solutions to these questions and remedial legislation has been necessary. Under the common law as it exists in the United States, on the other hand, the parties receive reasonably fair treatment under the doctrine. of unjust enrichment, a doctrine that had been given a *much* more liberal development by the American courts than the Commonwealth courts.

The Commission is thus concerned with whether the Province of British Columbia needs frustrated contracts legislation and, if it does, with the principles upon which the remedial statute should rest and what form it should take. The study is not, with some qualifications, concerned with the doctrine of frustration itself but rather with the consequences of the application of the doctrine. However, in order to appreciate the problems arising from its application, it is obviously necessary to know something about the doctrine. The common law position on the doctrine, as it exists in this Province, is outlined in Chapter II.

2. *History of Legislation*

In 1948 the Conference of Commissioners on Uniformity of Legislation in

Canada recommended a model *Frustrated Contracts Act*.[1] This model statute, which is set out in Appendix C, will be referred to as the *Uniform Act* in this Report.

The provisions of the *Uniform Act* were based on the English *Law Reform (Frustrated Contracts) Act, 1943*,[2] a statute enacted to implement the recommendations of the Seventh Interim Report of the English Law Revision Committee.[3] That Report is contained in Appendix A and the English statute in Appendix B.

The *Uniform Act* was adopted in Alberta[4], Manitoba,[5] New Brunswick,[6] Ontario[7] and Prince Edward Island[8] in 1949, and in Newfoundland[9] and both the Territories[10] in 1956. Thus British Columbia, Nova Scotia and Saskatchewan are the only three common law provinces that have not adopted the model statute.

Other Commonwealth jurisdictions have enacted similar legislation. New Zealand[11] did so on 1944 and the State of Victoria[12] in Australia followed suit somewhat later, in 1959. The Victoria statute, which has some significant differences, is set out in Appendix D.

A concordance of the provisions of the Uniform, English and Victoria enactments is provided in Appendix E.

In this Province, a bill containing the provisions of the *Uniform Act* was introduced in the Legislature by the then Attorney-General, the Honourable R.W. Bonner, Q.C., on March 16, 1959.[13] It was not apparently his intention to proceed with the bill until there had been an opportunity to receive comment upon it, particularly from the legal profession. Little comment was received by the Attorney General, although the Civil Justice Sub-Committee of the British Columbia Branch of the Canadian Bar Association approved the proposed legislation "*in toto*".[14] The bill was

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[1] *See* Appendix G of Proceedings of the 1948 Conference, at p. 73.

[2] 6 & 7 Geo. VI, c. 40.

[3] Cmd. 6009. (1939.)

[4] S.A. 1949, c. 44. *See* R.S.A. 1955, c. 123.

[5] S.M. 1949, c. 21. *See* R.S.M. 1970, c. F190.

[6] S.N.B. 1949, c. 19. *See* R.S.N.B. 1952, c. 94.

[7] S.O. 1949, c. 36. *See* R.S.O. 1960, c. 157.

[8] S.P.E.I. 1949, c. 15. *See* R.S.P.E.I. 1951, c. 66.

[9] S.N. 1956, No. 29.

[10] O.N.W.T. 1956 (2nd Sess.), c. 1: O.Y.T. 1956, c.1. *See also* R.O.Y.T. 1958, c. 48.

[11] 7 & 8 Geo. VI, No. 20.

[12] Queen Eliz. II, No. 6359.

[13] Bill (No. 48).

[14] *See* Minutes of the Civil Justice Committee, June 26, 1959 and May 26, 1960.

not given second reading nor was it ever re-introduced at a subsequent session of the Legislature, although it was prepared for introduction at the 1960 session as Bill 4. The 1959 bill, together with a list of minor drafting changes that were made in adopting the *Uniform Act* provisions, is set out in Appendix F.

There appear to be no reasons on the record as to why this proposed legislation was dropped. It may be that there was some dissatisfaction with the substance or form of the contents. There would have been, in the view of this Commission, as will be explained later, a number of good reasons for such dissatisfaction. While the Commission has no reservations about the need for frustrated contracts legislation, it considers that the *Uniform Act* has shortcomings in principle and that its provisions, while an improvement on the English legislation, are inclined to be obscure. The English legislation, from which the *Uniform Act* is drawn, was not well thought out or well-drafted. Comment by many distinguished legal writers bears this out.

In this Report, the Commission concludes that there should be frustrated contracts legislation, based on principles of restitution and apportionment of loss. A draft statute, set out in Appendix G, is recommended.

3. *Bibliography*

For a detailed explanation of the doctrine of frustration reference should be made to such standard works as Cheshire and Fifoot's *The Law of Contract*,[15] *Chitty on Contracts*,[16] and *Halsbury's Laws of England*.[17] The subject is also discussed in many of the texts dealing with sale of goods, carriage of goods by sea, building contracts and private international law. Canadian case law may be found, of course, in the Canadian Abridgement.

The Seventh Interim Report of the Law Revision Committee gives the background of the 1943 English legislation,[18] as do the Parliamentary Debates.[19]

An excellent small book was written by Professor Glanville Williams on the English legislation shortly after its enactment.[20] For a commentary on the statute, one should also refer to *Halsbury's Statutes of England*.[21]

The Legal Periodical Index for the period 1940-1970 lists some one hundred articles on the topic of frustration. A short selection of articles and notes that the Commission considers most relevant are:

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[15] 7th ed. 1969, at p. 507 *et seq.*

[16] 23rd ed., 1968, vol. I, at p. 1261 *et seq.*

[17] 3rd ed., 1954, vol, 8. *See also* R. G. McElroy, *Impossibility of Performance,* 1941 (ed. By Glanville L. Williams).

[18] Cmd. 6009. (1939.)

[19] *See* H. L. Deb., June 29, 1943, 135 *et seq.*; H. C. Deb. July 23, 1943, 1342 *eq seq.*, and July 28, 1741 *et seq.*

[20] *Law Reform (Frustrated Contracts) Act, 1943* (1944).

[21] 3rd ed. (1969)

"The Law Reform (Frustrated Contracts) Act, 1943," by A.D. McNair.[22]

"A Note on The Law Reform (Frustrated Contracts) Act, 1943," by Glanville Williams.[23]

"A Review of Glanville Williams' book *The Law Reform (Frustrated Contracts) Act, 1943*," by H.C. Gutteridge.[24]

"Frustrated Contracts: The Need for Law Reform," by Dean John D. Falconbridge.[25]

"The Choice of Law in Statutes," by J.H.C. Morris.[26]

"Reform of the Law of Frustrated Contracts in Saskatchewan," by Julien Payne.[27]

"The Frustrated Contracts Act," by Ivan Feltham.[28]

Reference should also be made to the Proceedings of the Conference of Commissioners on uniformity of Legislation in Canada for the years 1945 to 1948, 1955 and 1957.

4. *Consultation*

In order to assist it in making proposals for reform that are both relevant and sound, the Commission has adopted a general policy of inviting comment and criticism on its research and analysis before submitting its formal Report to you. The chief means by which the Commission will carry out this process of consultation is the circulation of working papers to those persons, groups or organizations who would find the subject under study of interest.

In September, 1970, the Commission completed a working paper on the subject dealt with in this Report. The working paper was forwarded for comment to the Commercial, Insurance and Maritime Law Subsections of the British Columbia Branch of the Canadian Bar Association, and a number of law professors and other persons having a special interest in the matter under study. The Subsections appointed special study groups to review the working paper. On November 7, 1970, a meeting of representatives of the Subsections, four law professors, and Commission members and staff took place at the Commission offices for a very fruitful exchange of views. Subsequently, the Commission received submissions from the Subsections.

The response to the working paper was of great assistance to the Commission in reaching its final conclusions. In a number of instances, the Commission revised its views from those it had expressed as tentative conclusions in the working paper.

The Commission is grateful to those who responded to its request for

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[22] 60 L.Q.R. 160 (1944).

[23] 7 M.L.R. 66 (1944).

[24] 61 L.Q.R. 97 (1945).

[25] 23 Can. Bar Rev. 43 and 469 (1945).

[26] 62 L.Q.R. 170 (1946).

[27] 25 Sask. Bar Rev. 94 (1960).

[28] 18 Advocate 5 (1960).

comment. In particular, the Commission would like to thank the Chairmen of the Commercial, Insurance and Maritime Law Subsections - Professor David Huberman, Mr. J. Lyle Woodley, and Mr. Jon L. Jessiman - for the time and work which they and their colleagues put into considering the Working Paper. Mr. Ivan Robertson, Mr. Kenneth C. MacKenzie, and Mr. Vernon R. Hill, Q.C., deserve special thanks in this respect.

In addition, the Commission was able to obtain the services of Professor Christopher Carr of the University of British Columbia Faculty of Law to advise the Commission in reaching its final conclusions and assist in the preparation of the Report. We are indebted to him for his invaluable help.

CHAPTER II THE DOCTRINE OF FRUSTRATION

1. *The Doctrine's Development*

Until the middle of the last century parties to a contract were not relieved from performing their obligations merely because the contract became impossible to perform, even though the event making performance impossible was beyond the control of the parties or was unforeseeable. Even if that event were the outbreak of war, the parties were still regarded by the law as bound to perform.

This harsh rule did not apply, of course, where the parties had expressly provided in the contract that their contractual obligations should terminate on the happening of the particular event. It was because the parties could, if they chose, expressly guard against contingencies that might make the contract impossible to perform that the common law refused to interfere. Thus, if the parties did not make an express stipulation to protect themselves, they placed themselves under an absolute liability to perform.

However, in the 1863 English decision of *Taylor* v. *Caldwell*[1] it was held that parties might be relieved from liability where there could be said to be an *implied* condition in the contract that such should be the case. In *Taylor* v. *Caldwell*, there was a contract for the use of a music hall on four specific nights. The music hall burnt down after the contract was signed but before the night of the first performance. The judge reasoned that the parties must be taken to have understood from the beginning that the fulfilment of the contract depended on the continued existence of the music hall.

Since 1863, there have been many cases dealing out of these decisions there has evolved the doctrine of frustration.

Although the reading into the contract of an implied term was the original basis of the doctrine of frustration, it is now the better view that the doctrine rests, not on the supposed intention of the parties, but that seems reasonable and just where there is a radical change in the obligations contracted.

The theory of the implied term has often been criticized. Chitty, for example says[2] it is artificial and often fictitious in its operation, since there would seldom be a genuine common intention to terminate the contract upon the occurrence of the particular event in question. The parties in the normal case have not foreseen the event, and even if they had, they would probably have "sought to introduce reservations, or qualifications, or compensations".

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[1] 3 B. & S. 826; 129 R.R. 573.

[2] Op. It., at vol. 1, at p. 591.

Cheshire and Fifoot state: [3]

> To attempt to guess the arrangements that the parties would have made at the time of the contract, had they contemplated the event that has now unexpectedly happened, is to attempt the impossible. Instead, the courts refuse to apply with contracts that have become impossible to perform and on the courts acting independently and imposing a solution the doctrine of frustration unless they consider that to hold the parties to further performance would, in the light of the changed circumstances, alter the fundamental nature of the contract.

The now prevailing position was clearly stated by Lord Radcliffe in a 1956 House of Lords decision, *Davis Contractors Ltd.* v. *Fareham U.D.C.*[4]

> By this time it might seem that the parties themselves have become so far disembodied spirits that their actual persons should be allowed to rest in peace. In their place there rises the figure of the fair and reasonable man. And the spokesman of the fair and reasonable man, who represents after all no more than the anthropomorphic conception of justice, is and must be the court itself. So perhaps it would be simpler to say at the outset that frustration occurs whenever the law recognizes that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. *Non haec in foeders veni.* It was not this that I promised to do.

This was a case in which a contractor had agreed to build seventy-eight houses within eight months for a *fixed sum*. The work took twenty-two months to complete for a number of reasons beyond the control of the contractor, the chief being a lack of skilled labour. The contractor argued that owing to the long delay, the contract ceased to be applicable and that he was entitled to be paid on a *quantum meruit* (value of the work done) basis, rather than the contract price. His argument was rejected for reasons that are discussed later.

The *Davis* case has been approved in the British Columbia[5] and Ontario[6] courts, as well as in the Supreme Court of Canada.[7]

The theoretical basis for the doctrine of frustration has been developed entirely by the English courts. The courts of other Commonwealth common law jurisdictions have applied the doctrine as part of the common law appropriate to their particular jurisdictions. The British Columbia cases are reviewed later in this chapter.

2. *Extent of the Doctrine's Operation*

The doctrine is still under development by the courts and the law is not as clear as it might be. There are, nevertheless, certain clearly established requirements that

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[3] *Op. cit.*, at p. 510.

[4] [1956] A.C. 696 at pp. 728-729

[5] *Electric Power Equipment Ltd.* v. *RCA Victor Co. Ltd.* (1963) 41 D.L.R. (2d) 727. On appeal, frustration is not discussed. *See* 46 D.L.R. (2) 722.

[6] *Dryden Construction Co. Ltd.* v. *Hydro Electric Power Commission of Ontario* (1957), 10 D.L.R. (2d) 124.

[7] *Peter Kiewit Sons Company of Canada Ltd.* v. *Eakins Construction Ltd.*, [1960] S.C.R. 36.

must be met before the doctrine will be applicable. These are:

1. A supervening event, the occurrence of which is not expressly provided for in the contract:

2. The supervening event must not have been caused by the fault of either party to the contract:

3. The supervening event must have resulted in a radical alteration in the obligations of the parties; and

4. There must be more than just hardship, inconvenience or material loss to the party seeking relief.

The last two requirements are closely related and it is not always an easy matter to decide whether a particular situation is sufficiently severe to pass these tests. The problem appears to arise with some frequency with respect to construction contracts where unexpected conditions (such as a labour shortage,[8] difficult terrain[9] or bad weather[10]) cause delay or additional expense. In these cases, the courts will not apply the doctrine merely because one of the parties has made a bad bargain or assumed obligations more onerous than had been contemplated.

At what point would the courts apply the doctrine? Suppose a contract cannot be performed because of a strike? Will it make any difference if the strike is by the employees of the contracting party or is one in which he has no direct involvement? What if the contracting party's line of credit was cut off or reduced by his bank so as to disable him from fulfilling contractual obligations? Would the court's view be influenced by whether the bank's action was based on Government monetary policy or on the ground that the contracting party had become a bad credit risk?

Until the law is further developed by the courts, the answers to these questions can only be speculative. At present, it is safe to say that the courts are reluctant to interfere with the contractual obligations of the parties. Insofar as the effect of strikes is concerned, there seems surprisingly little law. In two English cases in the late nineteenth century, strikes did not provide an excuse for non-performance.[11] In both these cases, it was the employees of the contracting parties that were on strike, although it is clear that the courts considered the strikes as being outside the control of the employers.

There has been some doubt as to the applicability of the doctrine to leases. This problem is discussed later in this chapter.

3. Application in British Columbia

In British Columbia, there have been at least sixteen reported cases where the doctrine has been invoked. Only in a few, however, has the doctrine been applied.

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[8] *Davis Contractors, Ltd.* v. *Fareham U.D.C.*, [1956] A.C. 696

[9] *Dryden Construction Co. Ltd.* v. *Hydro Electric Power Commission of Ontario* (1957), 10 D.L.R. (2d) 124; *Peter Kiewit Sons Company of Canada Ltd.* v. *Eakins Construction Ltd. [1960]* S.C.R. 36.

[10] *Electric Power Equipment Ltd.* v. *RCA Victor Co. Ltd.* (1963), 41 D.L.R. (2d) 727, 46 D.L.R. (2d) 722.

[11] *King and others* v. *Parker* (1876), 34 L.T. 887. *Budgett & Co.* v. *Binnington & Co.*, [1891] 1 Q.B. 35.

It may be helpful to set out briefly the fact situations in order to give a picture of the kind of circumstances in which it has been thought the doctrine would apply in this province. Of the sixteen cases, fifteen went to the British Columbia Court of Appeal, six to the Supreme Court of Canada and one to the Privy Council.

(a) *Doctrine applied*

1. *McKenna* v. *McNamee*[12] (1888)

X had a contract with the Government of British Columbia for the construction of the Esquimalt Graving Docks. X failed to carry on the work to the satisfaction of the Government and the contract was taken out of its hands. X believed that the contract could be reinstated and entered into an agreement with Y to complete the work. The contract with the Government had a prohibition against subletting and Y was aware of this and that the contract had been cancelled. X did its best to have the contract restored but was unsuccessful. Y sued for damages.

Held: X was not liable as there was an implied condition in the contract between X and Y that it would take effect only if the contract between X and the Government was reinstated.

2. *Topping* v. *Marlin*[13] (1910)

T staked out a number of timber limits and agreed to sell fourteen of these to M, who advanced the licence fees, partly in cash and partly by giving notes. A dispute led to a new agreement with fresh notes being made. The government had granted twelve of the licences but refused the other two. M claimed he was entitled to a proportionate reduction of his liability on being sued on one of the notes.

Held: Although the doctrine was applicable, M was still fully liable owing to the fact that the note was payable prior to the time of frustration, i.e., when the Government refused the licences.

3. *Aron* v. *Sproat*[14] (1921)

A contract was made for the moving of a house in the City of Vancouver. The contractor's application for a permit was turned down by the City Engineer.

Held: Action for damages for non-performance of contract dismissed.

4. *Cahan* v. *Fraser*[15] (1951)

An option was given to buy a house near Agassiz. Five hundred dollars were paid for the option and a similar sum to extend the option for a further thirty days. After the extension was given but before it expired there was a violent and extraordinary flooding of the Fraser River Valley, rendering the property inaccessible during the balance of the extended option period for the purpose of taking possession or estimating the amount of the damage.

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[12] (1888), 15 S.C.R. 311.

[13] (1910), 15 B.C.R. 52.

[14] (1921), 29 B.C.R. 194.

[15] [1951] 4 D.L.R. 112.

Held: The doctrine applied to the extended option and the $500 paid for it was recoverable.

4. *McDonald Aviation Co. Ltd.* v. *Queen Charlotte Airlines Ltd.*[16] (1952)

A plane was leased to do fishery patrol service for a period of four months at a minimum rental payable monthly. After three weeks of the lease had run, the plane crashed on Cracroft Island in Johnstone between Vancouver Island and the Mainland. There was no negligence found by the court.

Held: The party to whom the plane was rented was not liable for rent payable after the crash took place.

(b) *Doctrine assumed to apply*

1. *Australian Dispatch Line* v. *Anglo-Canadian Shipping Co.*[17] (1940)

Outbreak of war between China and Japan in 1937 would have made it extremely difficult to fulfil the terms of the charter requiring a ship to sail from Vancouver to Shanghai.

Held: The parties had treated the contract as frustrated and were bound by their conduct in so doing.

2. *Robbins* v. *Wilson Z. Cabeldu Ltd.*[18] (1944)

A car was sold to a car-dealer, who pursuant to the agreement of sale paid off the balance owing on the car and was to retain the remainder of the purchase price to be applied against the price of a new car when the vendor wished to buy one. The vendor applied for a new car but was unable to obtain from the Motor Vehicle Controller (established under wartime regulations) the necessary permit to purchase.

Held: Assuming the doctrine applied, the vendor was not entitled to recover an amount equivalent to the credit owing to the wording of the contract.

(c) *Doctrine not applied*

1. *Vancouver Breweries Ltd.* v. *Dana Fullerton*[19] (1915)

X had leased a licensed hotel to Y for ten years, covenanting to make such alterations as were required to maintain the licence. X assigned his interest in the lease to Z who failed to maintain the premises as required by the covenant. The licence was not renewed and Y refused to pay future rent.

Held: Y was liable for the rent (although he probably had a claim for damages for breach of contract).

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[16] [1951] 1 D.L.R. 195 and 582, [1952] 1 D.L.R. 291.

[17] [1939] 2 D.L.R. 56; [1940] 4 D.L.R. 104.

[18] [1944] 3 W.W.R. 255 and 625.

[19] (1915), 25 D.L.R. 508; 26 D.L.R. 665.

2. *Meeker* v. *Nicola Valley Lumber Co.*[20] (1917)

Under an agreement for sale of a mill-site property in the Nicola Valley, final payment was to be made when the vendor obtained title from the Crown. The purchaser took possession and subsequently made it impossible for the vendor to obtain the Crown grant by deciding to build his mill on a different site which was more favourably situated. The Crown's practice was not to grant lands for industrial sites except when the lands were to be used for the industrial purpose contemplated.

Held: The purchaser was liable for the balance owing, the vendor being excused from making title as a condition precedent to its right to payment.

3. *Carr* v. *Berg*[21] (1917)

X was an insurance broker who wrote up "hail" insurance policies in Alberta, premiums on these policies being paid for partly in cash and partly in notes. A was the general manager of an insurance company in Vancouver and X was the general agent of the company in Alberta. A entered an option with Z by which the latter was to sell A $50,000 worth of notes at a discount. (The notes were not then in existence as it was the beginning of the season.) A asked X to resign and as an inducement offered him the option. X accepted the offer but when the time came for delivery of the notes Z only had $10,000 worth.

Held: X was entitled to damages for breach of contract based on the profit he would have made had the $50,000 worth of notes been delivered to him.

5. *Grant Smith and Co.* v. *Seattle Construction and Dry Dock Co.*[22] (1918)

There was a lease of a dry dock for use in the construction of a breakwater in the City of Victoria. There was a covenant to insure but insurance was not taken out owing, it appears, to the high cost of obtaining it. An insurance company had turned down an application owing to certain structural alterations in the dry dock. The dry dock collapsed and became a total wreck. It was argued that the covenant to insure was impossible to perform.

Held: Liability existed on the covenant to insure.

5. *Canadian Government Merchant Marine* v. *Canadian Trading Co.*[23] (1922)

There was a contract to provide two ships, which were under construction, to carry lumber from Vancouver to Australia. The ships were not ready at the time called for in the contract owing to delays caused by disputes between the parties to the contract for construction of the ships and to a strike, or threatened strike.

Held: Damages were awarded for breach of the contract of affreightment.

6. *B.C. Mills, Tug and 24 Barge Co. Ltd.* v. *Kelley*[24] (1923)

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[20] (1917), 31 D.L.R. 607; 39 D.L.R. 497.

[21] (1917), 38 D.L.R. 176; 49 D.L.R. 693.

[22] (1919), 44 D.L.R. 90; 48 D.L.R. 172.

[23] (1922), 67 D.L.R. 485; 68 D.L.R. 544.

[24] [1922] 2 W.W.R. 792; [1923] 1 W.W.R. 597.

A contract for towage at $300 per day contemplated delays caused by bad weather. In fact there was six weeks of bad weather and the contract was cancelled, none of the towing having been done.

Held: The contract price was payable.

7. *Galt* v. *Frank Waterhouse & Co. of Canada Ltd.*[25] (1943)

A small coastal steamship was chartered for eighteen months requiring the charterer to pay the operating expenses including the cost of the annual overhaul. When the contract had nine months to run, a government inspection revealed that dry-rot had set in and that the ship required virtual reconstruction before an operating certificate could be given. The expense would have been at least $20,000 instead of the annual $3,000 to $5,000 which had been expended in previous years.

Held: Although the doctrine did not apply, the expression "cost of annual overhaul" could not include the cost of virtual reconstruction in the circumstances.

8. *Peter Kiewit Sons' Company of Canada Ltd.* v. *Eakins Construction Ltd.*[26] (1960)

There was a sub-contract for pile-driving made under a contract for the construction of part of the Second Narrows Bridge across Vancouver harbour. Problems not originally contemplated difficulties in the terrain, resulting in great additional expense.

Held: In view of the terms of the contract, there was no room for applying the doctrine.

9. *Electric Power Equipment Ltd.* v. *RCA Victor Co. Ltd.*[27] (1964)

There was a contract for the installation of power and communication cable at various sites in northern British Columbia and the Yukon. The contractor's (Electric Power's) obligations were based on "working conditions normally encountered during the months of September and October", although provision was made for additional costs to be assumed by RCA Victor should snow or temperature conditions hinder the progress of the work. Work did not get under way until November when weather conditions were such that construction was slower and more expensive than anticipated. The work was not completed and RCA Victor took over under a default clause in the contract. The contractor claimed $105,314.51.

Held: In view of the terms of the contract, there was no room for applying the doctrine.

4. *Some problems relating to the doctrine*

(a) *Does it need modification?*

(i) *Generally*

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[25] [1943] 3 D.L.R. 708; [1944] 2 D.L.R. 158.

[26] [1960] S.C.R. 361.

[27] (1963) 41 D.L.R. (2d) 727; 46 D.L.R. (2D) 722.

There are two questions

1. Is there a need for statutory modification of the doctrine?

2. If there is such a need, should the Commission's study of frustrated contracts legislation be the medium for making proposals for such modification?

It may help to answer the second question first. As mentioned at the beginning of the Report, the object of our study has been to examine the desirability of having legislation which will provide a fairer sorting out process than the common law does, once a contract is frustrated. The study has been concerned with the law relating to the consequences of frustration and not with the doctrine of frustration itself.

This does not mean, of course, that the Commission should balk at making proposals for change if the doctrine has obvious serious defects. It does indeed have a suggestion to make with respect to the doctrine's applicability to leases.

However, to undertake a full review of the doctrine would be a much larger project than the Commission contemplated. The infinite variety of contractual situations and of circumstances that might be considered as giving rise to frustration would require a careful and time-consuming study for which the Commission simply does not have the resources at this time, having regard to other areas of the law requiring reform. It is a question of priorities.

The appropriate occasion for such a study would be when contract law generally comes under review.

Even so, after what might be called a preliminary survey of the law, the Commission has not been convinced that there is any need for a general statutory modification of the doctrine. True, the doctrine has its critics. Some may say it is too narrow in its application. Others may say that the courts should be given statutory guidelines in order to bring clarification, particularly with respect to the effect of such matters as labour disputes or credit restrictions on the performance of contractual obligations. For the time being, however, the Commission would leave the further development of the doctrine to the courts.

We agree with Professor George F. Curtis, Dean of the Faculty of Law at the University of British Columbia and a long-time teacher of contract law, who has written us[28]

> ... with a doctrine so relatively new there is much to be said for retaining the flexibility of judicial experimenting.

(ii) *Leases*

Here, the Commission feels that there is an obvious defect in the doctrine that could be readily dealt with now.

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[28] Letter to the Commission dated June 9, 1970.

Whether or not the doctrine extends to leases has caused considerable controversy, as is pointed out at length in Chitty[29] and Cheshire and Fifoot.[30] The problem turns on the nature of a lease which has both contractual and property aspects. Under the common law, a lease confers an interest in land. A tenant acquires what is called a nonfreehold estate. If he has rented a house for a year at a monthly rent and after a month the house burns down, the lease would not be regarded as frustrated and he would be responsible for the remaining rent in the absence of any agreement to the contrary. Although the house has been destroyed, the subject-matter of the contract, which is the interest in land, is said to be still in existence. If, however, the land disappeared - say, as a result of an earthquake or flood, it is thought that the lease would be frustrated. In a recent Ontario case, expropriation was held to frustrate an agreement for a lease.[31]

The question has been resolved in British Columbia insofar as residential tenancies are concerned by recent changes made in the *Landlord and Tenant Act*.[32] Under the new Part II of the Act, which deals with residential tenancies, there are two relevant sections:

> 35. For the purposes of this Part, the relationship of landlord and tenant is one of contract only, and a tenancy agreement does not confer on the tenant an interest in land.
>
> 41. The doctrine of frustration applies to tenancy agreements.

Section 41, in particular, is a step forward in clarifying the law on this point. The Commission believes that there would be merit in placing this provision in Part I of the Act so that it would extend to all leases. It so recommends.

The Commission also proposes, in the event frustrated contracts legislation is enacted in this Province, that this provision be broadened so as to ensure that such legislation would apply to leases. This was provided for in the Ontario landlord and tenant statute, as follows:[33]

> 87. The doctrine of frustration applies to tenancy agreements and *The Frustrated Contracts Act* applies thereto.

Accordingly, the Commission recommends:

1. *The* Landlord and Tenant Act *should be amended to provide that the doctrine of frustration apply to leases generally; and*

2. *The frustrated contracts legislation later recommended in this* Report *should be made expressly applicable to frustrated leases.*

(b) *Should it be codified?*

There have long been arguments about the advantages and disadvantages of

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[29] *Op. cit.*, vol, 1, at pp. 609-612.

[30] *Op. cit.*, at pp. 518-519.

[31] Re *Dennis Commercial Properties Ltd.* and *Westmount Life Insurance Co.* (1969), 7 D.L.R. (3d) 214.

[32] R.S.B.C. 1960, c. 207, as amended by 1970, c. 18.

[33] R.S.O. 1960, c. 206, as amended 1968/69, c. 58.

codifying the common law. This whole question is a far too difficult and controversial one for the Commission to attempt to resolve here.

The reason for bringing up the question is that codification of the doctrine in a frustrated contracts statute could make that statute much easier to understand. One of the problems with the English and Uniform Acts is that they assume a knowledge of the doctrine of frustration. The doctrine is imported into the legislation by a statement that the enactment applies to contracts that have became impossible of performance or have been otherwise frustrated, and the parties to which for *that reason* have been discharged. One therefore has to look outside the statute at the common law to see if a particular contract has been frustrated. If it has been, one can then apply the statute.

Portions of the common law have been codified from time to time - perhaps the best known examples being the Canadian *Criminal Code* and the *Sale of Goods Act*[34] (copied from England), both of which were enacted at the end of the last century. At the present time the English Law Commission has as part of its programme the codification of contract law generally. So does the New South Wales Law Reform Commission, although it is awaiting the results of the English study before it embarks on this immense project.

The codification of the doctrine of frustration in the proposed frustrated contracts statute has an aesthetic appeal which the Commission has found difficult to resist. It has, however, done so, for the same reasons that it earlier rejected the possibility of a general modification of the doctrine. The very careful study that this would require would not, in the view of the Commission, represent an appropriate allocation of its resources at this time. The English Law Commission has not yet dealt with the doctrine in its codification of the law of contract. If it had, this Commission's position might differ as it would be able to utilize the English body's research and analysis.

However, there is also the question of whether the doctrine ought to be codified at all in its present stage of development. Codification could result in a rigid rule that might within a few years fail to meet the needs of society. As Dean Curtis has stated to us:[35]

> The thing that has struck me about the law of contract is the amount of change that is coming over the law in the last few years and I am fearful that if it gets codified we may find ourselves in the same position as the *Sale of Goods Act*. There is the terrible inertia of a code to stay put and not keep up with modern trends of thought and of need.

The Commission has concluded that it would not be wise to attempt a codification of the doctrine at present. No doubt the occasion will arise when the Commission will be able to consider fully the question of codification generally.

5. *Consequences of the Doctrine's Application*

When a contract is frustrated, it is void from the time of frustration. It remains valid and binding, however, for the period running from the time the contract was made to the time of frustration. Thus the parties to a frustrated contract are bound

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[34] R.S.B.C. 1960, c. 344.

[35] *Op. cit.*

to perform obligations which accrued prior to the moment of frustration but are discharged from having to perform obligations that accrue afterwards.[36]

Suppose, for example, X contracts with Y on September 1, 1970 for the use of a theatre. The contract requires X to pay $2000 on September 1st, a further $3,000 on October 1st, and $4,000 on November 1st. The theatre burns down on October 15th, at which time the doctrine applies. At this point X had paid the $2,000 that was due on September 1st but not the $3,000 that was due on October 1st. X must still pay the $1,000 due on October 1st since it had become payable prior to the date of frustration. But he is excused from paying the $4,000.

This was clearly the position until 1942. Up to that time, X was considered liable for the obligations that accrued prior to frustration, regardless of whether he had received any benefit under the contract. In the above example, suppose that Y's only obligation under the contract had been to provide the use of the theatre during the last week of October. X would never have received any benefit but he would end up $5,000 out of pocket.

In 1942, however, the House of Lords decided in the *Fibrosa* case that, if there was a total failure of consideration, the party who had made a payment might recover it.[37] Thus, applying the Fibrosa case to the illustration, X would not only be excused from paying the $3,000 that became due on October 1st, but he would also be entitled to recover the $2,000 payment of September 1st.

However, the *Fibrosa* case would be of no help to X if there had been partial performance by Y under the contract. If the contract had called for X to have the use of the theatre for two days in early October (as well as the last week in that month) and he had had the use of the theatre during those two days, he could obtain no relief.

In the *Fibrosa* case, an English company had agreed to sell and deliver certain machinery to a company in Poland for a lump sum. Part of the contract price, L1600, was payable in advance, but of this sum only L1000 was in fact paid. Two months later World War II broke out and German occupation rendered performance of the contract impossible. The Polish company (through its London agent) sought the return of the L1000 but the English company refused because it had done considerable work on the machinery.

Prior to the *Fibrosa* case, the principle was simply that the loss must lie where it had fallen and the courts refused to interfere. However, while the House of Lords did lessen somewhat the harshness of the law, as it had been, there were still shortcomings.

Cheshire and Fifoot sum up as follows:[38]

> The rule established by the *Fibrosa* case has thus diminished the injustice of the former law, but since it operates only in the event of a total failure of consideration, it does not remove every hardship. On the one hand, it does not permit the recovery of an advance payment if the consideration has only partly

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[36] *See Krell* v. *Henry*, [1903] 2 K.B. 740 and *Chandler* v. *Webster*, [1904] 1 K.B. 493.

[37] *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour, Ltd.*, [1943] A.C. 32.

[38] *Op. cit.*, at p. 522.

> failed, i.e., if the payer has received some benefit, though perhaps a slender one, for his money. On the other hand, the payee, in his turn, may suffer an injustice. Thus, while he may be compelled to repay the money on the ground that the payer has received no benefit, he may himself, in the partial performance of the contract, have incurred expenses for which he has no redress.

The problem was emphasized by the Lord Chancellor, Viscount Simon, in the *Fibrosa* case. He pointed out that, while the return of money paid[39]

> ... obviates the harshness with which the previous view in some instances treated the party who had made a prepayment, it cannot be regarded as dealing fairly between the parties in all cases, and must sometimes have the result of leaving the recipient who has to return the money at a grave disadvantage. He may have incurred expenses in connection with the partial carrying out of the contract which are equivalent, or more than equivalent, to the money which he prudently stipulated should be prepaid, but which he now has to return for reasons which are no fault of his. He may have to repay money, though he has executed almost the whole of the contractual work, which will be left on his hands. These results follow from the fact that the English common law does not undertake to apportion a prepaid sum in such circumstances ...

This statement, made in the House of Lords in 1942, sums up the law as it appears to be in British Columbia in 1971.

There is an additional point that should be made here. A number of recent cases involving construction contracts appear to have been brought on the assumption that if the contractor can succeed in having the courts hold the contract frustrated, then he, the contractor, would be entitled to receive compensation on a *quantum meruit* (value of the work done) basis.[40] This assumption does not fit in with basic principles as to distribution of loss at common law, as explained above. on this point, it is stated in Hudson's *Building & Engineering Contracts* that:[41]

> It is not clear, however, on what basis a contractor could recover on a *quantum meruit* in respect of work done before the frustration. At common law, the loss fell where it lay, and a contractor was entitled to any progress payments already made or due to him before the frustrating event, but could recover no more, although the value of the work done might exceed the progress payments.

Since in none of the recent cases referred to did the contractor succeed in having the doctrine of frustration applied, the question of whether he would have succeeded in *quantum meruit* had the doctrine applied was not resolved.

Legislative attempts at solving the problems which can arise when a contract is frustrated are described and discussed in the following two chapters. The Commission has, however, no doubt about the need for legislation. It recommends:

> *Legislation should be enacted to provide a fair system of rules for settling the positions of parties to contracts that have been prematurely brought to an end by the application of the common law doctrine of frustration.*

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[39] *Op. cit.*, at p. 615.

[40] *Davis Contractors, Ltd.*, v. *Fareham U.D.C.*, [1956] A.C. 696; *Peter Kiewit Sons Company of Canada Ltd.* v. *Eakins Construction Ltd.*, [1960] S.C.R. 361; *Dryden Construction Co. Ltd.* v. *Hydro Electric Power Commission of Ontario* (1957), 10 D.L.R.(2D) 124; *Electric Power Equipment Ltd.* v. *RCA Victor Co. Ltd.* (1963), 41 D.L.R. (2d) 727 and 46 D.L.R. (2d) 722.

[41] 9th ed. (1965), at pp. 253-254.

CHAPTER III FRUSTRATED CONTRACTS LEGISLATION

1. *The Report of the English Law Revision Committee*

In 1937, the Lord Chancellor referred the following subject to the Law Revision Committee:[1]

> Whether and, if so, in what respect the rule laid down or applied in *Chandler* v. *Webster* (1904) 1 K.B. 493 requires modification, and in particular to consider the observations made thereon in *Cantiare San Rocco, S.A.* v. *Clyde Shipbuilding and Engineering Co., Ltd.* [1924] A.C. 226 by Lords Dunedin and Shaw at pp. 247, 248 and 259.

The Committee's Report, which was presented to Parliament in 1939, is get out in Appendix A of this Report. The recommendations in that Report form the basis of the 1943 English statute on which the *Uniform Act* was modelled.

The Committee's terms of reference were narrow. Its Report states:[2]

> The Committee's terms of reference neither require nor permit it to report on the merits of the doctrine of frustration generally. They are limited to consideration of the rule, incidental to that doctrine as received in English Courts, that after a frustrating event the loss "lies where it falls".

Two members of the Committee expressed disappointment that the Report did not go far enough, stating that they had signed it because the suggested alterations would make the law fairer. They added, however, that:[3]

> The Report contains no recommendation regarding the converse case where the promisee has paid nothing: in this case it appears the loss is still to "lie where it falls". Presumably owing to the limited terms of reference, it is not in the Committee's power to deal with either this question or the other questions which arise on frustration.

The *Chandler* v. *Webster* case,[4] referred to in the terms of reference, involved the hiring of a room for the purpose of viewing the coronation procession of 1902. The total price of L141/15/0 was payable in advance, but only L100 had in fact been paid when the procession was called off. The court held that the 1.100 was not returnable and that the balance was still owing, since the obligation to pay had arisen prior to the time of frustration.

The other case referred to in the terms of reference contained comments that were critical of *Chandler* v. *Webster*. Lord Shaw, for example, described the rule as the "something for nothing" doctrine.[5]

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[1] *Op. cit.*, at p. 3.

[2] *Ibid.*

[3] *Ibid.*, at p. 11.

[4] [1904] 1 K.B. 493.

[5] [1924] A.C. 226 at p. 258.

It should be pointed out that the House of Lords' decision in the *Fibrosa* case[6] came three years after the Committee made its Report.

The Committee recommended that, on frustration of a contract, under which moneys had been paid or were payable prior to the time of frustration, the following rules should apply, except where the parties otherwise agreed:[7]

1. Money paid should be recoverable, subject to a deduction representing a fair allowance for expenditure incurred by the payee in performing his obligations under the contract.

2. Where such a deduction was to be made,

   (a) an allowance for overhead expenses should be included,

   (b) account should be taken of any benefits accruing to the payee by reason of his expenditure, and

   (c) loss of profit should not be taken into account.

3. The "amount recovered" should not exceed the total of the money paid or payable under the contract. It is not clear from the Report what this means. "Amount recovered" could mean the amount recovered by the payer or the amount deducted (or recoverable?) by the payee. The latter position would make more sense and appears to have been adopted by indirection in the proviso to section 1(2) of the English statute.

4. Where a part of a contract had been performed at the moment of frustration and that part of the contract was severable from the remainder of the contracts the proposed rules should

   (a) only apply to that part of the contract that remained unperformed, and

   (b) not affect or vary the price or other pecuniary consideration paid or payable in respect of that part of the contract which has been so performed.

5. In the application of these rules, no regard should be had to amounts receivable under any contracts of insurance.

The solution embodied in these recommendations was preferred over three other possible solutions. These were[8]

1. That the payer should be entitled to the return of all moneys he has paid to the payee,

2. The payer should be entitled to the repayment of all moneys, less the value of any benefits he may have received under the contract, and

3. The payer should be entitled to the repayment of all moneys he has paid to the payee, less one-half of any loss directly incurred by the payee for the purpose of performing the contract.

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[6] [1943] A.C. 32.

[7] *Op. cit.*, at pp. 7-8.

[8] *Ibid.*, at p. 7.

All the solutions considered by the Committee, it should be observed, were to apply only where there had been a payment of money. They do not deal with the situation where work has been performed under a contract before frustration and no moneys had become payable under the contract by that time. The reason for this, as was pointed out by two members of the Committee, was the narrow terms of reference.[9]

The Committee did not go into a lengthy discussion of the various solutions. It felt that it was reasonable to assume that where a payee stipulated for prepayment the payee intended to protect himself against loss. This intention; the Committee concluded, would be satisfactorily carried out if the recommended solution were adopted. As a qualification, the Committee added:[10]

> It is true that the payee though avoiding loss would fail to make the profit which he hoped to gain by the fulfilment of the contract, but in this respect he would be no worse off than the payer who would not obtain the thing contracted for and might fail to obtain the profit he envisaged.

In Appendix B of the Committee's Report, certain special problems relating to freight contracts were dealt with. These are discussed later in this Report.[11]

2. *The English Legislation*

(a) *Its enactment*

On June 22, 1943, the Lord Chancellor, Viscount Simon, introduced in the House of Lords a bill to amend the law relating to the frustration of contracts.[12] The bill passed through the House of Lords and then the House of Commons without change. It became law on August 5, 1943, as the *Law Reform (Frustrated Contracts) Act, 1943*.[13] It is set out in Appendix B of this Report.

In opening the debate on second reading of the bill, the Lord Chancellor, who a year earlier had given the leading judgment in the *Fibrosa* case,[14] stated that:[15]

> If your Lordships have looked at the Bill some of you at first sight may have thought it to be of a rather technical character, but I hope to be able to show very briefly that it is in fact a measure of real importance to the ordinary man and that what we are here proposing to do will be a great improvement in the present law.

The only major criticisms of the bill were made in the House of Commons,[16]

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[9] *Supra*, at pp. 37-38.

[10] *Op. cit.*, at p. 7.

[11] *Infra,* at p. 78.

[12] H.L. Deb., vol. 128, at 1.

[13] 6 & 7 Geo. VI, c. 40.

[14] [1943] A.C. 32.

[15] H.L. Deb., vol. 128, at 136 (June 29, 1943).

[16] H.C. Deb., vol. 291, at 1344-1346 (July 23, 1943) and at 1741 *eq seq.* (July 28, 1943).

where the insurance exception, discussed later in this Report, was attacked. It was also suggested that the legislation should be made retroactive owing to the effect of the war on contracts. However, no amendments were made.

(b) *Basic Principles*

(i) *Introduction*

For a detailed treatment of the English enactment, reference should be made to the texts and articles contained in the bibliography listed in Chapter I of this Report.

In addition, there is an analysis in the following chapter of some of the problems which occur under the statute's Canadian counterpart, the *Uniform Act*.

It is proposed here merely to set out the principles contained in the statute's provisions. In this respect, there is a dearth of case law on the various frustrated contracts Acts. In fact, there appears to be only two reported decisions on any of these enactments - one in Newfoundland and one in the State of Victoria.[17] This would seem to result, not from the clarity of the legislation, which is rather awkwardly drafted and somewhat obscure, but rather from the lack of fact situations which could lead to litigation over the meaning of certain provisions.

(ii) *Application*

The *English Act* applies:

(1) where a contract governed by English law is terminated under the common law doctrine of frustration,[18] and

(2) where, prior to the time of frustration, either,

(a) sums were paid or became payable under; the contract,[19] or

(b) some other valuable benefit was obtained by one party to the contract as a result of anything done in performance of the contract by another party thereto,[20] and

(3) whether or not there has been a total failure of consideration as there was in the *Fibrosa* case, and

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[17] *Parsons Bros. Ltd.* v. *Shea* (1965), 53 D.L.R. (2d) 86; *Lobb* v. *Vasey Housing Auxiliary* (War Widows Guild), [1963] V.R. 239.

[18] 6 & 7 Geo. VI, c. 40, s. 1 (1).

[19] S. 1 (2).

[20] S. 1 (3).

(4) whether or not the frustrated contract was entered into prior to the passage of the Act, so long as the frustrating event occurred on or after July 1, 1943,[21] and

(5) whether or not one of the parties to the contract is the Crown.[22]

The Act does not apply:

(1) to payments made or other acts done under the frustrated contract after the time of frustration,

(2) in respect of obligations that were due to be performed after the time of frustration,

(3) where the parties in their contract have excluded the operation of the statute by providing for the frustrating event,[23]

(4) to that part of the contract which can be properly severed (in circumstances described in the Act) from the part of the contract which has been frustrated,[24]

(5) to three specified exceptions,[25]

(a) voyage charter parties and contracts for the carriage of goods by sea,

(b) contracts of insurance, and

(c) certain contracts for the sale of goods.

(iii) *The Formula*

The Act comes into operation where, prior to the time of frustration, either

(1) sums were paid or became payable under the contract,[26] or

(2) some other valuable benefit was obtained by one party to the contract as a result of anything done in performance of the contract by another party thereto.[27]

These two situations will be treated separately.

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[21] S. 2 (1).

[22] S. 2 (2).

[23] S. 2 (3).

[24] S. 2 (4).

[25] S. 2 (5).

[26] S. 1 (2).

[27] S. 1 (3).

1. *Sums Paid or Payable* - The sums paid may be recovered and the sums payable cease to be payable, subject to an offset for incurred expenses. If the party to whom the sums were paid or payable has incurred expenses before the time of frustration, he may be able to retain sums he has been paid or recover sums payable to the extent of his expenses. However, he has no absolute right to his expenses. It is in the discretion of the court which may allow him to offset up to this extent "if it considers it just to do so having regard to all the circumstances of the case".

Although the right to make this offset is contained in a proviso to the provision that gives the payer relief in connection with sums paid of payable, it has been held that the person seeking to rely on it (or at least on a similar proviso in the State of Victoria Statute) must prove the facts necessary to bring himself within its terms.[28] It had been suggested that, since the right to offset was in the form of a proviso to the payer's right to relief, the onus was on the payer to exclude the proviso's operation. The court disagreed, stating that the proviso took effect as "an independent enactment".

2. *Benefit obtained* - Where one party obtains a valuable benefit (other than money) under the contract as a result of something done in performance of the contract by another party, then the latter may recover from the former the value of the benefit to the party obtaining it. As with the offset claim where moneys have been paid, this right of recovery is subject to the court's discretion. In exercising its discretion in this instance, the court is required to consider

(a) the amount of any of the expenses incurred by the benefited party, including sums paid or payable by him, and

(b) the effect, in relation to the said benefit, of the circumstances giving rise to the frustration of the contract.

It should be observed that the benefit must be *obtained*. Although one party may have incurred considerable expense in performing his obligations, it does not necessarily follow that the other party has obtained a benefit. This may be demonstrated by the circumstances in *Appleby* v. *Myers*:[29]

> X agreed to erect machinery on Y's premises in consideration of a promise to pay a sum of money. An accidental fire destroyed Y's premises and all they contained just when the erection of the machinery was almost complete. Applying the doctrine of frustration, Y was required to pay nothing.

The case occurred sixty years before the English enactment. If the same facts arose again, would X be entitled to some compensation under the statute? This would depend on whether Y had *obtained* a valuable benefit. It might be argued that he had obtained a benefit on the basis that the work had been done, although not completed as the contract required, i.e., that Y obtained a benefit from each act of work done by X in the performance of his contractual obligations. Goff and Jones state that this is the position which should prevail, save in exceptional

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[28] *Lobb* v. *Vasey Housing Auxiliary (War Widows Guild)*, [1963] V.R. 239 at p. 248.

[29] (1867), L.R. 2 C.P. 651.

circumstances.[30] But Cheshire and Fifoot reject that position, pointing out that Y had never received any real advantage and would not have until the contract was completed:[31]

> It is difficult to reconcile this suggestion with the words of the Act. A notional is not a valuable benefit, and the whole tenor of section 1(3) is that the possibility of recovery must be linked with and proportioned to the value of the benefit obtained. Had the legislature desired to provide for such a case as *Appleby* v. *Myers*, it would surely have made it clear that the right of recovery was to depend upon the work done by the plaintiff rather than upon the benefit obtained by the defendant.

The *Appleby* case has been applied in interpreting the Newfoundland statute.[31]

Cheshire and Fifoot say of the particular provision that it is not clear that it "does full justice".

The right to compensation for conferring a valuable benefit extends to situations where the benefit is obtained by a person other than the person from whom compensation is sought.[32] X may enter into a contract with Z, for example, by which z is to do something for the benefit of Y. Z may recover compensation from X (but not Y) under the Act for conferring a valuable benefit on Y.

Expenses-In estimating the expenses incurred, either in an offset claim or valuable benefit claim, a reasonable amount may be included

(1) for overhead expenses, and

(2) for any work or services performed personally by the party.[33]

Insofar as the latter item was provided for, it was apparently thought that it should be made clear that compensation should be payable whether the party did the work himself or incurred an expense by hiring someone to do it on his behalf.[34]

Insurance - As a general rule, in determining what sums ought to be returned or recovered, no account should be taken of any sums that become payable under any contract of insurance by reason of the circumstances giving rise to the frustration.[35]

Williams points out why this should be so:[36]

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[30] *See the Law of Restitution* (1966), at pp. 334-335.

[31] *Op. cit.*, at p. 525.

[31] *Parsons Bros. Ltd.* v. *Shea (1965), 53 D.L.R. (2d) 86.*

[32] 6 & 7 Geo. VI, c. 40, s. 1 (6).

[33] S. 1 (4).

[34] *See* Williams, *op. cit.*, at p. 56.

[35] 6 & 7 Geo. VI, c. 40, s. 1 (5).

[36] *Op. cit.*, at p. 56.

It is settled legal principle that the fact that a plaintiff has insured against a loss must not be allowed to affect any remedy that he would otherwise have against a third party. For this principle there are at least two reasons: (I) as regards the defendant (the third party), the insurance is res inter alios acta, and (ii) any other rule would defeat the insurer's right of subrogation.

(iv) *The Statute and the Committee Report*

It will have been noted that the statute went beyond the recommendations of the Law Revision Committee in one major respect.[37] This was in providing for compensation where a valuable benefit (other than money) had been conferred by one party, regardless of whether money had been paid or payable by another party. The Committee had only recommended that there be compensation for such a benefit where it could be offset against money recoverable by the other party.

The legislation also contained provisions dealing with a number of matters which the Committee did not consider. The Report is silent on the conflicts problem and the exceptions in respect of contracts of insurance and for the sale of goods, matters which are discussed in the following chapter of this Report. There are, in addition, a number of other minor differences but nothing is to be gained by referring to them here.

3. *The English Act as a Model*

(a) *General*

The *Uniform Act*, the New Zealand statute and the State of Victoria statute are all modelled on the *English Act*. There are few changes in substance, but there are considerable differences in arrangement, wording and punctuation.

A concordance of the provisions of the Uniform, English and Victoria statutes is set out in Appendix E. A number of significant differences are noted in the concordance.

(b) *In New Zealand*

New Zealand was the first of the Commonwealth jurisdictions to enact similar legislation. It did so the year following the passage of the *English Act*.

The Frustrated Contracts Act, 1944[38] is virtually identical to the English statute. The word "preceding" is preferred to "foregoing" and in section 3(3) the expression "if any" is placed in brackets rather than being preceded and followed by commas. The title and definition contained in section 3 of the *English Act* are provided for in sections 1 and 2, with the result that the numbering of the New Zealand provisions is different.

(c) *In Canada - The Uniform Act*

(i) *Adoption by the Uniformity Commissioners*

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[37] *Supra*, at p. 45.

[38] N.Z.S. 1944, No. 20.

Interest in Canada in the English statute appears to have been stimulated by an article in the 1945 Canadian Bar Review by Dean John D. Valconbridge of Osgoode Hall Law School.[39]

At the 1945 meeting of the Conference of Commissioners on Uniformity of Legislation in Canada, the topic was on the agenda but was not reached.[40] A report on the subject by the Manitoba Commissioners was included as an Appendix in the published proceedings.[41] In 1946, the Manitoba Commissioners presented the 1945 report and a further report, including a draft act.[42] The Conference decided to refer the matter to the Ontario Commissioners for a report the following year.[43]

In 1947, the Ontario Commissioners reported on the draft *Uniform Act* prepared by the Manitoba Commissioners as follows:[44]

This draft Act follows very closely the *English Act* of 1943. While the wording of the English Act may, in some respects, be cumbersome, and perhaps somewhat lacking in clarity, we are of the opinion that it would be unwise, by reason of the desirability of having uniformity so far as possible between the *English Act* and our *Uniform Act*, to redraft it.

The Ontario Commissioners did, however, recommend that the three exceptions, discussed in the next chapter, should be deleted.[45] The Conference resolved that the draft *Uniform Act*[46]

> ... which follows the language of *The Law Reform (Frustrated Contracts) Act, 1943*, of the United Kingdom, be referred to the Ontario Commissioners to redraft in accordance with the rules of drafting of this Conference and in accordance with the principles as agreed upon at this meeting ...

There is nothing in the published proceedings of the 1947 Conference to indicate what those agreed upon principles were. However, they are set out in the 1948 Report of the Ontario Commissioners.[47] The Conference had decided to follow the *English Act* in nearly all respects. It rejected the recommendation of the Ontario Commissioners that the three exceptions be dropped. It also decided that the expression "contract governed by the law of", the purpose of which was to define what contracts the statute should apply to, should be retained. One change, however, was agreed to. The draft act was not to include the equivalent of clauses (a) and (b) of section 1(3) of the English statute.

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[39] 23 Can. Bar Rev. 43 and 469.

[40] 1945 Conference Proceedings, at p. 27.

[41] *Ibid.*, at p. 188.

[42] 1946 Conference Proceedings, at pp. 23, 75.

[43] *Ibid.*, at p. 23.

[44] 1947 Conference Proceedings, at p. 20, 51-52.

[45] *Ibid.*, at p. 54.

[46] *Ibid.*, at p. 20.

[47] 1948 Conference Proceedings, at p. 71.

At the 1948 Conference the Ontario Commissioners presented their draft. It was adopted as the *Uniform Act* with some minor changes.[48]

In working out the provisions of the *Uniform Act*, the Uniformity Commissioners endeavoured to produce a model statute that was more understandable than the *English Act*. The *Uniform Act* is better arranged and there are some improvements in wording. Yet basically it is much the same. In the final result, there was only one change in substance. Section 3(2)(c)(I) of the *Uniform Act* has no counterpart in the English statute. This provision is discussed later.[49]

(ii) *Enactment of the Uniform Act*

Eight Canadian jurisdictions, as was mentioned in Chapter I,[50] have adopted the *Uniform Act*. The only, common law provinces that have not done so are Nova Scotia, Saskatchewan and British Columbia.

In none of the eight jurisdictions was any change in principle made. But in all, and in some more than others, very minor changes were made in punctuation, wording, and arrangement. It would not be worthwhile to catalogue these minor differences here.

(iii) *British Columbia's Bill (No. 48)*

Bill 48 introduced by the Attorney-General in the Legislature of this Province in 1959,[51] like that of many of the jurisdictions which had already adopted the *Uniform Act*, was virtually identical to the model statute. The bill, which is set out in Appendix F, contained no changes of substance and various minor changes in form.

Although these changes are of a very technical nature, they are set out at the end of Appendix F for the information of those who are interested in knowing the extent to which the *Uniform Act* was departed from.

(d) *In the State of Victoria*

The same year that Bill 48 was introduced in the British Columbia Legislature, the State of Victoria enacted its frustrated contracts statute.[52]

The Frustrated Contracts Act, 1959 is set out in Appendix D and included in the concordance with the Uniform and English Acts because it contains a number of departures in principle. These are:

1. There is no exception with respect the sale of goods and the *Victoria Act* expressly applies to contracts avoided under the equivalent of section 13 of our *Sale of Goods Act*.
2. The conflicts provision (this act applies to any contract governed by the

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[48] *Ibid.*, at p. 18.

[49] *Infra*, at p. 73.

[50] *Supra*, at p. 10.

[51] *Ibid.*

[52] Eliz. II, No. 6359.

law of this jurisdiction) has been omitted.

3. There is a special limitation period provided for in section 5.

The following chapter contains an analysis of some of the problems posed by the English and Uniform Acts.

CHAPTER IV PROBLEMS UNDER THE UNIFORM ACT

1. *Principles of compensation*

(a) *General*

The purpose of frustrated contracts legislation should be, in the view of the Commission, to provide the fairest possible way of adjusting the positions of parties to a frustrated contract.

In sorting out the position of the parties, there are three matters to be considered

1. The problem of restitution for obligations performed,

2. The problem of relief from liability for obligations unperformed but which were due to be performed prior to the time of frustration, and

3. The question of apportionment of loss.

It will be recalled that there is no difficulty with respect to unperformed obligations that were due to be performed after the time of frustration. The parties are discharged from performing these under the common law doctrine of frustration.

(b) *The Formula Criticized*

There are a number of criticisms that may be made of the formula for restitution which is established under the *Uniform Act*. Most of these criticisms have been made already by learned writers on the subject in relation to the similar provisions of the *English Act*. All the criticisms that are made here apply to both acts.

After these criticisms have been set out, other approaches to providing a suitable formula for restitution will be examined.

The criticisms given here should not be regarded as an exhaustive list. They are set out to demonstrate what may be regarded as the major defects of the *Uniform Act*.

(i) *The Off-Set*

Subsection (2) of section 4 of the *Uniform Act* provides for the payee off-setting his expenditures against sums paid or payable in relation to which the payer is seeking relief under subsection (1). The maximum the payee can off-set is the total of the sums paid and payable. Goff and Jones refer to the English equivalent of this provision as "the most controversial part of the Act." These authors write:[1]

> This provision follows the recommendation of the Law Revision Committee, which was based on the assumption that in stipulating for prepayment the payee intends to protect himself against loss under the contract. That assumption is open to criticism. It by no means follows that, where a prepayment is stipulated

[1] *Op. cit.*, at p. 332.

> for, the parties intend that the payer shall stand the risk of expenditure lost by the payee because of the frustration of the contract. The object of the advance may be to put the payee in funds to continue the contract, or to protect him from loss flowing from the payer's breach or insolvency. Moreover, it is arguable that, under the proviso, a party who has made an advance payment before the time of discharge which he was not bound to make, to that extent stands the risk of the other party's lost expenditure. Such a conclusion cannot have been intended by the Law Revision Committee, but its effect may in practice be alleviated or negatived by the exercise of judicial discretion.

This Commission agrees with the criticism of the Law Revision Committee's reasoning. To some extent, this deficiency of subsection (2) is lessened by subsection (3), which allows the party performing work to make a claim if the other party has *obtained a valuable benefit*. The Commission considers that this problem, as well as others, could be avoided by providing that each party is entitled to restitution for performance or part performance of obligations, regardless of how much money was paid or payable under the contract prior to frustration.

(ii) *Obtaining a Valuable Benefit*

The meaning of "obtained a valuable benefit" in subsection (3) of section 4 has already been discussed in reference to the kind of circumstances that arose in *Appleby v. Myers*.[2] Cheshire and Fifoot did not think that the English equivalent would provide relief where, although work had been done, the person for whom it had been done had derived no real advantage from it - and would not derive such an advantage until the work was completed. Goff and Jones, on the other hand, hoped and seemed to have thought that subsection (3) would allow recovery in such a case.

Obviously, the provision should be drafted in such a way as to avoid this controversy. The Commission believes that any such provision should make clear that performance or part performance of an obligation is itself sufficient to enable a claim for restitution to be made.

If this were the case, the difficulties confronting a court in determining what is the "value of the benefit" would be removed. Relief would be given on the basis of the expenditure incurred in performance. In this respect the Commission believes two factors should be spelled out:

1. The amount recoverable shall include only expenditures reasonably incurred in performing the contract.

2. If the performance involved something that can be and is returned *in specie* to the performer within a reasonable time, the amount of the claim should be reduced by the value of what has been returned.

This question is referred to again later in this chapter.[3]

(iii) *Judicial Discretion*

Under subsection (2), (3) and (4) of section 4 of the *Uniform Act*, the court is given a discretion with respect to allowing claims. Goff and Jones have written with

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[2] *Supra*, at p. 46.

[3] *Infra*, at p. 61.

respect to the English equivalent of subsection (2).[4]

> In commercial law, it is undesirable that these questions should rest on the uncertain exercise of judicial discretion.

This Commission agrees in principle. It is preferable that persons should know what their rights are.

(iv) *Apportionment of loss*

The *Uniform Act* does not expressly provide for apportionment of loss.

A few illustrations will show how apportionment of loss arises and how it is not adequately dealt with by the legislation.

Suppose X contracted to do certain work for Y in return for $5000, Y agreeing to pay the full contract price in advance. Subsequently the contract is frustrated.

> *Situation 1* - If X had not yet incurred any expenses in carrying out his obligations and Y had paid the $5000 as he had agreed to, Y would be entitled to recover the entire $5000 under section 4(l) (a).

> *Situation 2* - If X had not yet incurred any expenses in carrying out his obligations and Y had not yet paid the $5000, Y's obligation to pay the $5000 would cease by virtue of section 4(l) (b).

In situations 1 and 2, neither X or Y will have suffered any loss except insofar as what they would have *gained* by the contract. This would normally be expressed in terms of lost profit.

> *Situation 3* - If X had incurred expenses in the sum of $4000 in carrying out his obligations and Y had paid the $5000, Y would probably only be entitled to recover $1000 since X would be entitled to ask the court to allow him to off-set under section 4(2).

It is assumed in Situation 3 that no value can be retrieved from the partially completed work. The work could, for example, have been destroyed by fire. It is also assumed that X has done four-fifths of the work so that no argument can be raised as to the extent of his off-set.

In Situation 3, X has recovered his expenses and all he will be out is his lost profit. Y, on the other hand, is but of pocket $4000 and has nothing to show for it. There is a loss of $4000 and the burden is carried by Y. Is that fair? Should the $4000 loss be apportioned between X and Y equally? It might be argued that, at least in some circumstances, it was understood that one of the parties should bear the risk of failure to complete the contract. It might be further argued that insurance had been arranged on the basis of that contemplated allocation of risk.

The same problem would arise if Y had agreed to pay the contract price on completion of the work and X had incurred $4000 in expenses at the time of frustration. If X was regarded as having obtained a valuable benefit, Y would claim $4000 from X under section 4(3).

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[4] *Op. cit.,* at p. 333.

It is true that X's claim for $4000 in both these instances is subject to the court's judicial discretion. The court may allow X's claim in whole or in part if it "considers it just to do so having regard to all the circumstances". It must be doubtful, however, if a court would apportion loss in the exercise of its discretion. The intention appears to have been that it should not. There is no case law to assist us.

The point is: Should losses be apportioned between the parties and, if so, on what basis?

The problem of apportionment will be returned to later in this chapter.

(v) *Acts done after discharge*

The *Uniform Act* gives relief for things done prior to the time of frustration, but not afterwards. It is possible that a payment might be made on work done after the frustrating event in at least two circumstances. A party might not be aware of the facts that comprise the frustrating event or, being aware of them, might not have realized that at law these facts would have the effect of discharging the parties from having to perform further obligations. Apart from any frustrated contracts legislation, the party doing something after frustration probably has a remedy in the first case but not in the second.[5] Once frustration has occurred, the contract is at an end. It would appear that, where money was paid on the basis of a mistake of fact, the payer would be able to recover in an action for moneys had and received. Where the money was paid under a mistake of law, it probably would not be recoverable but it would be dangerous to attempt to oversimplify. In situations where work was done, rather than money paid, it may be that parallels could be drawn but again the law is not clear. It is probable that an action to be paid on a *quantum meruit* basis would succeed where the work was done under a mistake of fact and the other party accepted the work.

The payment of money or the performing of work after a particular contract is frustrated is something which is not likely to occur. The question is whether or not provision ought to be made in frustrated contracts legislation for such an unusual occurrence, at least where a mistake of fact is involved. While the Commission willingly concedes that an argument could be made for so providing, it is inclined not to make a recommendation to this effect. The Commission's view is that events that occur after the contract is at end should be settled under the existing law of restitution. If that law has shortcomings, then it might be appropriate for the Commission to review it in a general study at some future time. This study, with its narrow topic, is not a suitable vehicle for opening up this complex area of the law.

(c) *Another Approach*

Earlier in this Chapter, the Commission pointed out that one of the shortcomings of the *Uniform Act* was the uncertainty in the meaning of "obtained a valuable benefit". It would be preferable, the Commission stated, to have a provision requiring restitution for performance or part performance of a contractual obligation. It was also stated that the problem of apportionment of loss would be discussed later in this Chapter.

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[5] *See* Cheshire and Fifoot, *op. cit.*, at p. 581 *eq seq.*; Goff and Jones, *op. cit.*, at p. 331.

In analyzing the English legislation, Goff and Jones state:[6]

> There are two other solutions which might have been adopted. One is that, whereas benefits received by either party in pursuance of the contract should be restored or paid for, the loss of expenditure otherwise incurred under the contract should lie where it falls. This is the solution generally adopted in the United States. The other solution is that, in addition to restitution of benefits received, the two parties should bear equally the expenditure otherwise incurred by both under the contract. This solution regards the contract as a joint adventure which has failed without fault. The choice is not easy, but we suggest that the former of the two solutions should have been adopted by Parliament as being more in accordance with business ethics and commercial expectations.

The authors go on to say that the "simplicity and clarity" of the relevant provisions of the American Restatement of-Contracts contrast favourably with the "cumbrous discretionary" provisions of the English statute.

The Restatement contains the following:

> 468. Rights of Restitution
>
> 1. Except where a contract clearly provides otherwise, a party thereto who has rendered part performance for which there is no defined return performance fixed by the contract, and who is discharged from the duty of further performance by impossibility of rendering it, can get judgment for the value of the part performance rendered, unless it can be and is returned to him in specie within a reasonable time.
>
> 2. Except where a contract clearly provides otherwise, a party thereto who has rendered performance for which the other party is excused by impossibility from rendering the agreed exchange, can get judgment for the value of what he has rendered, less the value of what he has received, unless what he has rendered can be and is returned to him in specie within a reasonable time.
>
> 3. The value of performance within the meaning of subsections (1,2) is the benefit derived from the performance in advancing the object of the contract, not exceeding, however, a ratable portion of the contract price.

The Commission prefers the American position to that of the Uniform and English Acts.

On the whole, the Commission considers that restitution for performance or part performance of contractual obligations should be the governing principle. Entitlement to restitution should be based on what has been done by the performing party in the fulfilment of his contractual obligations, rather than on the benefits received or obtained by the other party.

The Commission also believes, however, that the American position does not go far enough since it does not provide for apportionment of loss.

Relief should be given, in the view of the Commission, in the situation discussed earlier in this chapter where:

(a) there has been performance or part performance of contractual obligations,

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[6] *Op. cit.*, at p. 333.

(b) the person performing is entitled to receive restitution, but

(c) the person for whom the performance was done will have nothing to show for it (e.g., work was destroyed by fire).

The Commission agrees with Glanville Williams, who stated, in reference to the English statute:[7]

> The situation with which the Act is concerned is the familiar one in which one of two parties has to suffer loss for which neither is responsible. In my submission, natural justice does not indicate either of such parties as the one to bear the whole of the loss. Natural justice neither says that the loss shall lie where it falls, nor yet says that the loss shall be picked up from where it happens to fall and transferred to the shoulders of the other party who would otherwise not have borne it. Either natural justice, on my understanding of it, is altogether silent on a case of this sort, or it decrees that the distribution of loss shall be equal. Equal division of loss is also economically sounder than the placing of loss on one party only, for each of the two parties may be able to bear half the loss without serious consequences when the whole loss might come close to ruining him.

He added:[8]

> It may be suggested, therefore, that in the normal case the just course, as required by the Act, and also the socially desirable course, would be to order the retention or repayment of half the loss incurred (subject to the overriding limits already stated), not the whole of it. To shift the whole loss in respect of expenses to the other party would, it is submitted, be as objectionable as shifting none.

In its working paper, the Commission proposed that the basic principles underlying frustrated contracts legislation should be restitution for what has been done and apportionment of loss. The response to the Working Paper has led the Commission to make an important qualification to that proposal. The Commercial Law Subsection, which agreed with the Commission that there was a need for frustrated contracts legislation, took the view that it was imperative that an exception be made when it was understood that the risk of loss should be borne by one of the parties to the contract. There are certain situations in which business practice and commercial understanding has arrived at the position where the parties contemplate payment by results, and payment by results only. Until the contract is completely performed, both parties intend or contemplate that any loss or damage shall lie exclusively on the performer. In such a case, custom and practice require the performer to bear the risk of loss or damage up until the time of completion of performance. It is, of course, perfectly open to the parties in this type of situation to provide expressly in the contract who bears what particular types of risk, and what is to happen in the event of impossibility of performance. The problem arises where no express provision has been made. In such a case, it may be that the courts would imply a provision, if there was a course of dealing, custom or common understanding that one party should bear the risk. If there was either an express or implied provision of this kind, the doctrine of frustration might not operate at all as the parties would have provided, at least to some extent, as to what should happen in the event of certain circumstances occurring. However, insofar as there is no express provision but there is a course of dealing, custom or common understanding that one party should bear the risk, there can be no guarantee that

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[7] *Op. cit.*, at pp. 35-36.

[8] *Ibid.*, at p. 36.

the courts would imply a provision. Consequently, the Commission has concluded that there should be a qualification as put forward by the Commercial Law Subsection. If the performing party generally took out insurance against the kind of event that caused a loss, this should be evidence of a course of dealing, custom or common understanding for the purpose of the qualification.

The word "restitution" by itself could conceivably cause difficulty, but it does convey the spirit of what the proposed legislation should accomplish. The Commission believes that difficulties in interpretation of both restitution" and "apportionment of loss" would largely be resolved if the proposed statute provides:

1. Insofar as a claim for restitution is based on expenditures, the amount recoverable should include only expenditures reasonably incurred in performing contractual obligations,

2. Account should be taken of any benefits which remain in the hands of the party claiming restitution,

3. No account should be taken of

   (a) loss of profits, or

   (b) insurance money that becomes payable by reason of the circumstances that give rise to the frustration, and

4. If performance consisted of or included delivery of property that could be and is returned to the performer within a reasonable time after the frustration, the amount of the claim should be reduced by the value of the returned property.

Since the purpose of frustrated contracts legislation is to provide a fair formula for adjusting the overall positions of the parties once the doctrine of frustration becomes applicable, the legislation should deal with obligations that were due to be performed before the frustrating event occurred, but which were unperformed. Both the English and Uniform Acts provide, for example, that sums payable (but unpaid) prior to frustration cease to be payable. Under this Commission's proposal, based as it is on wide principles of restitution and apportionment, prior unfulfilled obligations generally should be regarded as having been discharged by the frustration. There is, however, one exception. A party should remain liable for damages for consequential loss. For example, if a party failed to pay a sum as required by the contract, before frustration occurred, he should be relieved from paying that sum but should remain responsible for the loss his breach may have caused, i.e., the party to whom the sum was payable may have had to borrow funds as a result and have thus incurred interest charges.

To sum up, the Commission recommends:

There should be frustrated contracts legislation enacted in this Province incorporating the following:

Basic Principles

1. Every party to a frustrated contract should be entitled to restitution for the performance or part performance of any of his contractual obligations.

2. Each party should be relieved from fulfilling obligations that were due to be performed before the frustrating event but which were not performed, provided that no right to damages for consequential loss which accrued prior to frustration shall be affected.

3. If restitution were to be made, and if the party required to make it would suffer a loss because, owing to the circumstances that gave rise to the frustration, he has no benefit or the benefit is less in value than the amount payable by way of restitution, the loss should be apportioned equally between the party required to make restitution and the party to whom restitution is required to be made.

4. A person should not be entitled to restitution in respect of a loss in value of a contractual benefit, where that benefit was created by the performance or part performance of a contractual obligation if there was

   (a) a course of dealing between the parties to the contract or

   (b) a custom or a common understanding in the trade, business or profession of the party performing, or

   (c) an implied term of the contract that the party so performing should bear the risk of such loss in value.

Restitution and Apportionment

In determining what the parties are entitled to by way of restitution and apportionment:

1. Insofar as a claim for restitution is based on expenditures, the amount recoverable should include only expenditures reasonably incurred in performing contractual obligations.

2. Account should be taken of any benefits which remain in the hands of the party claiming restitution,

3. No account should be taken of

   (a) loss of profits, or

   (b) insurance money that becomes payable by reason of the circumstances that give rise to the frustration, and

4. If performance consisted of or included delivery of property that could be and is returned to the performer within a reasonable time after the frustration, the amount of the claim should be reduced by the value of the returned property.

Evidence of Understanding

In determining whether there was a course of dealing, custom or understanding that the party performing should bear the risk of a loss in value of a contractual benefit, the general effecting of insurance against the kind of event that caused the loss, where similar contracts are made, should be evidence of a course of dealing,

custom or common understanding.

2. *The Exceptions*

(a) *Contracts for the Sale of Goods*

The *Uniform Act* provides in Section 3(2) © that it does not apply

> to a contract for the sale of specific goods where the goods,
>
> (i) without the knowledge of the seller, have perished at the time when the contract is made,
>
> or
>
> (ii) without any fault on the part of the seller or buyer, perish before the risk passes to the buyer.

This provision represents an attempt by the Conference of Commissioners on Uniformity to improve upon section 2(5) (c) of the *English Act*, a clause which is generally regarded as badly drafted and unnecessary.

The English statute provides that it shall not apply

> 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.

Glanville Williams explained this provision:[9]

> This seems to be a somewhat involved way of saying that the Act does not apply to any contract for use sale of specific goods that perish, whether the risk passed to the buyer before the date of the perishing or not.

After stating that "this restriction upon the scope of the Act is to be regretted", Professor Williams gives an eight-page critical analysis of the clause,[10] which Dean Falconbridge[11] referred to as a "terrifying exposition". Cheshire and Fifoot refer to the English provision as being clumsily drafted" and "difficult to understand."[12] They conclude that it is "a little bewildering" and that:[13]

> ... it is difficult to see why an arbitrary distinction should have been made between different contracts for the sale of goods or, indeed, why it was thought necessary to exclude any such contract from the operation of the Act in a case where the doctrine of frustration is relevant. There seems no reason why the statutory provisions for the apportionment of loss should not have been

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[9] *Op. cit.*, at p. 81.

[10] *Ibid.*, at pp. 81-90.

[11] 23 Can. Bar Rev. 469, at p. 478.

[12] *Op. cit.*, at p. 526.

[13] *Ibid.*, at pp. 528-529. *See also* Gutteridge, *op. cit.*, at p. 98.

permitted in the case of any contract for the sale of goods.

Atiyah, in his text on the English *Sale of Goods Act*, advocates the repeal of the English provision.[14] Not one writer on the subject appears to have a good word for the form of the provision or for its presence in the Act. The only justification that has been given for this exception is that the consequences of frustration with respect to the contracts covered by the exception are adequately taken care of under existing rules that have been long-established and are well understood by the commercial community.[15] This cannot be regarded as a good reason for resisting change, if the result is unjust. As Dean Falconbridge has stated with respect to all three exceptions: [16]

> 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.

Glanville Williams found it "puzzling to know why these contracts were excluded from the Act", pointing out that the Law Revision Committee did not suggest their exclusion.[17]

No doubt it was this general rejection of the provision that led the Ontario Commissioners at the 1947 Conference on Uniformity to recommend that no similar provision be contained in the *Uniform Act*. The Ontario[18] Commissioners stated in their report

> Clause (c) appears to say that the Act does not apply to any contract for the sale of specific goods that perish, whether the risk passed to the buyer before the date of the perishing or not. This undoubtedly would cause hardship in many cases.

The Conference, however, rejected the recommendation of the Ontario Commissioners and the following year, when the *Uniform Act* was approved, it contained a supposedly improved version of the English provision. There is no discussion in the Proceedings of the 1947 Conference as to why the Ontario recommendation was turned down. Nor are any reasons given in the 1948 Proceedings for the changes that resulted in the revised uniform provision.

It is convenient to set out here sections 12 and 13 of the British Columbia *Sale of Goods Act*:[20]

> 12. Where there is a contract for the sale of specific goods, and the goods without the knowledge of the seller have perished at the time when the contract is made, the contract is void.

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[14] P.S. Atiyah, *The Sale of Goods*, 3rd ed. (1966), at p. 135.

[15] Chalmer's *Sale of Goods Act*, 1893, 14th ed. (1963), at p. 237. *See also* McNair, *op. cit.*, at p. 172.

[16] 23 Can. Bar Rev. 469, at p. 477.

[17] *Op. cit.*, at p. 69.

[18] 1947 Proceedings, at p. 54.

[20] R.S.B.C. 1960, c. 344.

13. Where there is an agreement to sell specific goods, and subsequently the goods, without any fault on the part of the seller or buyer, perish before the risk passes to the buyer, the agreement is thereby avoided.

These two sections are taken from, and are identical to, sections 6 and 7 of the English *Sale of Goods Act, 1893*,[21] which has been adopted in all the common law provinces in Canada and in both the territories. Section 13 is the same as the section 7 referred to in clause (c) of the section 2(5) of the English frustrated contracts statute.

Section 3(2) (c) of the *Uniform Act* differs from section 2(5) (c) of the English act in a number of respects:

1. It contains no specific reference to a *Sale of Goods Act*.

2. Sub-clause (I) of clause (c) of the *Uniform Act* has no equivalent in the English statute.

3. Sub-clause (ii) of clause (c) of the *Uniform Act* is different in wording from clause (c) of the English statute, being an attempt to capture in simplified form the substance of the English clause (c).

There are two main criticisms that can be made of the exception as it appears in the *Uniform Act*

1. Sub-clause (I) is irrelevant and should never have been placed in the Uniform Statute at all.[22] It purports to provide that the Act is not to apply to contracts that are void under law similar to section 12 of the British Columbia *Sale of Goods Act*. This provision of the *Sale of Goods Act*, which appears to have done nothing more than confirm what was already established at common law, has nothing to do with the doctrine of frustration. The contract is void at the time the contract is entered into because of the absence of the-contemplated subject-matter. There has been a common mistake by the parties as to the existence of the subject-matter of the contract. This is entirely different from a contract that was valid to begin with, but subsequently becomes impossible to perform.[23]

   Apart from sub-clause (I), therefore, the *Uniform Act* would not apply to a contract that was void under provisions similar to section 12 of the British Columbia *Sale of Goods Act*. *The Uniform Act*, like the English act, applies only to contracts which become void under the doctrine of frustration. It is true that a contract which is void under section 12 is impossible to perform, but that result would not bring the contract under the operation of the frustrated contracts statute. No one has ever suggested that such contracts are governed by the English enactment.

2. Although sub-clause (ii) of clause © of the *Uniform Act* is undoubtedly

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[21] 56 & 57 Vict., c. 71.

[22] *See* Payne, *op. cit.*, at p. 98.

[23] *See* Schmittoff, *The Sale of Goods*, 2nd ed. (1966), at p. 54; Chesire and Fifoot, *op. cit.*, at pp. 194, 196-204.

preferable in wording to clause © of the English statute, the reasons for rejecting the principle of the exception, as it appears in the English act, applies equally to the *Uniform Act*. First of all, hardships that frustrated contracts legislation is designed to relieve occur under contracts for the sale of goods in much the same way as under other contracts, and the statutory relief should be available in such cases. Secondly, the clause makes unjustifiable distinctions. The exception does not apply, for example, where there is a contract for the sale of goods and,

(a) it is a contract for the sale of unascertained goods, or

(b) the contract is frustrated for some other reason than the perishing of goods.[24]

Professor Payne has said of the statutory exception in clause (ii) that it is[25]

> ... ill-defined and perhaps also unjustified in principle for there seems no good reason for excluding statutory apportionment of loss in respect of any contract for the sale of goods which has been discharged by frustration.

Goff and Jones say of this provision that:[26]

> ... in its present form is open to the serious criticism that it draws an unnecessary distinction. In our view, it should be repealed.

The State of Victoria, in its 1959 frustrated contracts legislation, has omitted the exception. It has also expressly provided that its statute should apply to contracts avoided under the provision of the Victoria *Goods Act* which is similar to section 13 of the British Columbia *Sale of Goods Act*.[27] This Commission agrees with the approach taken in the State of Victoria. It believes that there is no justification for the exception. It also believes that frustrated contracts legislation should apply to contracts avoided by section 13.

Accordingly, the Commission recommends:

1. No exception for contracts for the sale of goods should be made.

2. Contracts avoided under section 13 of the *Sale of Goods Act* should be governed by the legislation recommended in this Report.

(b) *Contracts of Insurance*

Clause (b) of subsection 2 of section 3 of the *Uniform Act* provides that the statute does not apply to contracts of insurance. This is similar to section 2(5)(b) of the *English Act*.

Thus, unless an insurance contract otherwise provides, an insured cannot

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[24] *See* McNair, *op. cit.*, at p. 173.

[25] *Op. cit.*, at p. 98.

[26] *Op. cit.*, at p. 339.

[27] S.V. 1959, No. 6539, s. 3 (1). *See* Appendix D.

recover any part of the premium he has paid where the subject-matter of the risk ceases to exist during the period for which he is insured. An illustration is given in Cheshire and Fifoot.[28] If a person insures against sickness on January 1st, paying a year's premium, and then dies on February 1st, his executors cannot get back 11/12th of the premium.

This position is said to be not inequitable on the ground that[29]

> 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.

Professor Payne has attacked this view, stating[30]

> . . . this opinion entirely ignores the relative powers of the parties to a contract of insurance and also the fact that the insurance company is conveniently placed with regard to general distribution of the loss.

In his book on the *English Act*, Glanville Williams says that it is difficult to see why contracts of insurance are excluded. After pointing out that some insurance contracts expressly exclude the doctrine of frustration (and thus the operation of the act), he states:[31]

> If the contract of insurance does not so exclude the law of frustration, this branch of the law will apply to the contract, and if it applies it is hard to understand why the Act should not apply also.

The English Law Revision Committee did not make a recommendation that insurance contracts be excluded. It was silent on that point.

Goff and Jones state:[32]

> Logically there was no reason why the 1943 Act should not have empowered the courts to apportion the premium. The desirability of any such change in the law does not appear to have been considered. So fundamental a change would require careful consideration before it was affected.

On the other hand, Treitel, in his book on The Law of Contract, says:

> The object of this exception is to preserve the rule that there can, in general, be no apportionment of premiums under an insurance policy once the risk has begun to run. The whole essence of a contract of insurance is that "the contract is for the whole entire risk, and no part of the consideration shall be returned". Thus if a ship is insured but lost in some way not covered by the policy after part of the period of insurance has run, no part of the premium can be recovered

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[28] *Op. cit.*, at p. 526.

[29] H.C. Gutteridge, in a review of Glanville L. Williams' book, *The Law Reform (Frustrated Contracts) Act, 1943*, 61 L.Q.R. 97, at p. 99. (1945.)

[30] *Op. cit.*, at pp. 97-98.

[31] *Op. cit.,* at p. 80.

[32] *Op. cit.,* at p. 338.

> back. This is obviously in accordance with the intention of the parties, for such a contract is essentially speculative. Had the ship been lost by one of the perils insured against on the first day, the insurer would have had to bear the whole loss. Conversely, he can keep the whole premium if the ship is lost by an excepted peril at any time during the period of insurance.[33]

In its working paper, the Commission made the tentative proposal that the insurance exception of the *Uniform Act* and the *English Act*, not be made. This suggestion met with some opposition from commercial lawyers in the province. In particular, the Insurance Law Subsection was opposed. The Commission still feels that, in principle, contracts of insurance ought to be treated like any other contract for the purpose of the doctrine of frustration and its consequences. But the Commission concedes that there are practical reasons why contracts of insurance ought to be exempted from the proposed Act. First, the demands of justice are not clearly in favour of providing for the return of premiums in the event of frustration. A majority of commentators seem to favour the return of premiums, but there is an argument, put by Treitel, for the view that justice does not require the return of insurance premiums. Second, the problem is a relatively minor one. The amounts involved in the ordinary case of motor vehicle insurance or household insurance are likely to be small. Third, Professor Payne's argument concerning relative bargaining power is not as forceful as might appear, since it would be open to an insurance company to draft its standard contract form in such a way as to avoid the consequences of a frustrated contracts statute. Fourth, the law of insurance is a somewhat specialized branch of the law of contract, and an alteration in the rules applicable to the consequences of frustration of a contract of insurance might be better dealt with in a review of the law of insurance, rather than a review of the general law of contract. Fifth, since there is substantial uniformity in insurance law throughout Canada, and since the eight Canadian jurisdictions that have adopted the *Uniform Act* have retained the insurance exception, there is something to be said for maintaining uniformity on this point.

Accordingly, the Commission recommends:

Contracts of insurance be exempted from the operation of the legislation recommended in this Report.

(c) *Charterparties and Bills of Lading*

The *Uniform Act* provides, in section 3(2) (a), that the Act does not apply to a charterparty or a contract for the carriage of goods by sea, except a time charterparty or a charterparty by way of demise.

This provision is taken from section 2(5) of the *English Act*.

Halsbury's Laws of England states:[34]

> A contract for the carriage of goods in a ship is called in law a contract of affreightment. In practice these contracts are usually expressed in writing and most frequently in one or other of two types of document called respectively a charterparty and a bill of lading.

A charterparty is a contract by which a shipowner agrees to the hire of his

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[33] G.H. Treitel, The Law of Contract, 34d ed. (1970), at p. 776.

[34] 3rd ed., vol. 35, at p. 247.

entire ship, or part of it, for the carriage of goods. It may be for a determined voyage to one or more places or for a specified time. In the latter instance, it is referred to as a time charterparty. A charterparty by way of demise is one by which the temporary ownership of the vessel (with or without master and crew) is transferred to the charterer.[35]

The common law thus continues to apply to charterparties (except those for a specified period or by demise) and to contracts for the carriage of goods by sea. There are two important common law rules which are applicable[36] -

1. Where freight is paid in advance and the goods are not delivered owing to the frustration of the contract (say, by war), the shipper cannot recover any part of the advance payment even if the freight is entirely unearned.

2. Where freight does not become payable until the contract of carriage is completely performed, the shipowner is not entitled to be paid any freight where, owing to the frustration of the contract, he is unable to deliver at the place specified. This will be so even if the shipper receives a substantial benefit by receiving the goods at some point short of their destination.

It is obvious that these rules can cause hardship. This was recognized by the English Law Revision Committee, which regarded both the common law rules as unsatisfactory but recommended no change because they had long been accepted in commercial practice.

As regards the first rule, the Committee stated:[37]

> We think that the rule is ... unsatisfactory in principle but it has been regarded as settled law for a long time past and the business practice of shipowners and insurers is to some extent based on it. We consider, therefore, that it would be inopportune and undesirable to change it save as regards hire paid in advance under a time charterparty, in which case the practice is different. Most time charters, expressly or by implication, provide for an adjustment of hire in the case of loss or inefficiency of the ship and it is probably only *per incuria* that no similar provision is made in the case of frustration of the adventure.

The Committee then recommended that[38]

> ... the general rule as to the non-recovery advance freight be not changed; but that hire paid in advance under a time charter shall be recoverable in the event of frustration of the adventure in the same manner, and to the same extent, as other payments in advance made under a contract.

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[35] *Ibid.*, at pp. 247-248. *See also* R.P. Colinvaux, *Carver's British Shipping Laws*, 11th ed., 1963.

[36] *See* Appendix B of the Seventh Interim Report of the law Revision Committee (England), Cmd. 6009, 1939,
set out in Appendix A of this Report. *See also* Chesire and Fifoot, *op. cit.*, at p. 526.

[37] *Op. cit.*, at p. 10.

[38] *Ibid.*, at p. 11.

With respect to the second rule, the Committee said that its application[39]

> ... sometimes leads to hardship where the goods come into the hands of their owner short of their destination. The owner may, in that event, obtain the benefit of part performance without paying anything for it. But the rule has been acquiesced in and acted upon for so long that, although we regard it as unsatisfactory, we do not consider it desirable or necessary to change it.

Cheshire and Fifoot state that it is customary to insure against the risks engendered by these two rules.[40]

As Professor Julien Payne has pointed out in his article on Reform of the Law of Frustrated Contracts in Saskatchewan:[41]

> The exclusion of voyage charterparties from the application of the statute can only be justified as a concession to an established commercial practice.

But admitting that strong theoretical arguments might be advanced against the exception, he found that it was "difficult ultimately to disagree" with the conclusion of Gutteridge who had written in the Law Quarterly Review in respect of the similar English provision that[42]

> ... the rules of law relating to prepaid freight ... are perfectly well understood by men of business and are accepted by them. One can scarcely quarrel with Parliament for declining to bring about revolutionary changes in well-established business practices which are not demanded by those primarily concerned.

On the other hand, Goff and Jones describe the exception as "regrettable".[43]

In its working paper, the Commission tentatively concluded that this exception should not be made. This proposal, however, met with strong opposition from the Maritime Law Subsection on a number of grounds. Not all of these, in the view of the Commission, were valid. It was suggested, for example, that the legislation, unless it contained the exceptions, would interfere with international conventions in regard to carriage of goods by sea. This was apparently a reference to the International Conference on Maritime Law held at Brussels in 1922 and 1923, which formulated rules relating to sea transit, that were adopted in the Canadian *Water Carriage of Goods Act*[44] and similar statutes in other jurisdictions. That statute lays down rules for determining the position of the parties in certain circumstances, such as fire, acts of God and war. Where the statute applies, it would preclude the doctrine of frustration from operating because it determines what the result is to be in those circumstances. Since the doctrine would not be applicable in those circumstances, it follows that frustrated contracts legislation would not be applicable either.

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[39] *Ibid.*

[40] Chesire and Fifoot, *op. cit.,* at p. 526.

[41] 1960 Sask. Bar Review 94, at p. 97.

[42] 61 L.Q.R., at p. 98.

[43] *Op. cit.*, at p. 337.

[44] R.S.C. 1952, c. 291.

It is true, however, that if this exception were not made, British Columbia would have different rules for charterparties and bills of lading than those which have been long applied in the common law world. Like the English Law Revision Committee, this Commission regards certain of those rules as unsatisfactory but reluctantly has concluded that an exception should be made. First, shipping is a specialized and technical activity. Those who participate in it are, or ought to be, familiar with its rules and practices. Second, like insurance, the law relating to shipping is now so far disembodied from the general law of contract that a review of particular principles affecting shipping law might better be undertaken in the context of shipping law generally, rather than the law of contract. Third, shipping and marine insurance are in their nature very much international activities and the arguments in favour of uniformity of law in relation to them is much stronger than where laws have mainly domestic implications.

Accordingly, the Commission recommends:

Voyage charterparties and contracts for the carriage of goods by sea be exempted from the operation of the legislation recommended in this Report.

3. *The Conflicts Problem*

The *Uniform Act* provides that the statute is to apply to *any contract governed by the law of the province* enacting it. This innocent-looking proviso (or, to be correct, its counterpart in the English reform legislation of 1943) has caused considerable controversy among some of the most learned writers on private international law.

The purpose of the provision obviously is to make clear what contracts are to be governed by the statute where some foreign element is involved. For example, suppose a contract is entered into in Seattle for the manufacturing of machinery in Japan for delivery to a firm in Vancouver. Suppose also that for some reason the contract becomes impossible to perform and, at that time, the Vancouver firm has paid 10 per cent of the contract price and the machinery was nearly completely manufactured. Let us further suppose that an action is brought in the British Columbia courts by the Japanese firm to sort out the legal position.

The British Columbia court would have to decide what system or systems of law to apply. In all probability, the court's choice would be restricted to the law of Japan, the State of Washington or this Province.

There will be two questions for the court to answer:

1. What system of law is appropriate in determining whether or not the contract has been frustrated?

2. Assuming that the contract has been frustrated, what system of law is appropriate in determining the legal consequences of the frustration (i.e., how the problem of the part payment by the British Columbia firm and the work done by the Japanese firm is to be treated)?

Although it may be that the same system of law would be chosen in answering both questions, it is not clear that this must be the result.

The general position in private international law is that:

1. The first question would be answered by choosing the system of law intended to be applicable by the parties to the contract, or where such

intention is absent, the system with which the transaction has its closest and most real connection.

2. The second question, it would appear, is open to argument and might be answered by choosing:

(i) the system determined upon under the first question, or

(ii) the system of the place where the "unjust enrichment" took place.

The provision in the *Uniform Act* is intended to ensure that the answer to the second question will be the same as the answer to the first.

The provision has been described by Glanville Williams as a "juristic blunder" on the part of the draftsman[45] and as "unnecessary and inadequate" by J.H.C. Morris.[46] Both these distinguished professors of law would have liked to have seen the provision deleted from the English statute.

[45] *Op. cit.*, at p. 19.

[46] The Choice of Law Clauses in Statutes, 62 L.Q.R. 170, at p. 183. (1946.)

There are five criticisms that have been made of the provision, as it appeared in the English enactment:

1. It did not state what system of law was to be applied by the English courts to a contract that was governed by other that English law. This point was made by both Williams [47] and Morris.[48]

However, this criticism was effectively answered by Dean J.M. Falconbridge who pointed out that the statute was not applicable where the contract was not governed by English law.[49] It would be inappropriate for the statute to provide for the situations where some other system of law governed, thus excluding the statute from operating. The purpose of the statute is to sort out the legal consequences of contracts regarded as frustrated under English law, and not to provide a general revision of the rules of private international law. The Conference of Commissioners on Uniformity of Legislation in Canada agreed with Dean Falconbridge's view.[50]

2. The major criticism made by Williams was as follows:[51]

> Much more serious is the objection that the draftsman of the Act has hit upon a rule that would not command support from most specialists in the field of conflict of laws. Before selecting the system of law that ought to govern the situation dealt with in the Act, the question of classification must be considered: that is, it must be decided whether the situation is a contractual one or a quasi-contractual one. If it is a contractual situation the draftsman was perfectly right in choosing the proper law of the contract as the system of law to govern it. But it is submitted that the situation - one of restitution of benefits consequent upon a discharge of a contract - is not a contractual but a quasi-contractual one. If so, the contract and its proper law are irrelevant considerations. When the quasi-contractual situation arises the contract has disappeared, and it is therefore illogical to make the rule governing the quasi-contractual situation depend upon the proper law of the contract. The most weighty opinion held among conflict of laws lawyers is that the law to be applied should be the law of the place where the benefit is conferred, or the enrichment takes place. This is the view adopted in the American Restatement, and it is the view approved, after a careful examination of Anglo-America and Continental law, in a valuable article by Professor Gutteridge and Dr. Lipstein. They criticize the test of the proper law of the contract as involving "a cumulation of fictions: the first fiction being the assimilation of quasi-contract [with contract] in the strict sense, and the second fiction being the presumption of an intention that restitution should take place". They also point out that the test of the proper law, if applied, may lead to an *impasse*. "Certain systems of law, e.g., French law, regard frustration as avoiding a contract ab initio. If the proper law of the contract in such a case is held to be French law there is *ex hypothesi* no contract and our English court would have to seek for some other solution."

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[47] *Op. cit.*

[48] *Op. cit.*

[49] Falconbridge, *Essay on the Conflict of Laws*, 2nd ed. (1954), at p. 429.

[50] *See* 1947 Proceedings, at pp. 52-54, and 1948 Proceedings, at pp. 18, 71-72.

[51] *Op. cit.*, at p. 19-20.

Gutteridge himself, in a review of Williams' book, felt that the use of the term "juristic blunder" by Williams was "rather strong language in the circumstances". Professor Gutteridge stated:[52]

> ... the position which arises in the event of a conflict of laws relating to quasi-contractual liability is one of great uncertainty, and the respective advantages and drawbacks of the various solutions which have been suggested are very delicately balanced, so that it would seem to be unfair to reproach the legislator for adopting a solution which has, at least, the merit of limiting the operation of an English statute to disputes governed by English law.

Dean Falconbridge agreed:[53]

> 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 place where the alleged unjust enrichment occurs, 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.

Dr. Morris, on the other hand, would have deleted the provision, but for different reasons than Williams. He disagreed with Williams' criticism on three grounds[54]

(i) It was not clear that all the remedies provided by the act were quasi-contractual in nature. Apportionment of loss was not a remedy recognized by the common law, and

> ... therefore it would seem preferable to regard the rights of the partial performer under the Act as neither contractual nor quasi-contractual, but as stemming directly from the Act itself. If this is so, it is submitted that the draftsman was free to adopt what test he liked for the incidence of the new statutory remedies without being guilty of a 'juristic blunder'.

(ii) Even if the remedies provided by the enactment were regarded as quasi-contractual in nature, and even if the applicable conflicts rule was that the law of the place of enrichment governed, there was no reason for charging the draftsman with a 'juristic blunder' merely because he decided to change the rule - if he were able to effect the change without introducing incongruity or ignoring fundamental principles of the conflict of laws.

(iii) There was no well-settled rule deducible from English cases that the law governing quasi-contracts was the law of the place of enrichment. Morris disagreed with Williams that the weight of opinion was in that direction and quoted with approval from Dean Falconbridge's statement set out above. (It is not clear from Dean Falconbridge's article whether the latter half of that statement reflected the writer's view of what the law was, what

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[52] 61 L.Q.R. 97, at p. 98.

[53] Frustrated Contracts: The Ned for Reform, 23 Can. Bar Rev. 43 and 469, at pp. 471-472. *See also* pp. 59-60.

[54] *Op. cit.*, at pp. 181-183.

it ought to be, or was the reason that he approved the provision in the *English Act*.)

Morris was convinced that the words "governed by English law" were unnecessary "because the courts would have almost certainly have reached this result without their help".[55]

3. The *English Act* does not apply to Scotland or Northern Ireland. This result was not achieved in the usual way by having a specific provision to that effect. Instead, the statute only applies to contracts governed by English law. This means English law in a narrow sense so that the Scottish courts, or those of Northern Ireland, would not apply the statute when dealing with a contract governed by the law of their own jurisdictions. Falconbridge referred to the achievement of this result as constituting "an interesting departure in the drafting of statutes."[56] McNair called the use of the expression "a contract governed by English law" an "ingenious and ... novel device for defining the scope of operation of the statute".[57] Morris considered this a major defect of the enactment, stating that the statute, or similar legislation, should be part of the law of Scotland and Northern Ireland.[58]

4. There is judicial controversy as to the method of determination of the proper law of a contract. Having regard to that controversy, Professor Julien Payne has stated, the expression "governed by the law of" may well give rise to more problems than it solves.[59]

   To the extent that there is judicial controversy on the proper law of the contract, it would not seem that the expression would create any difficulty. Any doubts as to the proper law of the contract would have to be resolved in determining the law applicable with respect to the issue of frustration, i.e., before applying the Act.

5. It is not entirely clear whether the conflicts provision means the law applying to the formalities of the contract or the law applying to its essential validity. The latter is referred to as the proper law of the contract. This criticism is made in Halsbury's Statutes of England.[60] The formal validity of a contract, it should be pointed out, is governed by the law of the country where the contract is made or by the proper law of the contract.

   While it is possible to agree that the section might be clearer in this respect; most writers appear to have seen no difficulty. McNair, for example, saw no problem. He said:[61]

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[55] *Ibid.*, at p. 185.

[56] 23 Can. Bar Rev. 43, at p. 59.

[57] 60 L.Q.R. 160, at p. 161.

[58] *Op. cit.,* at pp. 183-184.

[59] *Op. cit.*, at p. 95.

[60] 3rd ed. (1969), vol. 7, at p. 11.

[61] *Op. cit.*, at p. 162.

> There can be no doubt that the expression "a contract governed by English law" means "a contract of which the proper law is English law".

Conclusion - Any attempt at private law reform by statute raises the problem of conflict of laws. Only a very few statutes contain a choice of law provision but the question whether to include one is relevant to many statutory reforms, particularly those with obvious international implications. However, there are dangers in tinkering with the law of conflicts on a piecemeal basis. It would add further confusion to what is already difficult area of the law to comprehend. In response to our Working Paper, Professor W.R. Lederman, former Dean of Queen's University Law School and an authority in private international law, recommended that there should be no conflicts provision in our draft act. He suggested that reform of private international law should not be mixed up with reform of contract law. He agreed with what was done in the State of Victoria - the omission of the conflicts provision.

In its working paper, the Commission proposed that there should be a conflicts provision contained in the draft act it was recommending. On further reflection, however, and now having the views of Professor Lederman and Professor Carr on this point, the Commission has decided against such a provision. While the arguments for and against a conflicts provision may appear to be fairly evenly balanced - and this could be argued, as a reason for adopting the *Uniform Act* provision, all the discussions referred to above introduce an unreal contention into an area where there are unlikely to be any problems. In most cases, at least, we believe the courts of this Province would apply a British Columbia frustrated contracts statute to contracts which they had were held terminated under the doctrine of frustration as it exists in this Province. This view is borne out by Dr. Morris' opinion.[62] On the whole, therefore, the Commission has come to the conclusion that it would be unnecessary and unwise to interfere with the general operation of the rules of private international law.

Accordingly, the Commission recommends:

A conflicts provision should not be contained in the draft statute.

4. *Limitation Period*

Neither the Uniform or English Acts provide a limitation period for the making of claims, while the Victoria statute does.[63]

Since the proposed legislation would create new rights, there should be a limitation period for the bringing of actions to enforce those rights. The period should be a reasonable one. It seems to the Commission that the most appropriate period would be the same as for a breach of the particular contract which has been frustrated. The period for breach may vary, depending on whether the contract is a specialty (a deed under seal) or pot. The general period of limitation for actions for breach of contract is six years,[64] and the period in respect of specialties is twenty

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[62] Supra, at pp. 88-89. *See also* Dicey and Morris, The Conflict of Laws, 8th ed., 1967, at pp. 903, 905-906.

[63] 8 Eliz. II, No. 6359, s. 5. *See* Appendix D.

[64] *Statute of Limitations,* R.S.B.C. 1960, c. 370, s. 3.

years.[65]

The period should commence to run from the time of frustration.

Accordingly, the Commission recommends:

1. *There should be a limitation period for the bringing of actions to enforce rights under the proposed legislation.*

2. *The limitation period should be the same as the period for a breach of the particular contract that has been frustrated.*

3. *The limitation period should begin to run from the time of frustration.*

5. *Application of Legislation*

Both the Uniform and English Acts contain provisions making the legislation applicable to contracts *entered* into *before* or after the legislation came into force, although the frustration must have occurred after that time.[66] The draft statute in the Commission's Working Paper contained a similar provision.

On further reflection, and having the views of the Commercial Law Subsection, the Commission has come to the conclusion that it would not be proper to make the legislation apply to existing contracts.

Although the purpose of the proposed legislation is to provide a fairer solution than now exists, there is an element of retroactivity in the Uniform and English provisions that the Commission believes should be avoided. Although the Uniform and English Acts only come into operation if there has been frustration after the legislation came into force, their statutes, nevertheless, may apply to contracts entered into prior to their enactment. This may have the effect of imposing on parties to a contract an adjustment of their positions which would be materially different from what they might have contemplated when the contract was entered into. If the legislation had been in effect at the time they entered into the contract, they might have expressly provided for the consequences of the frustrating event and so avoided the application of the statute.

Accordingly, the Commission recommends:

Should the proposed legislation be enacted, it should only be applicable to contracts entered into after it comes into force.

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[65] *Ibid.*, s. 49.

[66] *Uniform Act*, s. 3 (1); *Law Reform (Frustrated Contracts) Act, 1943*, s. 2 (1). *See* Appendices C and B respectively.

CHAPTER V CONCLUSIONS

1. *General*

In this study, the Commission has had two objectives. It sought to determine whether a frustrated contracts statute is needed in this Province. Then, having concluded that there is a need for such a statute, the Commission set out to establish the principles which should be the basis for the legislation and the form the legislation should take.

In Chapter IV of this Report, the Commission has recommended that legislation should be enacted based on two principles, restitution for what has been done under a contract and apportionment of loss. This represents a considerable departure from the principles embodied in the *Uniform Act* - a departure which the Commission has recommended only after much deliberation.

When the Commission first undertook this study of frustrated contracts legislation, it had expected that it would find the *Uniform Act* suitable for adoption in this Province, with perhaps some minor modifications. The Commission firmly believes that it is desirable to promote uniformity of legislation among the provinces and territories. The Commissions expectations were encouraged by the fact that a number of Canadian jurisdictions had already adopted the Act. The Commission also believes, however, that a model enactment should not be adopted for the sake of uniformity if it contains serious defects.

The Commission has no doubts about the need for frustrated contracts legislation, but it has reluctantly come to the conclusion that the *Uniform Act* has such shortcomings that an alternative solution in warranted.

The *Uniform Act,* based as it is on the English act, suffers from the narrow terms of reference that were given to the English Law Revision Committee. That Committee was directed to consider the rule laid down in *Chandler* v. *Webster* and thus applied itself only to circumstances where money had been paid, or was payable, under a contract that subsequently became frustrated. It did not consider the problem of the consequences of frustration in a general way. The English and Uniform Acts, it is true, go beyond the recommendations of the Law Revision Committee in making provision for relief where a valuable benefit (other than money) had been obtained regardless of whether money was paid or payable prior to frustration. We have pointed out, however, that the meaning of this provision is not clear and that, in all probability, the provision does not go far enough. Apart from that provision, the formula for relief where monies have been or are payable with the accompanying offset for expenses incurred, which was drawn from the Committee's Report, does not provide the fair solution that this Commission believes is called for.

A summary of the Commission's recommendations follows. In Appendix G, there is a draft statute incorporating those recommendations. Drafting legislation requires special skills, which the Commission makes no pretence at possessing, and is a time-consuming task. Generally, it would be a wrong allocation of the Commission's time and present resources to engage in drafting, rather than in formulating proposals for reform. In this instance, however, we have drafted a statute since we had the Uniform Act and other legislation to draw from. The Commission recognizes that its draft is subject to improvement but puts it forward in the hope that it will be of some assistance to those charged with the responsibility

of drafting, should it be decided that the Commission's recommendations be implemented.

2. *Summary of Recommendations*

The recommendations of the Commission are set out below. The page at which each recommendation may be found in the body of the Report is indicated.

1. *The Need for Legislation* - Legislation should be enacted to provide a fair system of rules-for settling the positions of parties to contracts that have been prematurely brought to an end by the application of the common law doctrine of frustration.

2. *The Basic Principles* - Legislation should be enacted based on the following principles:

    1. Every party to a frustrated contract should be entitled to restitution for the performance or part performance of any of his contractual obligations.

    2. Each party should be relieved from fulfilling obligations that were due to be performed before the frustrating event but which were not performed, provided that no right to damages for consequential loss which accrued prior to frustration shall be affected .

    3. If restitution were to be made, and if the party required to make it would suffer a loss because, owing to the circumstances that or the benefit is less in value than the amount payable by Way of restitution, the loss should be apportioned equally between the party required to make restitution and the party to whom restitution is required to be made.

    4. A person should not be entitled to restitution in respect of a loss in value of a contractual benefit,.where that benefit was created by the performance or part performance of a contractual obligation if there was

        (a) a course of dealing between the parties to the contract, or

        (b) a custom or a common understanding in the trade, business or profession of the party performing, or

        (c) an implied term of the contract,

    that the party so performing should bear the risk of such loss in value.

3. *Restitution and Apportionment*

In determining what the parties are entitled to by way of restitution and apportionment:

1. on expenditures, the amount recoverable should include only expenditures reasonably incurred in performing contractual obligations.

2. Account should be taken of any benefits which remain in the hands of the party claiming restitution.

3. No account should be taken of

(a) loss of profits, or

(b) insurance money that becomes payable by reason of the circumstances that give rise to the frustration.

4. If performance consisted of or included delivery of property that could be and is returned to the performer within a reasonable time after the frustration, the amount of the claim should be reduced by the value of the returned property.

4. *Application of Act*

1. Should the proposed legislation be enacted, it should only be applicable to contracts entered into after it comes into force.

2. The legislation should not be applicable to

(a) contracts of insurance; and

(b) voyage charterparties and contracts for the carriage of goods by sea.

3. The legislation should apply to contracts for the sale of goods which have been either

(a) terminated by the common law doctrine of frustration, or

(b) avoided under section 13 of the *Sale of Goods Act*.

4. A conflicts provision should not be contained in the legislation.

5. *Evidence of Understanding*

In determining whether there was a course of dealing, custom or understanding that the party performing should bear the risk of a loss in value of a contractual benefit, the general effecting of insurance against the kind of event that caused the loss, where similar contracts are made, should be evidence of a course of dealing, custom or common understanding.

6. *Limitation of Actions*

1. There should be a limitation period for the bringing 6f actions to enforce rights under the proposed legislation.

2. The limitation period should be the same as the period for a breach of the particular contract that has been frustrated.

3. The limitation period should begin to run from the time of frustration.

7. *The Doctrine and Leases*

1. The *Landlord and Tenant Act* should be amended to provide that the doctrine of frustration apply to leases generally.

2. The legislation recommended in this Report should be made expressly applicable to leases.

As mentioned earlier in this Chapter, draft legislation incorporating these recommendations is contained in Appendix G.

E. D. FULTON
Chairman

R. GOSSE
Commissioner

F. U. COLLIER
Commissioner

February 17, 1971.