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Implicit Dimensions of Contract

Discrete, Relational and Network Contracts

Edited by
DAVID CAMPBELL
HUGH COLLINS
JOHN WIGHTMAN

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Beyond Custom: Contract, Contexts, and the Recognition of Implicit Understandings

JOHN WIGHTMAN

IN AMERICAN CONTRACT law, and the rich academic literature which engages with it, there has long been a recognition of the significance of the implicit understandings which can swirl around the processes of negotiation, modification and performance. The roots of this recognition are many, but they include the work of Karl Llewellyn, the contextual orientation of the Uniform Commercial Code which he influenced,[1] and the differing contributions of Ian Macneil and Stewart Macaulay. Macneil shifted the emphasis from the discrete, one shot contract, with the terms spelt out in full at the moment of formation (presentiation), to the contract which emerges around a relation, where much may be left open and the process of commitment gradual rather than sudden, as the parties establish understandings as their relationship evolves.[2] Macaulay has demonstrated that the performance of contracts is frequently governed by the parties' own understandings which are at variance with the letter of contract terms which they have

[1] On Llewellyn's influence see W Twining *Karl Llewelleyn and the Realist Movement* (London, Weidenfeld and Nicholson, 1973) 270–301. Contextual provisions of the UCC include 1–203 (obligation of good faith) and 1–205 (course of dealing and course of trade); for a History of the formation of the UCC, see AR Kamp 'Downtown Code: the History of the UCC 1949–1954' (2001) 99 Buffalo *Law Review* 359.

[2] See generally Macneil, IR 'The Many Futures of Contract' (1974) 47 *University of Southern California Law Review* 691; 'Contracts Adjustments of Long-term Economic Relations Under Classical, Neoclassical, and Relational Contract Law' (1978) 72 *Northwestern University Law Review* 854; *The New Social Contract* (New Haven, Yale University Press, 1980).

signed, and that these understandings are heavily shaped by the customs and practices of the trading communities in which they operate.[3]

Although these insights are familiar, probably hackneyed, to American contracts lawyers, in English law, and its traditionally more homogenous literature, the role of implicit dimensions has received much less attention. Without a general doctrine of good faith, or other general context-based provisions such as those contained in the UCC, most academic commentary published in the UK has shown little interest in mining the rich seams of issues which Macaulay, Macneil and others after them have opened in the US.[4] Stirrings of greater academic interest are evident, as is a greater consciousness on the part of some leading judges of the role of context in making sense of contracts.[5]

However, the fact that significant judicial and academic interest in contextual and relational issues is relatively recent does not mean that English contract law has been oblivious to the implicit understandings of the parties. In chapter 2 in this volume Campbell and Collins argue that many of the doctrines of orthodox English contract law can be understood as drawing on implicit understandings of the parties. This conclusion is in line with that of more traditional scholars who have argued, for example, that English contract law contains the resources to respond to relational contracts[6] and that a good faith doctrine is unnecessary because its function can be discharged by other doctrinal tools, for example implied terms.[7]

[3] S Macaulay, 'Non-contractual Relations in Business' (1963) 28 *American Sociological Review* 55; 'Elegant Models, Empirical Pictures, and the Complexities of Contract' (1977) 11 *Law and Society Review* 507; 'An Empirical View of Contract' [1985] *Wisconsin Law Review* 561; 'Relational Contracts Floating on a Sea of Custom? Thoughts about the Ideas of Ian Macneil and Lisa Bernstein' (2000) 94 *Northwestern University Law Review* 775.

[4] There are of course notable exceptions, of which Beale and Dugdale's is probably the best known: M Beale and T Dugdale, 'Contracts Between Businessmen: Planning and the Use of Contractual Remedies' (1975) 2 *British Journal of Law and Society* 45. This article must come high in any table of the most cited (UK) law journal articles in the last 25 years, yet there has been until quite recently astonishingly little empirical research which has followed in their footsteps. Substantial studies have now emerged, although it is striking that much of the work has focussed on the contractual arrangements within the public sector, rather than on mainstream commercial contracting. See especially the essays in the second part of D Campbell and P Vincent Jones (eds) *Contract and Economic Organisation* (Aldershot, Dartmouth, 1996), and also S Deakin and J Mitchie (eds) *Contracts, Co-operation, and Competition* (Oxford, Oxford University Press, 1997).

[5] See text at n 19 below.

[6] E McKendrick 'The Regulation of Long Term Contracts in English Law' in J Beatson and D Friedmann (eds) *Good Faith and Fault in Contract Law* (Oxford, Clarendon Press, 1995).

[7] MG Bridge, 'Does Anglo Canadian Contract Law Need a Doctrine of Good Faith?' (1984) 9 *Canadian Business Law Journal* 385.

Campbell and Collins' argument also receives indirect support from the traditional pride which many of the most respected judges have taken in being responsive to exigencies of commercial convenience.[8] English contract law may be less showy than American law, but it has traditionally preferred (*pace* Lord Denning) to work unobtrusively by adapting existing doctrines and taking into account commercial expectations without doctrinal upheaval—or at least that may be how some would put it.

It is thus possible that the greater recent emphasis on the openness of English law to the importance of the context of the parties may be as much a change in self description as a significant shift in underlying reality. However, even if one can, at a general level, identify some broad brush tendency to recognise implicit understandings stemming from the parties' context, much remains to be clarified about the detail and incidence of such developments. I do not minimise the significance of these issues, but my own focus here is in one sense a jump beyond the debate about the recognition of implicit understandings in English law.

I intend to move on from this engagement and take as established, for present purposes, that implicit understandings *are* a vital part of the machinery of existing English contract law, despite the law being expressed in language that sometimes gives the opposite impression. I want in one sense to flip the issue over. Rather than demonstrate how doctrine which is structured using agreement-based concepts is dependent on absorbing implicit dimensions, I propose to take this more or less for granted and ask the next question: if contract doctrine *is* often dependent on incorporating the implicit dimensions of the parties' relationship, what happens when those understandings are non-existent, or generated in ways other than those typical in mainstream commercial contracts?

My starting point is thus to suggest a generalisation: that the extent and nature of implicit understandings are not constants across all kinds of contracts, but vary signifcantly according to context. Can we get

[8] See for example: Lord Devlin, 'The Relation Between Commercial Law and Commercial Practice' (1951) 14 *Modern Law Review* 249; Lord Goff, 'Commercial Contracts and the Commercial Court' [1984] *Lloyds Maritime and Commercial Law Quarterly* 382; Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 *Law Quarterly Review* 433, and also the judicial pronouncements of Lord Diplock (eg *Antaios Cia Naviera SA v Salen Rederierna AB* [1985 AC 191, 201) and Lord Wilberforce (eg *New Zealand Shipping Co Ltd v AM Satterthwaite* [1975] AC 154, 167); see also R Brownsword, *Contract Law: Themes for the Twenty-First Century* (2000) 124–143.

further than saying this is a plausible generalisation? One approach might be to embark on empirical research across different kinds of contracting contexts.[9] Among other problems, this would need a selection of contexts, and thus criteria for selection. On the other hand, a substantial body of empirical work has now accumulated, and reported cases have at least some value as evidence of practice. The path I have chosen is to attempt to get some purchase on the *general* issues about the varying incidence and nature of implicit understandings by identifying two models of contractual relations. After exploring in section 1 the different senses in which implicit is used, in section 2 I construct a model of contracting practice—the contracting community model—which I argue covers most of the situations where implicit understandings are routinely recognised in the law of contract. This is an ideal type; it is intended to present a simplified but coherent picture of how implicit understandings may emerge, so that elements which favour the emergence of implicit understandings can be more clearly identified.

In section 3, I construct a second model, the personal consumption model, which is intended to highlight some features of contractual relations which do not foster the emergence of customary implicit understandings. In Section 4 I explore some of the implications for contracting practice and contract law where customary implicit understandings are not developed, and look at other types of contract relation which do not exhibit these kinds of understandings.[10]

1. MEANINGS OF 'IMPLICIT'

Neither 'implicit dimension' or 'implicit understanding' is a term of art, in either the law or the literature about contracting practice. Either could be treated as a residual category, defined by what is left after express agreement has been removed—thus it could be defined as 'all

[9] The direction of the enquiry in some respects resembles that of B Lyons and J Mehta's 'Private Sector Business Contracts—text Between the Lines' in S Deakin and J Mitchie (eds) *Contracts, Co-operation, and Competition* (Oxford, Oxford University Press, 1997), in which they sought, by empirical investigation, to test Williamson's theory of contract types.

[10] The exploration of these issues involves looking at contracting practice as well as contract law, and I refer to some of the well known empirical studies and to other sources that shed light on contracting practice. But I am conscious that some of the claims made are ultimately empirical ones which, although I believe they are plausible in the light of what we know, require further empirical investigation.

the knowledge, practices and norms pertaining to contracting which are not express.' However, this includes matters of which the parties to any exchange will typically be wholly unaware—notably things such as the regulatory structure which controls the way certain products or services are made or traded. These may accurately be described as part of the social institutions of exchange, but lack any element of understanding or awareness, which arguably is usually included in usages of 'implicit'.

By 'implicit', I will mean the knowledge, practices and or norms pertaining to contracting in general (or an individual transaction) of which the parties to a particular contract are actually aware, (or can, in the circumstances, reasonably be expected to be aware), but which are not typically rendered express in their contracting activity. However, by saying the parties are 'aware' I do not mean to convey that they must be consciously deliberating (albeit silently) at the moment of contracting: 'aware' includes assumptions about knowledge practice and norms which the parties bring to the contractual relationship. In one sense, implicit dimensions includes all the assumptions about the operation of transactions which are needed to endow the transaction with meaning. It useful to make a number of preliminary distinctions, initially by identifying three kinds of implicit understandings.

First, there are the implicit understandings stemming from a shared language, knowledge of the social institution of money, currency, and a shared 'market mentality'[11] ('general understandings'). The market mentality includes many tacit understandings about buying and selling, about the nature of private ownership, about money and modes of payment, the banking system, expectations of interest and the like. These provide the minium social institutions for exchange in developed societies, and are general, in that they are not specific to any species of transaction; they are very widespread in societies with long established market economies.

Secondly, there are those implicit understandings which emerge over time between the parties to a particular contract—'inter-party understandings'. For example, in an employment contract, understandings may evolve which stem from specific behaviour of the parties. These are distinct from the general understandings because they relate to behaviour rather than background knowledge. Moreover, these understandings

[11] K Polanyi, 'Our Obsolete Market Mentality' in K Polanyi (ed), *Primitive, Archaic and Modern Economies* (Boston, Beacon Press, 1968).

need not actually emerge during the span of any contract which is the subject matter of any dispute. They may be built up as part of a long-term trading relationship, which itself may be composed of frequent but relatively discrete contracts. Understandings laid down in this way will often take on meaning in the context set by the third type of implicit understandings.

The third type consist of implicit understandings about how commercial relations in a particular sector are carried on, in particular the practices and norms with which participants need to become familiar if they are to participate in the sector ('customary understandings'). It is this sense of implicit understanding that the empirical work of Macaulay and others has brought home most forcefully, in that much of that empirical work paints a picture of contracting as an activity where parties actions are shaped by informal understandings as much, (and often more than) the letter of their contract, even if cast in written form. It is customary understandings which, I will argue, are typically drawn upon in contract doctrine.

Although these three senses of implicitness can be differentiated, they are obviously related. General understandings are a necessary platform for both customary understandings and inter-party understandings. Most importantly, customary understandings provide the framework within which the parties deal and the baseline for one-off adjustments, including those reached by inter-party implicit understandings.

So far, the discussion of implicit understandings has assumed that these are shared between the parties. However, I do not propose to treat it as a necessary characteristic of 'implicit' that the understandings are shared, and will examine situations where there are unvoiced understandings which are held by one side only. For example, it is common in consumer contexts for the supplier to know much more of the background context in which the parties deal than the consumer, and the consumer may equally make assumptions or harbour expectations which are not shared by the supplier. Where understandings are divergent in this way, they can still play an important role in conferring meaning on the contracting process, and (I will argue) have potential significance in legal determination.

The existence of implicit understandings (whether shared or divergent) is often signalled when we use the language of reasonable expectation. This expression tends to be used to mean more than merely saying that one party's expectations are a mirror image of whatever the

contract terms provide. It includes expectations which are more widely grounded, which may be based on implied terms, but equally may be based on aspects of the background context which confers meaning on the parties dealings. Overall, I am treating 'implicit understandings' as including all the background assumptions about the transaction and its course that the parties bring to the contract.[12]

2. THE CONTRACTING COMMUNITY MODEL OF CONTRACTUAL RELATIONS

The Features of the Contracting Community Model

The contracting community model refers to contractual relations which occur within a market sector where there are established practices for carrying on trade which any firm wishing to participate in the trade will normally have to take part in. There are three basic features.

First, there is specialist knowledge about the 'physical nature' of the 'products' being traded.[13] This is primarily knowledge of the substance of the product or service, and will typically include technical knowledge relating to its construction and performance specification, and this will include knowledge of alternatives available in the sector. Equivalent dimensions of knowledge are also developed in the case of fungibles such as grain, coffee etc.[14]

Secondly, there is specialist knowledge of the way the trade is carried on, such that knowledge of these practices is necessary to participate effectively in the sector. This knowledge of how the product or service in question is typically traded will include aspects such as in what units

[12] This is not because I am taking some view of what the correct meaning is, but rather because implicit understandings have a function in many commercial contracts which I argue is left unperformed in contexts where the understandings are arrived at in different ways. See section 4 below.

[13] I am using 'product' as a generic term to include all things which are traded, including services, labour, intellectual property rights, and by 'physical nature' I mean the inherent characteristics of the product.

[14] Lisa Bernstein's empirical work (especially on commodities markets) is replete with examples of this specialist knowledge, despite the fact she argues against the automatic incorporation of custom in adjudication. See 'The Questionable Empirical Basis of Article 2's Incorporationist Strategy' (1999) 66 *University of Chicago Law Review* 710 and 'Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms' (1996) 114 *University of Pennsylvania Law Review* 1765; see text at n 34 below.

it is traded, the pricing structure and arrangements for payment, quality control, what legal instruments (financial and otherwise) are used. Most of the fields of commerce with which contract lawyers become familiar from case law are about contracting communities in this sense—shipping, the international sale of commodities, insurance, construction and so forth. Typically, these sectors have developed social institutions of exchange which play a key role in mediating and structuring exchange behaviour, a notable example being the bill of lading.

The third feature is knowledge of the practices that are used when hitches in performance arise. This knowledge is based on knowledge about the physical attributes of the product or service, including what can go wrong with these products/services in general. But it also includes knowledge about how hitches such as shortfalls in the quality or quantity of goods or services are actually handled, or how late payment or other late performance is regarded. The actual techniques used to handle resulting disputes may vary greatly across different sectors, so that in some cases dispute resolution is almost always informal, with rare recourse to the terms of contracts, while in others arbitration or litigation may be a much nearer prospect.[15] Whichever approach tends to be adopted, the present point is that knowldge of what tends to happen when performance miscarries in some way is part of the contracting community model.[16]

For these features to obtain, there will need to be a number of contractors who are repeat players, although it is not necessary that the contractors always contract with parties known to them. The key element for a contracting community to generate these features is its social organisation, so that the practices themselves are shaped, and knowledge of them disseminated, through interaction.[17] Market

[15] Compare, for example, Beale and Dugdale's study (n 4 above) with that of M Bridge on grain contracts in commodities markets: 'Good Faith in Commercial Contracts' in R Brownsword, NJ Hird and G Howells (eds) *Good Faith: Concept and Context* (Aldershot, Dartmouth, 1999) 139.

[16] This is not to say that, where customary implicit understandings exist, they will provide a constant, homogenous backcloth for every contract. The point is that these are the understandings which the parties expect in the absence of arrangements to the contrary, some elements of which will be normal in most contracts. It is arguable that it is precisely this background of shared implicit understandings which enable the parties to focus attention on the detail of matters which they wish to expressly negotiate.

[17] A contracting community of this type may also be further integrated by the role of a trade association, or groups of trade associations.

relations are the social relations which construct, preserve and renew these understandings.[18]

Although the three features above are described in terms of matters of fact, the understandings about trade practice, including the handling of miscarried performance, may harden into generalised expectations whenever they are so much a part of doing business in a sector that those in that sector assume others will (unless announced otherwise) conform with the usual practices; in that sense these understandings may have a normative dimension. These implicit understandings are, in terms of the meanings of 'implicit' discussed above, shared and customary. They provide a kind of normative and cognitive grid within which exchange relations are carried out.

The Contracting Community Model and the Law

I have described the features of the contracting community model mainly in terms of contracting behaviour, rather than in terms of the content of contract doctrine. However, the customary implicit understandings in the contractual relationships covered by the contracting community model are clearly detectable in contract doctrine. Perhaps the most striking, and significant example, can be seen in the law relating to the construction of contracts.

The understanding of construction which is now embraced by leading Law Lords places great weight on understanding contract terms in the whole context in which they are set. The views of Lord Wilberforce expressed in *Reardon Smith Line Ltd v Hansen-Tangen*[19] have been influential:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as 'the surrounding circumstances' but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the

[18] A feature which may (but not necessarily) accompany this matrix of factual and normative understandings is a high degree of trust. By trust, I mean the voluntary exposure to the risk of opportunistic behaviour by the other party. Where firms are known to one another, either because of previous dealings or reputation, there may be high levels of trust shown in the performance of the other; this may be evident in, for example, the granting of extensive credit, the co-operative handling of difficulties, etc; see further the text at n 45 below.

[19] [1976 1 WLR 989, 995.

> contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating. . . . [W]hat the court must do must be to place itself in thought in the same factual matrix as that in which the parties were. All of these opinions seem to me implicitly to recognise that, in the search for the relevant background, there may be facts which form part of the circumstances in which the parties contract in which one, or both, may take no particular interest, their minds being addressed to or concentrated on other facts so that if asked they would assert that they did not have these facts in the forefront of their mind, but that will not prevent those facts from forming part of an objective setting in which the contract is to be construed.

More recently, Lord Hoffmann, in passages that have been widely quoted, has re-emphasised Lord Wilberforce's contextual approach. In the *Investors Compensation Scheme v West Bromwich Building Society*[20] he said:

> Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract. [This] includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

And in *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd*:[21]

> The meaning of words, as they would appear in a dictionary, and the effect of their syntactical arrangement, as it would appear in a grammar, is part of the material which we use to understand a speaker's utterance. But it is only a part; another part is our knowledge of the background against which the utterance was made. It is that background which enables us, not only to choose the intended meaning when a word has more than one dictionary meaning, but also . . . to understand a speaker's meaning, often without ambiguity, when he has used the wrong words.

[20] [1998] 1 WLR 896, 912.

[21] [1997] AC 749, 775. See also Lord Steyn at 771:

> In determining the meaning of the language of a commercial contract, and unilateral contractual notices, the law therefore generally favours a commercially sensible construction. The reason for this approach is that a commercial construction is more likely to give effect to the intention of the parties. Words are therefore interpreted in the way in which a reasonable commercial person would construe them. And the standard of the reasonable commercial person is hostile to technical interpretations and undue emphasis on niceties of language.

This contextual approach is used to displace an apparent meaning not just where the words in question are ambiguous on their face, but also where (as in *Investors*) they have a clear meaning but one which did not make much commercial sense, and where (as in *Mannai*) the words have a clear meaning which the reasonable recipient would realise was not intended.

Although this contextual approach has received renewed prominence in recent years, the reference to aspects of the background to the contract that was not made express can be detected in other parts of the law of contract. For example, the use of context was clear in law on the construction of exception clauses as far back as the nineteenth century. Where written contracts contained onerous terms, attempts were made to construe the offending express term with reference to the 'main object' or purpose of the contract. This had clear affinities with the modern contextual approach, as is made clear in Lord Halsbury's judgment in the leading case of *Glynn v Margetson*:[22]

> Looking at the whole of the instrument, and seeing what one must regard . . . as its main purpose, one must reject the words, indeed whole provisions, if they are inconsistent with what one assumes to be the main purpose or object of the contract . . . Mercantile men when they do business in this form . . . recollect that a business sense will be given to business documents, and that therefore they are not under peril of leaving it absolutely to the shipowner himself to do what he will with the cargo.[23]

The 'main object' was not found in the express terms of the contract, but was deduced from the surrounding circumstances.[24] The terms used in these passages do, I think, demonstrate a focus on the shared understandings which are based on the knowledge of those familiar with the contracting contexts in which the parties operate—what I am calling customary implicit understandings.[25]

[22] [1893] AC 351, 357. A ship was carrying oranges from Malaga to Liverpool, and under the bill of lading the ship was permitted to visit almost any port in Europe or Africa. The House of Lords held that the clause could not permit the ship to call at any port because it had to be read subject to the main object of the contract.

[23] *Ibid*, 357 and 359.

[24] See B Coote, *Exception Clauses* (London, Sweet and Maxwell, 1964) for a discussion of the case law on deducing the 'main objects' from the surrounding circumstances.

[25] The point can be taken further by arguing that context is necessary to understand meaning: see Campbell and Collins, ch 2 in this volume and DV Snyder, 'Language and Formalities in Commercial Contracts: a Defense of Custom and Conduct' (2001) 54 *Southern Methodist University Law Review* 617. Also, even in some of the cases where literalism has been preferred the court has acknowledged that it was perfectly clear what was intended when viewed contextually; a notable example is *Hankey v Clavering* [1942] 2 KB 326.

Most of the examples of implicit understandings elaborated by Campbell and Collins are also cases of implicit understandings which are customary and which develop in contracting communities.[26] A contracting community can provide a relatively rich context which enables the court to draw on practices, customs and understandings which can inject meaning into open-ended standards.[27] Although many of these standards embody reasonableness in some guise, and reasonableness is readily mocked as an open licence to do anything a court wants, the shared practices of a contracting community can, in many cases, offer a way of clarifying meaning which enables it to remain a plausible search for objectivity.[28]

An emphasis on the context within which the parties contract, and on what they take for granted rather than what they have made express, is perhaps usually associated with relational contract theory. It is true that contracting communities may have strong expectations about high levels of co-operation, and may develop norms which inhibit opportunism and favour the harmonious settling of disputes without disrupting the commercial relationship, all of which are regarded as relational norms. However, this is not a necessary characteristic of a contracting community in the sense I am employing it; it is not intended to connote any necessary affiliation with communitarian or relational contract law,[29] and may equally display individualistic

[26] Clear examples include the mitigation and remoteness rule in damages law, and implied terms. Examples which are not covered seem to be the 'organisation rules' (Campbell and Collins, ch 2 in this volume) and possibly *Sagar v Ridehalgh* [1930] 2 Ch 117 (the case about defective piece work).

[27] There are also parts of the law where an exploration of customary understandings might have avoided doctrinal confusion. For example, in the battle of forms case *Butler Machine Tool Ex-Cell-O* [1979] 1 WLR 401 the issue was which form prevailed: the seller's form, which contained a price escalation clause, or the buyers form, which did not. The majority handled this using the orthodox offer/counter offer analysis. Arguably the key question should have been what, in the light of prevailing practice in the sector, the reasonable buyer would have expected: this would have provided a baseline or default position which required clear consent to adjust. *The Principles of European Contract Law* contain very clear contextual provisions, see especially eg Art 1.105 (on usage), Art 1.201 (good faith), and Art 5 101/102 (interpretation).

[28] I should make clear here that the argument is not coextensive with the conventionalist argument for default rules (for a very valuable discussion of the bases of default rules, see CA Riley, 'Designing Default Rules in Contract: Consent, Conventionalism and Efficiency' 20 *Oxford Journal of Legal Studies* 367.) The scope of what is understood as default rules varies (Riley equates them to implied terms), but they are less pervasive in doctrine than the implicit understandings I am addressing here.

[29] The term 'relational' is used in quite a few different senses; for example, it is sometimes used to mean norms which favour co-operation, and sometimes to mean norms which are derived form the parties context rather than from agreement. In contracting

norms. It is the idea of specialist, shared trading practices, embracing knowledge and expectations, which characterises the contracting community model, and this can exist in contracting contexts where co-operative norms are not well developed.[30] This neutrality regarding the content of contract norms at the level of contracting communities as a general category stems from the fact that the norms reflect actual practice, and the law will in turn reflect that reality: if the norms are individualistic, then contract law will often reflect those norms.

Contracting Communities and Neoformalism

An emphasis on the contextual interpretation of contracts has been seen as being at odds with a literal or formalistic approach. Macaulay's original article demonstrated that it may be a common practice in contracting communities to pay scant attention to the terms of the contract, and a central claim of Macaulay and many others has been that custom and conduct is vital when the terms of the contract are being construed in litigation, to the point that such custom may prevail over contradictory express terms in a standard form.[31] A neoformalist movement has now begun to reassert the case for literal interpretation, and this might be thought to undermine the claim that exchange relations in contracting communities are rich in implicit understandings.[32] Nevertheless, some aspects of neoformalist arguments valuably illuminate the role of implicit understandings in contracting communities.

Neoformalism has challenged the incorporationist approach of the UCC, which has for the last 50 years placed custom and conduct at the heart of the principles of commercial contract law.[33] After undertaking

communities, norms are always relational in the second sense and sometimes relational in the first sense.

[30] A clear example of this appears to be commodity sales of grain. Bridge argues that the practice of the five firms which dominate the world trade in grain includes adversarial activity: 'They sue each other regularly, but it is as if litigation is business carried on by other means. Opportunistic behaviour by one contracting party does not appear to sour continuing and prospective dealings between the same parties': Bridge, n 15 above, 151.

[31] See Macaulay's discussion of *Nanakuli Paving and Rock Co v Shell Oil Co* 664 F 2d 772 (1982) in 'Relational Contracts Floating on a Sea of Custom?', n 3 above, 791. A fairly close equivalent in UK law is *Schuler L (AG) v Wickman Machine Tool Sales Ltd* [1974] 235.

[32] Eg see D Charny 'The New Formalism in Contract' (1999) 66 *University of Chicago Law Review* 842.

[33] For discussion of reform of the UCC, see Snyder (n 25 above) and other articles in the *Southern Methodist University Law Review* Symposium (2001).

massive empirical work, Bernstein has argued that, even where customs or conduct can be established, it does not follow that courts should use them to depart from the plain meaning of written terms.[34] Her argument is based on a distinction between two kinds of norms: relationship preserving norms (RPN), and end game norms (EGN).[35] She sees the kind of norms contained in customs, for example where one party is prepared to make concessions by overlooking technical breaches, as typically relationship preserving. End game norms, on the other hand, are less concerned with co-operation, and are permissive of withdrawal. These norms are often found expressed in written terms relating to such things as the right to terminate for breach. Bernstein's point is that the custom and conduct enshrined in the UCC may embody RPN, which will be appropriate norms to apply where the parties are attempting to preserve the relationship. A contracting party may be happy to make concessions during the course of the relationship, but equally may not want to confer an entitlement to that concession when the relationship has broken down. Thus, given that the courts are only involved where one party (at least) has embarked on an end game, invoking RPN when the parties have reached the end game is an application of the wrong norms.

This argument recognises that custom and conduct may exist which are inconsistent with written terms, but argues that this is not sufficient reason to allow custom or conduct to prevail over written terms because that may not be what the party intended in the end game situation—in other words, the concession made in line with custom may not have been intended to be binding when things get rough and litigation results.

This argument has been subject to sustained criticism, some of it from writers otherwise sympathetic to Bernstein's position. However, what is of interest for present purposes is that even Bernstein's own position acknowledges an intricate relationship between custom and the operation of standard forms. Her argument is explicitly premised on a distribution between matters which the parties leave to the legal realm and matters which they withdraw from the legal realm, so that, although she found plenty examples of RPNs in her empirical work, she argues that these should be understood as confined by the parties to

[34] See 'Merchant Law in a Merchant Court', n 14 above.
[35] *Ibid*, 1796.

the non-legal rather than the legal realm. She claims that the distinction between RPNs and EGNs is in fact one of which contractors are aware:

> There is empirical evidence from a variety of contracting contexts that suggests that merchants behave in a way that reflects an implicit understanding of the distinction between end-game and relationship-preserving norms and that they do not necessarily want the RPNs they follow during the cooperative phase of their relationship to be used to resolve disputes when their relationship is at end-game stage.[36]

Interestingly, what Bernstein is doing here is adding a different kind of norm—not a substantive norm about preserving the relationship, or about the end game, but a meta-norm about the appropriate scope and context of those substantive norms. Paradoxically, by attributing to contractors in a commercial sector awareness not only of substantive customs, but also a meta-norm about when it is acceptable to switch between different kinds of norm, Bernstein is affirming that the implicit understandings of the contractors are even richer than may have been suggested by a focus on the substantive norms themselves.

An interesting upshot of Bernstein's analysis is that, although she provides support (in appropriate situations) for the formalist response of enforcing the written terms of the contract in the face of any contrary customary understandings, she does so by effectively inserting two additional steps in the reasoning. In orthodox terms, the justification for enforcing the terms is that this is what the parties have arrived at as their contract: legitimacy flows from their act of voluntary assent ('direct formalism'). Bernstein's analysis, however, does not derive the legitimacy of enforcing the terms solely from the act of consent in formation of the contract. Her first step is to recognise the RPNs which may be contained in the implicit understandings deriving from custom, which may displace the contract terms in actual performance. Step two is to reintroduce the express terms when the end game arrives, because at that point only the EGNs in the contract terms are appropriate. Now, if it was open to a contractor to trigger end game norms at any time, without reference to who was responsible for bringing about the end game, nor how they had done it, the extra two steps from direct formalism would be insignificant—anyone could throw the switch to end game at any time and wipe out the expectations derived from the RPNs based on custom. However, Bernstein does not appear to stake

[36] *Ibid*, 1798.

out this extreme ground, and this leaves in play the central question of when the switch can be thrown—in other words, the extent to which the RPNs of customary understandings play a role in defining when end game can be brought about.

I am not here concerned to pursue the issue of when the switch can be thrown. My point is that Bernstein provides copious support for the claim that the relationship between customary understandings and standard forms is a subtle and complex one in which not only is meaning conferred on the standard forms, but also understandings are established about when terms may be relied on and when they may not. In a nutshell, the role of implicit understandings derived from the contracting community of the parties can be seen as the means by which they come to know *not only what the usual written contract says, but when it can be taken to mean what it says.*

Moreover, the additional steps in the reasoning behind the enforcement of express terms can be seen as providing support for seeing express terms as nested in, or enclosed by, implicit understandings, in the sense that the meaning and significance of the express terms is drawn from the implicit understandings through which the parties understand and structure the transaction. And this point can be widened to apply not only to the approach to individual terms but to the whole process of dealing, so that the transition from negotiation to performance—which will sometimes involve a moment of conscious formation—can be understood as guided and given meaning by the parties' knowledge of how trading is conducted, and the usual expectations that arise. This perspective inverts the usual primacy of agreement, which to orthodox contract law comes first, and within which may appear implied obligations, or standards of reasonableness, which fill out gaps in the express agreement. If we start with implicit understandings, and see these as the essential precondition for the parties to engage in highly sophisticated commercial relations, these understandings frame the interaction and locate the role of express agreement as clarifying the details for a particular transaction, rather than as the primary source of obligations between the parties.

I have already suggested that the emphasis on the context within which the parties deal does not mean that the norms in contracting communities can only be those which are usually associated with relational contract law; the same neutrality applies to the present point about the nesting of express agreement within implicit understandings. Within a contracting community, it may be well understood that deal-

ing is strictly at arm's length and that no obligations are undertaken until some recognised symbolic stage of contract formation has been passed. When the law declines to enforce anything short of this, it is indeed giving effect to the implicit understandings that the parties bring to the process of dealing. Formally, the law declares there is no contract, because there is no agreement with consideration. Yet this can equally well be construed as recognising that, in the sector in which the parties trade, it is understood that this is how commercial relations are formed—in other words, the holding of no contract is justifiable by reference to the parties implicit understandings.[37]

The Reach of the Contracting Community Model

Although the contracting community model covers many of the contexts dealt with by commercial contract law, the two are by no means coextensive. An important category of commercial contracts which are not covered are those where only one side is typically a repeat player. Thus, where a supplier is selling to businesses, the large majority of which are infrequent purchasers, not only will the purchasers not develop specialist knowledge, but the recurrent interaction between suppliers and buyers necessary for participation in the creation of recognised trading practices is much less likely to exist.[38] Contracts coming into this category are those for the purchase of large capital items like major machine tools, or premises. However, the size of the organisations concerned is a variable here too, as frequency is typically a function of scale, and so larger organisations will, through centralised purchasing or procurement departments, acquire experience which will not be available to smaller firms.

[37] On this view, the doctrine of intention to create legal relations may have more substance than it is usually granted. More generally, classical law doctrines can be seen as fitting with such implicit understandings whenever these understandings are grounded on individualistic norms.

[38] An illustration of this situation is *R and B Customs Brokers Co Ltd v United Dominion Trust Ltd* [1988] 1 WLR 321, where a firm of brokers sued the seller of a defective car, and the Court of Appeal held that they should be treated as a consumer, for the purposes of Unfair Contract Terms Act 1977 s 6, because this contract was not integral to their business, and nor was it made with any regularity. The decision has been roundly criticised (in my view correctly) for applying a concept of business which was developed in an entirely different context, especially when, even if the claimants had not dealt as consumer, the exclusion clause would have been subject to a reasonableness test. Nevertheless, it provides an example of business purchasing without a contracting community.

On the other hand, the contracting community model does cover those situations where there are background understandings of which regular contractors are normally aware, but in a particular case one party says they were in fact not aware of them. This is in line with the approach of the law, which is almost invariably objective: as Lord Hoffmann emphasised in his restatement of the contextual approach, it is the understanding of a reasonable person with the background knowledge of the parties that matters.[39]

The purpose in constructing the contracting community model is to assist in clarifying the circumstances in which contract law reflects implicit understandings, and also the kind of understandings that are typically represented. The model provides a coherent setting in which implicit understandings—typically customary—can emerge along with established practices and norms which confer meaning on often complex exchange relations. In legal terms, these implicit understandings can be seen as serving two related functions: they give content to legal obligation, through both framing contextual interpretation of the meaning of express contract terms, and providing the basis for implied terms, and by conferring meaning on standards of reasonableness. And they confer a degree of legitimacy on those obligations which flow from the familiar practices of the contract community.[40]

Not all contracts are made in the context of a contracting community, and I turn below to examine the way in which implicit understandings may arise in contracting contexts which are quite different from the contracting community model, principally in the personal consumption model.

3. THE PERSONAL CONSUMPTION MODEL OF CONTRACTUAL RELATIONS

The personal consumption model is intended to identify a pervasive type of contract which provides unfavourable circumstances for the emergence of the implicit understandings associated with the contracting community model. This should foster the drawing out of the features which inhibit such understandings, and so enable the two models

[39] *Mannai Investment Co Ltd v Eagle Star Life Assurance*, n 21 above, 775.

[40] In this respect the implicit understandings mirror the classical function of express agreement.

to be used to elucidate the scope and nature of implicit understandings in situations which are not entirely covered by either model.

The Features of the Personal Consumption Model

The personal consumption model refers to contractual relations which are characterised by three principal features which typically arise in many higher value consumer transactions. First, the contracts concern complex products which require specialist knowledge to appraise. This knowledge covers a spectrum from knowledge of the technical specification of the product, its features in use, the features which differentiate it from alternative products, to knowledge about its future performance. All this applies pretty clearly not only to purchases such as domestic appliances, vehicles, household services (plumbing, electrical, building), but also to financial services such as insurance, pensions, and mortgages, credit and banking, and to professional services such as legal services and medical services.

All of these transactions will involve either experience or credence goods.[41] Experience goods are those where attributes such as quality cannot be assessed until after they have been purchased, for example a restaurant meal. Credence goods are those where, even with experience of the good, the purchaser will not be able to assess its quality—either never, or not for a long time. Examples are many financial services, especially pensions, and many legal and medical services. These concepts can be used not just to designate a whole good, but also particular attributes, so that (for example) a new car has some search characteristics (it can be test driven), some experience characteristics

[41] Experience and credence goods are concepts developed in economic theory about information, and are contrasted with search goods, where the quality and nature of the good can be assessed before purchase. For a non-technical discussion see Director of Fair Trading's report *Competition in the Professions* OFT328 (2001) para 35. See also R Ekelund *et al*, 'Advertising and Information: An Empirical Study of Search, Experience and Credence Goods' (1995) 22 *Journal of Economic Studies* 33; R Smith and A Bush, 'Towards Developing a Measure of Search, Experience, and Credence Qualities for Products and Services', available at http://www.sbaer.uca.edu/Research/2000/swma/00swma194.htm. Although I am using this classification of goods, I am not directly interested in the overall issue it is used by economists to analyse, which is market failure. I argue below that the features associated with these different goods are of use in making sense of the incidence of the social processes which generate implicit understandings.

(eg petrol consumption, reliability), and some credence characteristics (eg safety features such as crumple zones, durability of components).[42]

The feature of complexity does not itself distinguish personal consumption contracts from those within a contracting community—in many cases the products which are transacted will be the same. The feature of complexity is a necessary characteristic, which is given significance when combined with the other features of the model.

The second feature is that one party—normally the purchaser of the product—enters contracts of any single type infrequently, while the other is in business to supply the product. This is typically the case with most of the items in the list above. Although it is of course a commonplace to point out that consumers are often not repeat players when they enter transactions, the feature I want to emphasise here is that the consumer is buying in a market where all the buyers are in a similar position of not being repeat players. This has implications for the social organisation of such markets (especially for experience and credence goods), in relation to information flows, and resulting expectations, which I pursue below.

The third feature is that consumers' purchasing behaviour is typically driven by a more complex engine—individual preferences—than is the case with participants in the production and distribution system who do not actually consume the end product. Economic actors other than consumers are generally taken to be driven by an instrumental search for profit, and by virtue of being repeat players, learn what mix of products and supplies serves this goal. This contrast has a number of implications. Consumers facing a choice about a complex product which is purchased infrequently will often find that they need to discover more than information about the product—they have to discover what their preferences are. Although experience with previous purchases can form preferences in relation to frequently purchased or unchanging goods (eg food), this is less possible where the product is purchased infrequently and technical development is rapid. This is because the consumer is faced with the problem of not having had the experience of using the product which is often necessary in order for preferences to be formed. When I need a new hi-fi I can use a consumer magazine (eg *Hi-Fi*

[42] In fact it is possible to see many goods having at least some credence elements, notably where the consumer will be unable to tell whether statements about the circumstances of production are accurate, eg whether it contains genetically modified ingredients, whether food was produced organically, whether paper came from renewable forests, whether beef originated in the UK, whether clothing was made using child labour, etc.

Choice) to find out about all the features of the systems currently on sale. But such magazines cannot tell me which features I want, as many of them did not exist last time I bought a system, and it is usually wholly impractical to acquire the varied experience necessary to establish properly what my feature preferences would be.[43]

But at least with a hi-fi one may discover, quite soon after purchase, something about one's preferences; even this is not possible with many credence goods, where it may be many years after contracting before the understanding of alternatives enables preferences to be formed. The problem with pensions, for example, is not just that in many cases the nature of what the purchaser eventually gets is not known for many years (often decades), but that it may only be around the point of retirement that the purchaser will have informed preferences about the various elements which different pension packages may combine.

The combination of the three features of the personal consumption model means that the role of implicit understandings here is quite different from the contracting community model. Most centrally, it seems much less likely that customary implicit understandings will be able to emerge. A key reason for this is the quite different ways in which information is generated and dispersed.

In the personal consumption model, the market in the products concerned is characterised by the infrequent purchase of complex products. The fact that the goods will be experience or credence goods means that purchasers do not acquire and refine information about specification or performance of the goods by the experience of trading itself, but are dependent on other sources of information. In the contracting community model, individual purchasers (businesses) not only acquire information about the product from experience, but may also share knowledge with each other. This will help shape a market context in which some knowledge is taken for granted between contractors, so that many expectations which stem from implicit understandings are generalised. In contrast, in the personal consumption model, not only is the market composed of purchasers who cannot acquire the information in the same way, but the information which is in circulation will predominantly be that generated by the manufacturer or supplier.

[43] This point about the role of experience in forming preferences is distinct from the notion of experience goods. With experience goods, purchase is necessary to discover information about a characteristic of the product itself; the role of experience in preference formation is that through it the purchaser discovers whether they want that characteristic or not.

Some of this information will be detailed product specification, although this will often be of limited use for the reasons already outlined. More importantly, suppliers and manufactures rely on reputation and branding as means of transmitting information about the product, and it is recognised in marketing theory that branding is a powerful means of communicating qualities such as reliability to consumers. However, whether it is branding, reputation, or detailed product information, the fact remains that expectations are shaped by information which emanates from one side (ie supplier or manufacturer). This contrasts sharply with the contracting community model, where information about complex products is generated not only by suppliers and manufacturers, but by contractors' own experience in trading in the products in question.

The information asymmetry between suppliers and consumers in relation to complex products is well recognised, but it is not this alone which results in the absence of the customary implicit understandings which are characteristic of commercial contracting communities. Implicit understandings also concern expectations about the typical behaviour of the contracting parties in relation to how contracts are negotiated, after-sales service, how hitches in performance are treated, and how disputes may be handled. Where there are customary understandings about such matters, this means that any contractor knows not only how the supplier they are going to deal with will generally behave, but also how others are likely to behave too. Moreover, if these expectations are generalised, suppliers may well know that those with whom they deal will have these expectations about behaviour where performance issues arise. We have seen how, in contracts covered by the contracting community model, implicit understandings may include not just knowledge about the product, but also norms about how problems will be sorted out. It seems less likely that these shared normative expectations will be present in contracts covered by the personal consumption model, for the infrequency of dealing, coupled with the absence of understanding of the dimensions of complex products (especially credence goods), mean that consumers in general do not get in the position to establish such implicit understandings.[44]

[44] An example of uncertainty about trade practices is that many consumers appear uncertain about when it is expected practice to attempt to negotiate a discount, and when it is not. Uncertainty about this, which of course is typically known to a supplier, leads to a form of price discrimination, where suppliers publish prices allowing a margin for discount, but only reduce the price when necessary. The absence of any shared understandings about negotiation may also make more possible discrimination on grounds of

It is possible to identify some clear contrasts between the two models by closing in on two aspects: under the next two headings I contrast the models in relation to the role of trust and the role of standard form contracts.

Consumers, Implicit Understandings and Trust

A clear contrast between the personal consumption model and the contracting community model can be seen in the role of trust.[45] In one sense, given the emphasis that many firms place on cultivating a reputation as a reliable provider of goods and services, one might expect to find that trust figures prominently in this contractual model. However, although trust does exist, it is in a significantly different form from that encountered in the contracting community model.

Although it is plausible to suppose trust flourishes most readily where the parties are known to each other, trust may arise between strangers, and it is normal in many consumer contexts. Thus large retailers will, through their customer service policies, typically wish to maintain consumer confidence in the quality of the products they sell. Similarly, manufacturers of brand named goods will go to great lengths to maintain brand integrity.[46]

However, although consumer contexts may exhibit trust in this way, it is nevertheless very different to that encountered in commercial contracting communities. The trust tends to be very much one sided, in that consumers are trusted hardly at all—for example, credit is normally only available when the risk can be transferred to a credit card company or other source of consumer credit. But the role of implicit understandings in permitting trust in commercial contexts helps to focus on what element is missing in many consumer contexts.

race and gender; see I Ayres, 'Fair Driving: Race and Gender Discrimination in the Retail Car Market' (1991) 104 *Harvard Law Review* 817, where the discrimination in the face of identical negotiation strategies deployed by customers in the retail car market is clearly demonstrated.

[45] By trust here I refer to the situation where one party voluntarily exposes themselves to the risk of opportunistic behaviour by the other.

[46] The classic instance of the prompt withdrawal of Perrier Water from shops across the world following the discovery of contamination by benzene has found its place in textbooks on marketing: eg S Dibb *et al*, *Marketing: Concepts and Strategies* (Boston, Houghton, Mifflin, 2001) 519.

It is possible to distinguish two different dimensions where one party trusts another to do (or not do) something. One is the factor already noted, ie the willingness to be exposed to the risk of the other behaving opportunistically by not performing. The other dimension is the content of the trust, ie the thing which the person trusted is trusted to do, and it is in relation to this that implicit understandings play a significant role. Some of the content of the trust will be spelt out by the main terms of contract—the price, the basic nature of the product or service being supplied. Much will not be spelt out, especially the incidentals of performing certain contracts, or what happens if the performance miscarries in some way. These are precisely the matters that are, in many commercial contracts, settled by implicit understandings—the parties know how the goods are packaged, how payment is typically made, what happens when a subcontractors' work is slightly substandard, and so forth.[47] Sometimes, these matters can be settled by general implicit understandings, and owe nothing to any customary knowledge of the trade. But equally, sometimes more specialist knowledge is necessary to give content to these expectations, which, where a contracting community exists, can be supplied by customary implicit understandings. Where no such contracting community exists, trust becomes problematic: one party may in principle trust the other, but trust them to do *what*?

Ignorance about the content of trust is clearest in relation to credence goods, for example legal or medical services, where the client or patient typically cannot assess the quality of what has been done. In these contexts, there are professionally defined obligations—the doctor's obligation to act in the patient's best interests, or the solicitor's fiduciary duty to act in the client's interests, not his or her own. These obligations place clear limits on the pursuit of self interest by such service providers, although they do not take the form of norms which are shaped by the practices of contracting community involving the recipients of the services, but stem instead from professional organisation or public regulation. In these contexts, the fact that the recipient of the service does not understand or know the content of the thing the provider is undertaking to do is dealt with by imposing an obligation to act in the recipient's interests. But, beyond these fiduciary-type cases,

[47] Indeed, the cost reducing function of trust, in avoiding the need to spell out all the obligations at the outset, depends upon the parties trusting each other that reasonable expectations will be met.

the content of trust, where this has not been spelt out, may be non-existent, because it will not have been formed by the emergence of implicit understandings. In this sense, the trust is open ended, and open to abuse. Thus, a bank may wish to be trusted by its ordinary private customers; this may unproblematically include the expectation that the bank will deal honestly (eg will produce statements which are not deliberately falsified), or will do those things the bank undertakes to do. But, beyond this, what is the content of trust that a consumer should expect? Does it, for example, include an expectation that the bank will inform customers when it introduces more favourable accounts than the ones they currently use?[48]

Where a service is bespoke—in that it is tailored to the circumstances of each customer—and it also has credence good characteristics, trust is even more problematic; the building trades provide a good example. From a private householder's point of view, plumbing or electrical services have large credence elements, and they will not be in any position to tell whether standard practices and specifications have been observed, nor how contingencies such as a change in materials, delay, or defective materials would usually be handled. In contrast, where the same trades are being employed on a construction project by a main contractor, it is plausible to suppose that, not only will monitoring of the plumber or electrician be more apparent (and thus less necessary), but there will be some understandings regarding the handling of contingencies.

The reach of trust thus depends upon the contractor having an expectation of the content of the trust (ie what the other will do), and on them being able to assess whether that thing has been done. Where the contractor being trusted knows that the other has such expectations, and can assess the outcome, they will be inclined, for reputational reasons, to justify the trust and do what is expected: trust places normative boundaries on the opportunistic pursuit of self interest.[49] In the contracts covered by the personal consumption model, it is much less likely that consumers will form these expectations and be able to assess whether they have been met, and so the ultimate policing of trust—the concern with reputation—is weaker as an influence on behaviour.

[48] This can arise whether the customer is a borrower or a lender; for examples, see the references to the Banking Code at n 72 below.

[49] For discussion of loss of reputation as a sanction in relation to contracts, see D Charny, 'Non-Legal Sanctions in Commercial Relationships' (1990) 104 *Harvard Law Review* 373.

The Taming of Standard Forms

It has long been recognised that standard forms pose particularly severe problems in consumer contracts. Many suppliers produce one-sided sets of terms, which aim to protect the interests of the supplier, and which are provided on a take it or leave it basis.[50] Although there is widespread recognition that these terms can often be oppressive, there is much less agreement about what the precise basis of the objection is. A recurrent theme in the critique of standard forms is that they have not really been agreed by the party who is confronted with them.[51] I will argue that it is useful to understand the problem with standard forms in terms of the absence of the customary implicit understandings which prevail in many commercial contexts. To establish this, I will identify the ways in which a standard form contract may be 'tamed': that is, the way in which a standard form may be rendered less objectionable by the circumstances in which it is used.

First, the terms may be the subject of express negotiation by the parties to the contract in question. Strictly, such negotiation would mean the terms are no longer standard terms, and so the objection of absence of agreement could not apply.

Secondly, the terms in question may have been the subject of term-shopping. This is a mechanism that can, in theory, result in terms being treated as the product of consent of the parties even where they are presented by any individual supplier on a take it or leave it basis. The argument is that, where different suppliers offer different standard forms, customers can, if the terms are visible to them, 'shop' for the more favourable terms by not contracting with the suppliers offering the less favourable terms.[52] As long as there is a sufficient margin of term shoppers, then the less favourable terms should be driven out; this happens without any need for negotiation, in the same way that price competition can take place without any haggling over prices. Term

[50] Various explanations for this phenomenon are possible, including the exploitation of monopoly power. See T Rakoff, 'Contracts of Adhesion—an Essay in Reconstruction' (1983) 96 *Harvard Law Review* 1174 for analysis of this position, and the argument that contracts of adhesion are explicable as the attempt of an organisation to exercise control over its internal processes.

[51] For a discussion of economic rationales for intervention, see MJ Trebilcock, 'An Economic Approach to the Doctrine of Unconscionability' in BJ Reiter and J Swan (eds) *Studies in Contract Law* (Toronto, Butterworths, 1980) 379; also H Beale, 'Unfair Contracts in Britain and Europe' [1989] *Current Legal Problems* 197, 199–201.

[52] See papers by Trebilcock (n 51 above) and Rakoff (n 50 above).

shopping can only occur where the terms are visible, and a sufficient margin of customers shop for them.

The 'taming' effect of negotiation and term shopping principally lies in the ability of customers to influence, by withholding consent to trade, the content of the terms. Taken at face value, neither negotiation nor term shopping would appear to require implicit understandings shared by the parties—at least as far as the term in question (negotiated or shopped) is concerned.[53]

Thirdly, a standard form may not be the one sided production of a supplier, but rather be the product of negotiation by the trade association or other bodies representing the various interests in a commercial sector. A clear example of this is the JCT family of standard forms used in the construction industry. These forms are drafted by the Joint Contracts Tribunal, on which is represented main contractors, surveyors, clients, architects and the like. These contracts are not designed to protect the interests of one side against another, but aim to achieve a balance of the interests concerned.[54] This kind of form will require the existence of a developed contracting community with established institutions which can undertake the work. The standard form is 'tamed' here not by the agreement of individual contractors who use it, but by a process of representative negotiation which means that drafting reflects the balance of interests, and so one sided terms are more likely to be eradicated.

The fourth way in which standard forms may be tamed is where the standard form—possibly one framed by the process just described—may be widely used across a market sector, and thus become well known through usage.[55] In this process, knowledge of what the terms

[53] However, even if a contractor has adequate knowledge of the term in issue, negotiation or term shopping can only be rationally conducted where there is some knowledge of the other terms which are not being negotiated or term shopped. As Rakoff points out, the risk is that, as visible terms are negotiated or term shopped, a contractor may be making non-maximising decisions in relation to the less visible terms which are also being affected: Rakoff, n 50 above, 1226.

[54] Other examples are the bills of lading, standard conditions for the sale for land, and commodities contracts. Note that one reason why the clause in *Mitchell (George) (Chesterhall) Ltd v Finney Lock Seeds* [1983] 2 AC 803, which limited the liability of a seller of seed, did not pass the statutory test of reasonableness was that it was promulgated by the seller's trade association without any consultation with representatives of farmers.

[55] For clear examples where forms were not incorporated by signature or notice but became part of the contract on this basis see *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] AC 31 and *British Crane Hire Corporation Ltd v Ipswich Plant Hire Ltd* [1975] QB 303.

mean—or more accurately are treated as meaning—will be disseminated by participation in the practices of a contracting community, a clear example of which is that of shipping. The knowledge which is diffused is not so much knowledge of the bare content of terms, but knowledge also of the circumstances with which they deal, and how and when they are usually invoked. Here, informally acquired knowledge will become embedded as customary implicit understandings, and, if the law gets out of line with such understandings, it may on occasion be made to swerve to reflect them.[56]

The fifth way is closely related to the fourth. Not only may a practical understanding of what the terms means become diffused as a recognised practice, but those practices may include the expectation that a party who is favoured by a particular term does not insist on it being enforced. In other words, a gap opens up between the formal meaning of the term and the actual practice of the parties.[57] Again, where the terms are used widely in a sector, it is possible for knowledge of the gap to be effectively part of the knowledge of what the terms mean. Bernstein's work makes clear the often subtle way in which informal understandings interact with the letter of the contract.[58]

Of the five ways in which standard forms can be tamed, three require the existence of a contracting community, in which customary understandings can be established. The two methods which may (at least in theory) work without implicit understandings—negotiation and term shopping—are in any case of debatable significance in relation to the content of standard forms.[59] Moreover, not only do the other three methods provide a way of removing one sided terms (or policing their use), they also provide an additional legitimacy for the terms which are

[56] The classic instance of this is the decision in *New Zealand Shipping v Satterthwaite* [1975] AC 154 where the commercial expectation that a third party (stevedores) was covered by a limitation clause in a bill of lading was vindicated by inventing a collateral contract to which they were party.

[57] For discussion of this gap see Macaulay, 'Relational Contracts on A Sea of Custom', n 3 above; see also the chapter by Campbell and Collins in this volume, which points out that in *Mitchell (George) (Chesterhall) Ltd v Finney Lock Seeds* [1983] 2 AC 803, when the House of Lords held that the limitation was unreasonable because it departed from usual practice, it was applying an implicit understanding of the trade. Where a gap is established between a practice and what a term provides, it does of course make term shopping more difficult: term shopping can only be rational, in the presence of a gap, where the contractor actually becomes acquainted with the practice.

[58] See articles by Bernstein, n 14 above.

[59] Even its advocates recognise that term shopping is only possible under relatively limited circumstances; for a rejection of the approach see VP Goldberg, 'Institutional Change and the Quasi-Invisible Hand (1974) 17 *J Law and Economics* 461.

regarded as part of the contract. Thus, if we defend the legitimacy of the terms in standard forms *solely* on the basis of some technical act of consent like signature, then not only is it difficult to justify the one-sided terms, but there is no more reason, *stemming from the mere act of signing*, for regarding the less objectionable terms as legitimate: standard forms are not read, still less understood. However, where terms are used in contexts where there are customary implicit understandings, not only are the inappropriately onerous terms likely to be removed or not relied upon, but those that are left are more likely to be seen as the product of a more legitimate process of consent.

If we now turn to the consumer context, we can see that the typical absence of customary implicit understandings lies behind some of the recognised problems with standard forms in consumer contracts. Most obviously, the third method—negotiation between representatives of interests—does not occur in consumer contracts, and this means that consumer contracts are typically drafted to protect the interests of the drafting party.

But it is the absence of the final two methods which arguably makes the enforcement of standard forms in consumer contracts especially unsatisfactory. Both methods involve the acquisition of knowledge of what the terms are usually taken to mean, which may or may not reflect their plain meaning. When this is coupled with knowledge about the circumstances with which the terms are intended to deal, and how performance problems will be handled, the parties will share understandings about what the terms mean in practice. But in contracts covered by the personal consumption model, it is much less likely that these processes can emerge, with the result that consumers do not learn of the terms, nor their usual meanings, and nor do they acquire practical knowledge of the circumstances which they are invoked. Moreover, it is also much less likely that recognised understandings will have developed around how the eventualities with which the standard forms terms deals will actually be handled in practice.[60]

It is also plausible to suppose that the gap method will be unusual in the consumer context, because there will not typically have been the frequency of contracting to establish diffused understandings about the practice in relation to the terms. This is not to say that suppliers invariably enforce terms against consumers when entitled to do so—indeed

[60] One way of investigating this claim would be to select a sector where firms routinely supply both business and private customers—possible examples may be found in the construction trades.

there is clear empirical evidence to the contrary.[61] Where the consumer context arguably differs is that there may be no generally known *practice* of not invoking the strict terms which the contractors will know or anticipate, because consumers will not typically form a contracting community within which such an expectation can be formed. This means the supplier can choose when to make a concession—in other words, they can 'concession discriminate', and allow the granting of concessions to be purely guided by their own self interest.

In summary, I am suggesting that the significance of implicit understandings in relation to standard forms is twofold. First, it is plausible to suppose that these understandings within a contracting community play an important role in 'taming' standard forms—by eliminating inappropriately onerous terms, by communicating the practical consequences of particular terms through the establishment of trade practices, and by fostering a contracting culture in which the practice not to enforce terms may become embedded. And the accumulation of experience and the sharing of background understandings about how contracts typically function in a sector may thus amount to a more powerful legitimating reason for holding the parties bound to terms which reflect practice than any act of express consent at the technical moment of formation.

Second, the absence of customary implicit understandings in the personal consumption model means that they cannot operate to tame or justify standard forms. Thus, it is not so much the lack of express agreement to the terms that renders them objectionable, but rather the fact that they are used in a context which, because there is no contracting community, is deprived of the social processes which may disseminate the knowledge, practices and norms which may make the resulting standard form a workable piece of self-regulation.

The Reach of the Personal Consumption Model

The two models are intended to capture the basic situations which are probably the most and least favourable to the formation of implicit understandings. Although many familiar contracting situations fall within them, some are not covered at all, or display some features of

[61] See W Whitford 'Strict Products Liability and the Automdobile Industry: Much Ado About Nothing' 1968 *Wisconsin Law Review* 83, 143–53.

both. Thus the models are not intended to divide neatly all commercial contracts from all consumer ones. For example, many contracts made by individuals in a private capacity are not covered by the personal consumption model. Purchases of simple products for cash—typically search goods—are not covered, and this exclusion makes sense as there is much less scope or need for the generation of shared understandings to provide a context in which transactions are carried out.

The situation where a product is purchased frequently also falls outside the model. Here, the fact that the market is adjusted to frequent purchase means that information will be gained by experience and so leave the consumer less dependent on suppliers. Where there is also recurrent experience of performance which miscarries, it is also possible for practices to develop about how these situations are typically handled.[62]

There are also some kinds of commercial contracts which display features of the personal consumption model. One is the situation already mentioned where the small or medium sized organisation purchases a large value item which, for it and most others typically buying in that market, is an infrequent transaction.[63] The same problem about the lack of customary implicit understandings built up in a contracting community can arise here too, although, the third feature of the personal consumption model, the pursuit of utility rather than profit, does not apply.[64]

A further use of the models is that they can be used to assess the prospects of customary implicit understandings in contract types that do not involve the same element of supply which is assumed in both of the models. For example, residential tenancy contracts differ from the personal consumption model in that there is no good or service supplied, and there seems to be a greater opportunity for the tenant to

[62] However, even here, there may be elements of a product about which it is difficult for the consumer to acquire knowledge; food is a notable example. Although food is a very highly differentiated product, with massive choice being communicated through branding, marketing and labelling, most foods still have some credence good characteristics, eg the amount of pesticide residues.

[63] This absence of contracting community can be combatted by small firms pursuing their interests through a trade association, so enabling them to obtain some of the benefits of being repeat players which may accrue to large organisations.

[64] One use of the analysis in terms of ideal type models is that it can identify hybrid or mixed contexts, which exhibit features of more than one model. An example is where there is a contracting community in the sense I have described, but a subset of the participants are infrequent contractors who, as a result, do not in fact share the knowledge of its practices, which will have been shaped by regular participants.

etablish understandings with a landlord over the period of a tenancy. Nevertheless, there will still typically be no contracting community, because individual tenants will tend not to contract with different landlords with any frequency, and so generalised customary understandings may well not develop. Without this background, the law may still find it difficult to give content to matters which were not rendered explicit.[65]

Another example is those contracts by which a person becomes a member of an institution, for example a trade union. These too are not readily characterised as 'supply', and will also typically sustain a long term relationship that may last many years. Yet, despite the thicker nature of the relationship between a member and an organisation, the 'market' in membership does not consist of frequent changes of allegiance, with the result that members are also not repeat players who establish with a number of 'suppliers' the background understandings which are typical of the contracting community model. Thus, when the courts have imposed an obligation on the organisation to treat the member according to the principles of natural justice, this is difficult to explain as deriving from the implicit understandings of a contracting community in which such shared expectations have been developed.[66]

In yet another category of contracts, the background understandings which the parties carry though a relationship are shared but not customary. This is the case with intimate relations (eg cohabitation) where the parties have not adopted an explicit cohabitation contract, but have reached tacit understandings about such things as the disposition of property or financial support. The law (especially in the UK) has been resistant to finding anything contractual in these relationships, and part of the reason for this may be that there will rarely be any contracting community available as a source of customary norms to be applied. However (as I have argued elsewhere) it is possible to see in some of these relations definite shared understandings which are implicit rather than express, and which deserve legal recognition.[67]

[65] See *Liverpool City Council v Irwin* [1977] AC 239, discussion at n 76 below.

[66] *Lee v Showmen's Guild* [1952] 1 KB 189; see also D Oliver, *Common Values and the Public Private Divide* (London, Butterworths, 1999) 177–86. The position is similar in the relationship between a student and a university: see J Wightman *Contract: A Critical Commentary* (London, Pluto Press, 1996) 122–36.

[67] See J Wightman, 'Intimate Relationships, Relational Contract Theory, and the Reach of Contract' (2000) 8 *Feminist Legal Studies* 93, 105–13.

Overall, the significance of the personal consumption model is that it identifies a widely found set of conditions which appear unpropitious for the development of the customary implicit understandings which are typically recognised in traditional contract law. Where all these characteristics are found together, a situation will fall entirely within the model, but equally it is possible to identify situations where only some of the characteristics will be found. In some of these (such as membership contracts), the credence characteristics will still be found, despite a long-term relationship between the parties. However, the absence of customary understandings does not mean that in situations displaying some or all of the features comprising the model there are no expectations nor understandings at all; there typically are, and the question thus arises of what, if anything, should be made of them. I now turn to examine that general issue.

4. BEYOND CUSTOMARY UNDERSTANDINGS

Given that the law relies on customary implicit understandings, what should happen when, because of the contracting context, these are thin or non-existent? I explore this below, but first turn to consider why the absence of such understandings should matter.

The Absence of Customary Understandings

It might be argued that, when contracting takes place in a context which is not rich in customary understandings, this is because the type of contracting in question has no need for them. This is partly true, but goes too far. Contracts covered by the contracting community model tend to be more relational, and hence less discrete, than contracts covered by the personal consumption model. However, this does not mean that all contracts covered by the personal consumption model are discrete in this sense.

It is possible to identify contracts which are of a discrete, or one shot kind which lack the relational dimension which is arguably necessary for customary implicit understandings (in addition to general understandings) to develop. An instance of this is Macneil's original stock example of the discrete contract—'the cash purchase of gasoline at a station on the New Jersey turn pike by someone who rarely travels the

road'.[68] Here, customary implicit understandings do not exist. Conventions about payment are general, and the goods are identical to goods elsewhere (partly through regulation). There seems no need for customary implicit understandings because of the uniform expectations about what is received, its delivery and payment, and the apparent extreme rarity of any failure by the goods to correspond with the expectations formed about them; general implicit understandings are enough.

However, the position is different in relation to the infrequently purchased complex products which figure in the personal consumption model. Although these contracts may not be seen as particularly relational, in that the parties only come together for these sales, and there is typically no longer term relation between the parties,[69] these one shot sales nevertheless differ from the petrol example because they can be said to be *potentially relational*. By this I mean that in their nature, exchanges of this kind may lead to further contact and relations between the parties, usually arising out of problems in performance. In contracts covered by the contracting community model, implicit understandings may develop about how these issues will be dealt with—they may or may not embrace norms requiring high degrees of co-operation, but shared expectations about what will occur are possible. Where such problems arise in contracts covered by the personal consumption model, there is a gap in the parties understandings: although the supplier is likely to have encountered the situation before, for each consumer it will normally be the first time, and they will not have any expectation which derives from generalised practices in the sector that, in the case of the contracting community model, derive from previous shared handling. The upshot of this is that, in contracts covered by the personal consumption model, the functions that are performed elsewhere by implicit understandings remain unperformed.[70]

[68] 'Contracts Adjustments of Long-term Economic Relations Under Classical, Neoclassical, and Relational Contract Law' (1978) 72 *Northwestern University Law Review* 854, 857.

[69] Even where the consumer buys a succession of electrical goods from the same store, the transactions are typically treated wholly separately, and it would seem rare, after the retailing revolution, for face-to-face relationships to be established or endure between individual shoppers and staff in (for example) a large out-of- town electrical goods store.

[70] Perversely, this can also be true of contracts which may look very relational. Some contracts that consumers enter into may be very long term indeed, like a mortgage, yet there may be no actual contact between the parties, beyond the sending of statements and adjustment of standing orders for years (not even this with direct debit). It may only be when (say) an endowment mortgage fails to generate the expected returns 25 years later that parties have cause to speak. In terms of face-to-face relations, this is a discrete contract where the performance happens to be very spread out.

And the result of this is that the behaviour of the supplier is not disciplined by norms which encapsulate the reasonable expectations of the consumer, with the further consequence that, when legal determination is needed, it cannot draw on such expectations in framing obligations. We can thus identify a category of 'gap' situations where performance issues may arise which, in a mainstream commercial context, would be resolved by reference to customary understandings, but because of the context, lack this resource for the resolution or avoidance of disputes.[71]

Although there may be gaps in the customary implicit understandings in contracts for infrequently purchased complex products, it does not follow that there are no implicit understandings about the matters at all. It is here where shared understandings run out and we encounter the possibility of divergent or unilateral understandings, ie where the parties do not expect the same thing. One response is for the law to use these unilateral understandings in dealing with the gap.

Unilateral Expectations

The basic feature of unilateral expectations is that the assumptions which the parties bring to contractual relationships are different, and these are not aligned in the process of negotiation and performance. But a discrepancy in the subjective expectations is not enough, for this can happen in many commercial contexts. In addition, there must be no background of customary understandings which enables one to say that one party's set of assumptions are reasonable and the other's are not. For example, a mortgagor may have assumed that he or she would be able to redeem without penalty the mortgage which they have taken out to purchase their home, while it may be the practice of the bank or building society—expressed in a standard form which has been signed—to require a substantial release payment.[72] Each side may have formed an expectation about what happens which, as far as they

[71] The debate about 'default rules' addresses how gaps in the contract should be filled. One way of filling the gap is through custom and usage; my point is that this will be a less productive method in contracts covered by the personal consumption model than in contracts covered by the contracting community model (see Riley, n 28 above).

[72] This is somewhat analogous to the more complicated facts of the first case to be referred to the courts under the Unfair Terms in Consumer Contracts Regulations: *Director General of Fair Trading v First National Bank plc* [2002] 1 AC 481. These kind of unilateral expectations have posed serious problems in relation to financial products, and in 1992 the banks produced the Code of Good Banking Practice (now the Banking

are concerned, appears reasonable, and there is in this situation no customary understanding, shaped by the practices of a contracting community, which can provide the answer. As a result, it will often be more difficult to apply standards of reasonableness, since the court cannot give content to that standard by asking what the established understandings in that contracting sector are.

In at least some of the situations covered by the personal consumption model, there are cogent reasons why these expectations should be taken seriously. First, the nature of the informational asymmetry means that the supplier will have typically played a major role in establishing the information base on which the consumer relies. This applies not just to the hard information supplied in leaflets about (say) a financial product, but also more general output in the form of advertising and other marketing activity. This information conveys not only data about different products, but also, perhaps of more importance, impressions about reliability, trustworthiness, economy, as well as more diffuse social meanings and images which are attached to goods. In traditional legal terms, the further the supplier strays from hard information, the less likely it will be that they are held responsible for the content. Yet, where goods with credence chararacteristics are concerned, it may well be precisely the more diffuse communication about reputation, reliability etc which is influential, and which is targeted by suppliers in their marketing activity. Arguably, where suppliers are predominantly responsible for virtually the whole informational context in which a consumer acts, they should comply with the reasonable expectations which this engenders, even where these expectations are at odds with the express terms of the contract.

This argument is fortified by the fact that, as discussed in the context of trust, suppliers are not, despite the potentially massive informational asymmetry, acting in a fiduciary-type capacity. The problem that was posed in giving content to open-ended trust is an example of a wider phenomenon which exists wherever an organisation is simultaneously boasting of its customer service focus, and attempting to maximise its returns. Inevitably, profit-seeking firms do not pursue customers' interests in a fiduciary sense—this might involve recommending a cheaper or better competitor. They may well wish sincerely to meet customers expressed desires, while at the same time attempting

Code). The Banking Ombudsman (now the Financial Services Ombudsman) has also been critical of a variety of practices. See http://www.financial-ombudsman.org.uk/publications/ombudsman-news/banking/about-september.htm

to extract profit from other aspects of the deal. For example, an OFT report concluded that the selling of extended warranties on domestic appliance by electrical retailers was operating contrary to the consumers' interests.[73] The focus on customer care in marketing and reputation building may well mean that a supplier will go to great lengths to keep consumers content. However, the underside may be that, in activities invisible to the public, strategies are hatched to maximise returns by taking advantages of informational asymmetries and the absence of customary understandings which can, in a contracting community, set boundaries to the pursuit of self interest.[74]

Thus, in the kind of contracts covered by the personal consumption model, there may well be good reason for holding a supplier to the unilateral expectations which a consumer may have acquired as part of the transacting process—even when these do not reflect actual practice.[75] We now turn to see how far this kind of expectation is recognised in the law.

[73] It was found that the practice of 'bundling' the extended warranty with the sale, so that the warranty could only be bought with the appliance, coupled with the absence of alternative prices, or the incidence of the breakdowns which the warranties covered, meant that overcharging was taking place. (OFT 1994). Another strategy which belies the appearance of customer care is 'informational noise' where firms, by artificial over-differentiation of models and deals (eg cookers, mobile phones, pensions) make comparison impossible or too time consuming, which in turn will lead to differential pricing. Credence goods are especially susceptible to this: see generally *Consumer Detriment Under Conditions of Imperfect Information*, Office of Fair Trading Research Paper 11 (1997).

[74] An example of price discrimination can be seen in the practice of some banks and building societies in relation to certain new accounts. In the fight for more investors, one strategy is to advertise a new savings account with a very competitive rate. Some time later, a new marketing campaign will announce another new account, paying a similar rate. Meanwhile, the interest rate on the first account is edged back, and no new investors are offered it. Some investors will transfer to the new account, but those that stay in the old account will suffer price discrimination ie, will be paid less for the use of their money. The result is that the institution can maximise the number of new investors by offering rates of interest which do not have to be paid to all existing investors. The neatness of this (as with most price discrimination) is that the ones who lose out do not generally realise they have lost. This formerly prevalent practice is now being tackled by the Financial Services Ombudsman: see URL at n 72 above.

[75] Much more difficult are instances that concern more incidental aspects of a transaction, where the purchaser has no expectation at all, because the issue which crops up had never crossed their mind until it arises. It is much more difficult for expectations to provide content for any obligation here. Even so, the purchaser may well, retrospectively, take the view that what is now being offered or expected of them is not what they would have expected, had they known and understood the possibility. Although this is in one sense an expectation with the benefit of hindsight, which in traditional legal terms comes too late to shape obligation, the purchaser may be seen as crystallising an expectation that is atemporal, in that, had they understood and experienced this outcome before entering the contract, they would have formed the same expectation as they in fact formed when the performance issue arose.

Legal Recognition of Unilateral Expectations

Overall, the ordinary rules of contract law do not appear to be well adapted to recognising implicit understandings which are not customary. The usual tests for implied terms will not normally reflect expectations which are unilateral in this sense, because these tests arguably work best when there is a contracting community to provide a set of practices and meanings on which the courts can draw. For example, in *Liverpool City Council Irwin*,[76] the Council provided a 'tenancy agreement' to residential tenants of their flats which only contained the tenant's obligations and not the Council's. It was eventually held by the House of Lords that, under the test of necessity for the implication if terms, that the Council owed duties relating to the upkeep of common areas such as the lift and rubbish chute. However, difficulty was experienced in framing the duties, and this was arguably due to the fact that the court did not see the case as an instance of a general category of case in which the purposes and background understandings are well known. The House of Lords did not, for example, refer to other arrangements on blocks of flats, and instead attempted to derive the obligations on the basis of what was necessary. This, however, seemingly places no weight on the expectations of the tenants, which, had there been an operative contracting community, may well have shaped the background understandings on which the court would otherwise have drawn.[77] As it was, the enquiry into what was necessary muffled any explicit analysis of what the council tenants' reasonable expectations may have been regarding the maintenance of lifts etc.

[76] n 65 above.

[77] Another case where absence of a contracting community can be seen as posing problems for implication is *Reid v Rush Tompkins* [1990] 1 WLR 212. The claimant was an employee of the defendant working in Ethiopia, and was badly injured in a road accident which was not the defendant's fault. The claimant argued that there was an implied term in the contract of employment, either requiring the employer to provide insurance cover for accidental injury, or requiring the employer to inform the employee that insurance cover was essential given the conditions which prevailed in Ethiopia. This was rejected by the Court of Appeal on the basis of the test of necessity in *Liverpool City Council v Irwin*. Although not developed here, it is arguable that this case goes against a trend in employment law which has seen the courts prepared to develop terms that vindicate unilateral expectations; see in particular *Scally v Southern Health and Social Services Board* [1991] IRLR 522, *Spring v Guardian Assurance* [1994] 3 WLR 354, and *Malik v BCCI* [1998] AC 20.

Perhaps the main obstacle to the recognition of unilateral expectations has been the objective principle of agreement. Where there may be doubt about what the parties have agreed to, then what matters is how the offer or agreement would appear to a reasonable contractor. This has tended to involve applying a standard of objectivity drawn from the practice of the contracting community in question, and so results in those contracting in such situations being treated as having the usual background knowledge. It is more difficult to apply the objective principle where there is no contracting community to define the standard on which the courts may draw, yet this has not resulted in the courts using the principle to deprive terms (eg in standard forms) of effect where they have been incorporated into the contract.[78] Most of the situations covered by the personal consumption model involve standard forms, and these have caused serious problems for the law.

Once such terms have been incorporated into the contract by signature, there is little that can be done to reflect unilateral expectations other than through construction techniques.[79] Part of the problem here is the legacy left by the foundering of the English common law's attempt to deal with the standard form in non-commercial situations. The doctrine of fundamental breach was developed around the middle of the twentieth century as a means of dealing with onerous clauses (mainly exception or exemption clauses) in signed contracts. It developed out of a number of doctrines established in a commercial cases, notably deviation, which had been used as an aid in the construction of onerous terms. In the precursors of fundamental breach, attempts were made to construe the offending express term with reference to the main object or purpose of the contract.[80] This was plainly a contextual construction of the term, which looked beyond the term itself to the background knowledge and understandings the parties brought to the

[78] See JR Spencer, 'Signature, Consent, and the Rule in *L'Estrange v Graucob*' [1973] CLJ 104, where it is argued that it was open to the court in *L'Estrange v Graucob* [1934] KB 394 to hold, on the basis of the objective theory, that the terms were not part of the contract.

[79] The exception is a case like *Schroeder Music Publishing Co Ltd v Macaulay* [1974] 1 WLR 1308, where a standard form contract confining musicians' ability to record and compose for others was held invalid under the restraint of trade doctrine and so contrary to public policy. The public policy doctrine has not otherwise been used to handle standard forms, although there are cases which suggest this would not have been unarguable; see eg *Johnson v Moreton* [1980] AC 37, where the doctrine was used to render invalid a clause depriving an agricultural tenant of security of tenure conferred by statute.

[80] See eg *Glynn v Margetson*, n 23 above; Coote, n 24 above, 94–98.

contract. Virtually all the cases in which construction techniques were used concerned contracting communities, mainly concerned with the carriage of goods.

The construction approach was put under pressure in consumer cases where a clause was duly incorporated into the contract, and was not ambiguous, yet it apparently entitled a seller (for example) to deliver a heap of scrap instead of a car. It was of course obvious that such a clause defeated the reasonable expectation of the buyer, and in the 1950s and early 1960s doctrine emerged—mainly in consumer cases—which went beyond being a rule of construction, and became effectively a rule of law that some obligations could not be excluded. Considerable confusion reigned even after the rule of law approach was rejected by the House of Lords in 1966, and legislation was eventually introduced to handle the problem.

Although the legislation provided a much clearer and more satisfactory approach to exclusion clause cases, the effective abandonment of the common law doctrine meant that no principles were developed which directly addressed the problem of the unilateral expectation. The 'rule of law' cases like *Karsales (Harrow) Ltd v Wallis*,[81] or *Levison v Patent Steam Carpet Cleaning Co Ltd*[82] can be seen as an attempt to recognise that there was a problem in treating a clause as part of the contract when it was so plainly contrary to the reasonable expectation of the consumer, but no principled recognition of this was adopted in the general law of contract.[83]

Legislation since the 1970s can be seen to address clearly the problem of these unilateral expectations. Especially notable is the provision in the Unfair Contract Terms Act 1977 which imposes a reasonableness test on a clause by which one person claims to be entitled to render another a contractual performance substantially different from what was reasonably expected.[84] Similarly, the regulations implementing the directive on unfair terms in consumer contracts can be seen as a response to the problems of unilateral expectations, although expecta-

[81] [1956] 1 WLR 936.

[82] [1978] QB 69.

[83] It is possible that a contributory factor may have been that a construction approach, informed by context, was more adapted to dealing with commercial contracts because these tended to display customary implicit understandings which shaped the process.

[84] See s 3, which is however confined in its scope by Sch 1: the Act does not apply to contracts of insurance, contracts relating to an interest in land, and contracts creating or transferring securities, thus excluding contracts for most financial products.

tion is not used as a test of validity in either the general principle of good faith, or in the 'grey list' terms in the Unfair Terms in Consumer Contracts Directive.[85]

These provisions appear to deal with many of the substantive problems, but it is striking that they do so without disturbing the underlying basis of common law principle. Although a wider scope is granted to unilateral expectations where the issue is the incorporation of written terms by reasonable notice,[86] the common law approach to written terms which are signed remains inhospitable to the recognition of unilateral expectations.[87] The Directive on Unfair Terms in Consumer Contracts is less restricted than the Unfair Contract Terms Act 1977, but its capacity to recognise the unilateral expectation in relation to standard forms is limited in two ways. As it is confined to consumer contracts, it cannot apply to commercial or other kinds of contracts which display features of the personal consumption model. And it does not apply to contracts made before 1995, which means that many long term contracts relating to mortgages, pensions and life insurance are beyond its scope. In a recent consultation paper, the Law Commission has proposed a rationalisation of the law now contained in the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contracts Regulations 1999, and, although the proposals relating to consumer contracts mainly simplify the two regimes, in relation to commercial contract more striking changes are provisionally proposed.[88] Currently, the provisions of UCTA relating to business to business contracts only affect contract terms which attempt to exclude or limit a liability, or which entitle the defendant to render a performance substantially different from that which was reasonably expected.[89] They do not catch terms which seek to impose or modify the other party's obligations, for

[85] For other piecemeal reforms which can be seen in the same way, see the cooling off and cancellation rights contained in the Consumer Credit Act 1974, Timeshare Act 1992, Consumer Contracts (Distance Selling) Regulations 2000.

[86] The emphasis in the leading case of *Parker v South Eastern Rlwy* on what the party on the receiving end of the ticket or notice would reasonably expect it to contain has meant that this doctrine can work well where there is a contracting community *and* where there is not. Thus, in *Interfoto Picture Library Ltd v Stilletto Visual Programmes* [1989] QB 433 the court could refer to reasonable expectations about the usual rate for overdue slides (against which the plaintiff's rate was very high), while in consumer cases (like *Thornton v Shoe Lane Parking* [1971] 2 QB 163) unilateral expectations of consumers—which may diverge from corporate practice—could be reflected equally well.

[87] *The Principles of European Contract Law* contain provisions which could be the basis of a challenge to terms which defeat a unilateral expectation; see n 27 above.

[88] *Unfair Terms in Contracts*, Law Commission Consultation Paper 166 (2002).

[89] s 3(2)(b)(i).

example by entitling a seller to impose extra charges. The consultation paper tentatively proposes bringing such terms in business to business contracts within the scope of legislative control, and so it is possible that the problem of unilateral expectations will be addressed in a commercial as well as a consumer context.

Although these legal provisons can give expression to unilateral expectations, they do not generally embody the reasonable expectation standard in their formulations. If these provisions are seen in some ways as responding to the deficit or gap in governing norms which results when contracting for complex products takes place without a background of implicit understandings, then there is a case for an explicit focus on unilateral expectations as a resource for filling the gap.[90]

Conclusion

Taking it as established that implicit understandings play an important role in the formulation and application of contract law, I have explored how the incidence and nature of those understandings may vary across different kinds of contracting contexts. By constructing two models of contracting relations—the contracting community model, and the personal consumption model—I have attempted to identify features which favour the development of such understandings, and also features which are less hospitable to them. This analysis suggests that the implicit understandings which the law reflects most readily tend to be those reached between contractors dealing within a contractual community, and that these understandings are typically customary understandings.

Where the context is less hospitable to such understandings, this does not mean that there are no issues of the kind that, in other contexts, are dealt with by implicit understandings. Where the elements of the personal consumption model are present—complex products with

[90] This can be seen as the effect of applying the good faith standard in the US in situations where contracting communities are absent. For argument to this effect in the context of contracts between nursing homes and their residents see Maureen Armour, 'A Nursing Home's Good Faith Duty "To" Care: Redefining a Fragile Relationship Using the Law of Contract' (1994) 39 *St Louis University Law Journal* 217; and in contracts between students and universities see Timothy Davis, 'An Absence of Good Faith: Defining a University's Educational Obligation to Student-Athletes' (1991 28 *Houston Law Rev* 743.

experience or credence characteristics, bought infrequently—there can be a gap or deficit in the operation of the law: when performance issues arise, the legal doctrines normally applied do not have the raw material in implicit understandings that, in the contracting community model, provide the basis of the law's response.

However, the absence of these customary understandings does not mean that there are no implicit understandings at all. In contracts displaying features of the personal consumption model, there may often be understandings which are not shared and which thus give rise to unilateral expectations. I argue that, where there is no contracting community to foster shared understandings, these unilateral expectations may deserve to shape an obligation to fill the gap, in part because it is precisely in situations covered by the personal consumption model that the supplier provides the informational context and so significantly shapes the expectations which the purchaser brings to the transaction. And, where credence goods such as financial products are in issue, the massive assymetry of information, coupled with the supplier's pursuit of their own interest, suggests that the supplier should be expected to act in an almost semi-fiduciary capacity. Many detailed reforms, as well as sector-wide standards of self regulation (such as the Banking Code) can be seen as responding to unilateral expectations in contexts where there is no contracting community to generate and disseminate the background assumptions which confer meaning on most commercial contracting.

A further reason for granting weight to unilateral expectations in legal determination stems from the different view of the social processes of contracting which is revealed by an emphasis on implicit understandings. Once the formal act of signature to a written contract is placed in the context of the shared understandings of parties in a contracting community, it can be argued that it is on these understandings, in which the express terms are nested, that the contractual relationship substantially stands. The law's traditional emphasis on the usual outward manifestation of agreement—written terms—can carry the assumption that the act of consent is to be found in an isolated act of 'agreeing' the terms at the moment of formation. Certainly, it is when seen in this way that the argument for the literal enforcement of terms seems most persuasive. But an emphasis on the layers of implicit understandings makes clear that the ways in which contractors come to understand what complex transactions in contracting communities mean is by participating in these transactions and acquiring the implicit

understandings. In purely cognitive terms, implicit understandings are arguably a necessary part in many contexts of making sense of the contracting process, and hence of consenting to one's participation in it.

Where a context of this kind exists, the law should—and generally does—reflect the social meanings context confers on the contracting process. But where there is no such context, and so no shared customary understandings, the contracting process will still often be given meaning by unilateral assumptions the parties make. These meanings are still part of the social processes of contracting, and the law should not ignore them on the basis that they do not appear in the form typical of commercial contracts.