

# LIABILITY FOR PRE-CONTRACTUAL MISSTATEMENTS

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## I. Introduction

Until the House of Lords decision in *Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd.*<sup>1</sup> in 1963, the lack of any general remedy for negligent misstatements causing purely financial loss meant that a party, induced to enter into a contract by another's misrepresentations, was inadequately protected. A claim for damages suffered was liable to be met by those twin pillars of classical law, namely *Derry v. Peek*<sup>2</sup> and *Heilbut, Symons & Co. v. Buckleton*.<sup>3</sup> The first case decided expressly that simple negligence was insufficient to constitute the tort of deceit as there had to be actual dishonesty on the part of the defendant<sup>4</sup> and impliedly that there was no liability at all for merely negligent misstatements.<sup>5</sup> Thus, Lord Bramwell said that: "To found an action for damages there must be a contract and breach, or fraud."<sup>6</sup> The second case limited relief in contract by demanding that an intention, on the part of the representor, that a statement should constitute a contractual term be proved strictly, especially where there was a written contract between the parties.<sup>7</sup> Lord Moulton said that it was of the utmost importance for the House of Lords to "maintain in its full integrity the principle that a person is not liable in damages for an innocent misrepresentation, no matter in what way or under what form the attack is made."<sup>8</sup> Whilst equity alleviated the representee's position through the remedy of rescission, no damages could be claimed in equity and rescission itself could be barred for a number of different reasons.<sup>9</sup>

This paper examines the remedies available to a party who has been induced to enter into a disadvantageous contract through another's misrepresentations. It deals first with contractual remedies and shows that contractual liability is so hidebound by restrictions that it fails to meet the needs of the representee in these circumstances. Moreover, it demonstrates that a contractual remedy may often be an inappropriate way of resolving the problem. Contractual damages may sit uneasily where the basis of the plaintiff's claim is that he, by entering into the contract, has relied upon the defendant's misrepresentations to his detriment rather than that the

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1. [1964] A.C. 465 (H.L.).

2. (1889), 14 App. Cas. 337 (H.L.).

3. [1913] A.C. 30 (H.L.).

4. *Supra* n. 2, at 374 (*per* Lord Herschell).

5. This was certainly the interpretation favoured by the Court of Appeal just four years later in *Le Lievre v. Gould*, [1893] 1 Q.B. 491 where Lord Esher M.R. said at page 498:

But negligence, however great, does not of itself constitute fraud. The official referee . . . came to the conclusion that the defendant, though he had acted negligently, had not wilfully made any false statement, or been guilty of any fraud. All that he had done was to give untrue certificates negligently. Such negligence, in the absence of contract with the plaintiffs, can give no right of action at law or in equity.

6. *Supra* n. 2, at 347.

7. See generally: Greig, "Misrepresentations and Sales of Goods" (1971), 87 L.Q. Rev. 179.

8. *Supra* n. 3, at 51.

9. The remedy of rescission is discussed briefly in section II.B. of this paper, *infra*.

defendant has guaranteed the truth of his representations.<sup>10</sup> Rescission, on the other hand, even where available, may often be seen as too draconian in that it requires the whole transaction to be upset.<sup>11</sup>

This paper then proceeds to examine tortious liability for precontractual misstatements. It concentrates on the tort of negligent misstatement, tracing its development as a remedy for pre-contractual misrepresentations. It discusses the obstacles which still remain to the employment of this cause of action. Taking the view that in many cases this new tort provides the most satisfactory way of protecting the representee, it raises the hope that such obstacles can be overcome.

## II. Contractual Liability

In contract, a representee may claim that a certain statement constitutes a contractual term for breach of which damages can be recovered, or may seek to rescind the contract in equity on the ground of misrepresentation. Each of these courses of action is discussed in turn.

### A. Damages for Breach of Contract

#### 1. Parol Evidence Rule

Where a contract has been recorded in writing, a plaintiff, in order to recover damages for breach of contract, will be forced to contend with the parol evidence rule.<sup>12</sup> The classic formulation of that rule was given by Lord Denman C.J. in *Goss v. Lord Nugent*:

By the general rules of the common law, if there be a contract which has been reduced into writing, verbal evidence is not allowed to be given of what passed between the parties, either before the instrument was made, or during the time that it was in a state of preparation, so as to add to or subtract from, or in any manner to vary or qualify the written contract:<sup>13</sup>

Where the rule is applied, a plaintiff will be unable to argue successfully that the defendant's pre-contractual representations constituted terms of the contract between the parties. He will be denied a contractual claim for damages. A plaintiff's position, therefore, may depend upon how strictly a particular court applies the rule.

The English courts have been prepared to treat the rule as more in the nature of a common sense presumption that a document which looks like a contract is to be regarded as embodying the entire contract between the parties.<sup>14</sup> A plaintiff, however, has two avenues open to him to rebut such a presumption. First, he may be able to convince a court that certain oral representations constitute a contract collateral to the written contract. Secondly, he may be able to establish that there is a single contract between the parties which is partly written and partly oral. The fact that there is

10. See generally: Taylor, "Expectation, Reliance and Misrepresentation" (1982), 45 Mod. L. Rev. 139; Reiter, "Contracts, Torts, Relations and Reliance" in *Studies in Contract Law* (Reiter and Swan ed. 1980) 253-255.

11. Reiter, *ibid.*

12. See generally: Treitel, *The Law of Contract* (5th ed. 1979) 135-143; McLauchlan, *The Parol Evidence Rule* (1976).

13. (1833), 5 B. & Ad. 58 at 64-65, 110 E.R. 713 at 716 (K.B.).

14. Wedderburn, "Collateral Contracts", [1959] Camb. L.J. 58 at 61-64; McLauchlan, *supra* n. 12 at 50-52.

writing, therefore, merely becomes an important factor in the determination of whether the oral representations were made and, if so, whether the parties intended them to be contractual terms. Lord Moulton, in *Heilbut Symons & Co. v. Buckleton*,<sup>15</sup> warned of the dangers of "lessening the authority of written contracts by making it possible to vary them by suggesting the existence of verbal collateral agreements relating to the same subject-matter."<sup>16</sup>

The influence of the parol evidence rule accounts, in large measure, for the growth of the collateral contract.<sup>17</sup> This concept made its first appearance in the latter half of the nineteenth century. It was used to enforce prior positive oral undertakings made by one party to induce another to enter into a written contract. In some cases, the undertakings related to a matter unconnected with the written contract, as in *Lindley v. Lacey*,<sup>18</sup> where the plaintiff refused to execute a contract for the sale of his business to the defendant until the prospective purchaser undertook to settle an action being brought against the plaintiff by a third party. In other cases, the undertakings were connected with the subject-matter of the written contract; the typical example being where a landlord induced a tenant to execute a lease by promising to do certain repairs<sup>19</sup> or to keep down game<sup>20</sup> or to carry out some similar matter. In both sets of cases, a court was able to find two contracts, the main written contract and an independent oral agreement, the consideration for which was the execution of the principal contract. The purity of the parol evidence rule, therefore, remained unscathed since one contract was wholly written and the other wholly oral.

There seems to have been two common elements, one negative and the other positive, to the finding of a collateral contract in the nineteenth century cases. First, such contracts did not include statements about the present state of the subject-matter of the main contract rather than undertakings to perform certain matters in the future.<sup>21</sup> Secondly, such contracts were most readily inferred where one party refused to enter into the written contract unless he received the oral assurances in question.<sup>22</sup> The scope of such contracts was not broadened until the important judgment of Lord Moulton in *Heilbut Symons & Co. v. Buckleton*<sup>23</sup> where he gave the following definition of the collateral contract:

It is evident, both on principle and on authority, that there may be a contract the consideration for which is the making of some other contract. 'If you will make such and such a contract I will give you one hundred pounds,' is in every sense of the word a complete legal contract. It is collateral to the main contract, but each has an independent existence, and

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15. *Supra* n. 3.

16. *Ibid.*, at 47.

17. See, Wedderburn, *supra* n. 14; McLauchlan, *supra* n. 12, at 88-97; McLauchlan, "The Inconsistent Collateral Contract" (1976), 3 Dal. L.J. 136.

18. (1864), 17 C.B. (N.S.) 578, 144 E.R. 232 (C.P.).

19. For example, *Mann v. Nunn* (1874), 30 L.T. 526 (C.P.).

20. For example, *Morgan v. Griffith* (1871), L.R. 6 Ex. 70 (Exch. Ch.); *Erskine v. Adeane* (1873), L.R. 8 Ch. App. 756.

21. See Greig, *supra* n. 7, at 184-185.

22. See McLauchlan, *supra* n. 12, at 95-96.

23. *Supra* n. 3.

they do not differ in respect of their possessing to the full the character and status of a contract.<sup>24</sup>

One effect of this judgment was to open up the possibility of establishing a collateral contract in respect of any kind of precontractual oral statements. Simple representations about the subject-matter of a written contract, for example, could be and were classified as collateral contracts.<sup>25</sup> Another effect of the judgment, however, was to obscure the distinction between collateral contracts and warranties through its definition of a warranty as "a contract collateral to the main contract".<sup>26</sup> A warranty is not in itself a separate contract but is one of the terms of a single contract. It is a collateral term in the sense that it is "collateral to the express object of"<sup>27</sup> the contract of which it forms a part but it is not automatically a collateral contract.<sup>28</sup> The equation of a warranty with a collateral contract seems to have been the result of Lord Moulton's belief in the strict nature of the parol evidence rule and his distrust of oral evidence generally. Combined with his emphasis upon the need to establish clearly an intention to warrant, which is discussed below,<sup>29</sup> he saw the collateral contract as a limiting device to be used very sparingly to amend the parties' written agreement:

But such collateral contracts must from their very nature be rare . . . Such collateral contracts, the sole effect of which is to vary or add to the terms of the principal contract, are . . . viewed with suspicion by the law. They must be proved strictly. Not only the terms of such contracts but the existence of an *animus contrahendi* on the part of all the parties to them must be clearly shewn. Any laxity on these points would enable parties to escape from the full performance of the obligations of contracts unquestionably entered into by them and more especially would have the effect of lessening the authority of written contracts . . .<sup>30</sup>

He would have been surprised by the alacrity with which the device was seized to grant relief in respect of pre-contractual oral representations.<sup>31</sup> By using the device of the collateral contract in these circumstances, later courts were able to convince themselves that the parol evidence rule was being upheld.<sup>32</sup>

Arguably, there is still a serious limitation upon the use of the collateral contract to evade the parol evidence rule. It has often been asserted that a collateral contract cannot be established if its terms would contradict those of the written contract.<sup>33</sup> There are signs that this limitation is being increasingly ignored, at least in England. In *City and Westminster Proper-*

24. *Ibid.*, at 47.

25. For example, *Webster v. Higgin*, [1948] 2 All E.R. 127 (C.A.); *Dick Bentley Productions, Ltd. v. Harold Smith (Motors), Ltd.*, [1965] 2 All E.R. 65 at 68 (*per* Salmon L.J.) (C.A.). See generally: Greig, *supra* n. 7, at 185-189.

26. *Supra* n. 3, at 47.

27. *Chanter v. Hopkins* (1838), 4 M. & W. 399 at 404, 150 E.R. 1484 at 1486 (*per* Lord Abinger C.B.) (Exch. D.).

28. On the distinction between collateral contracts and warranties, see Wedderburn, *supra* n. 14 at 64-67 and McLauchlan, *supra* n. 12 at 90-94.

29. Section II.A.2. of this paper.

30. *Supra* n. 3, at 47.

31. See *Esso Petroleum Co. Ltd. v. Mardon*, [1976] Q.B. 801 at 817. (*per* Lord Denning M.R.).

32. This point was made succinctly by Wedderburn, *supra* n. 14, at 69, where he wrote:

. . . [I]t is clear that a division of a transaction into (i) main written contract and (ii) collateral oral contract eases the conscience of those who believe that the parol evidence rule is a strict and meaningful prohibition. After all, the written contract is not varied, added to, or contradicted. It stays intact — quite a different answer from that which a 'one-contract' analysis demands.

33. For example, *Erskine v. Adeane*, *supra* n. 20, at 766 (*per* Mellish L.J.). See generally: McLauchlan, *supra* n. 17.

*ties (1934) Ltd. v. Mudd*,<sup>34</sup> for example, a tenant was induced to sign a lease, containing a covenant that the premises would be used for business purposes only, by the landlord's oral assurance that it would not object to the tenant sleeping on the premises as he had done in the past. Harman J. held that "there was a clear contract acted upon by the [tenant] to his detriment and from which the [landlord] cannot be allowed to resile."<sup>35</sup> Unfortunately, there was no consideration in this case of the leading authorities on collateral contracts and so its stature is in some doubt. Ideally, the fact of contradiction should just be another factor in the determination of whether an alleged collateral agreement was in fact made. Clearly it will be easier for a party to establish the existence of a collateral contract which merely adds terms to the written contract. In the case of a direct contradiction with a later written contract, a defendant always has the strong argument that the parties had agreed to set aside any prior oral assurances as exemplified by their execution of a written contract inconsistent with such assurances.

Professor McLauchlan has convincingly shown that there is no need to rely upon what may often be the fiction of a collateral contract in order to obviate the parol evidence rule.<sup>36</sup> He points out that "there is a written contract for the purpose of the application of the rule only when the writing is intended by the parties as a contractual document which is to contain all the terms of their agreement."<sup>37</sup> The parol evidence rule creates a presumption that a document containing contractual terms embodies the complete contract between the parties. As has been pointed out earlier, the fact that the alleged oral representations were omitted from the writing is directly relevant to the issues of whether the oral statements were in fact made and, if so, of whether they were intended to have contractual effect. A court, however, should always listen to the argument of one party that the document in question was not intended to contain the whole contract and that the contractual terms are partly written and partly oral.

Professor McLauchlan has isolated the factors which will assist a court in its determination of whether the writing should be regarded as the entire contract.<sup>38</sup> Such factors include, (1) the nature of the writing<sup>39</sup> — the more formal and detailed the writing, the less likely the courts will be to allow it to be amended by oral evidence; (2) whether the document has been signed<sup>40</sup> — where a document has been signed by both parties, it is more likely to be regarded as the complete contract between the parties; (3) the status of the parties<sup>41</sup> — businessmen, for example, are much more likely than others to want to record their contracts entirely in writing; (4) the preparation of the document<sup>42</sup> — where both parties have participated in drafting the

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34. [1959] Ch. 129.

35. *Ibid.*, at 145-146.

36. McLauchlan, *supra* n. 12.

37. *Ibid.*, at 143.

38. *Ibid.*, at 58-79.

39. *Ibid.*, at 59-63.

40. *Ibid.*, at 63-64.

41. *Ibid.*, at 64-65.

42. *Ibid.*, at 65.

document, the presumption of completeness will be more likely to operate; (5) whether the writing is in a standard form<sup>43</sup> — by its very nature a standard form contract has not been drawn up to record the specific transaction in question and hence there is more scope for an oral variation of the standard terms in a particular case; and (6) whether the writing specifically provides that it is to constitute the entire contract between the parties.<sup>44</sup>

Recently, the English courts have shown a willingness to view the parol evidence rule in the light suggested by Professor McLauchlan and to determine that a contract is partly written and partly oral. One such case is the Court of Appeal decision in *Mendelssohn v. Normand Ltd.*<sup>45</sup> In that case, the plaintiff drove his car into the defendant's garage. There was a suitcase on the back seat containing jewellery. The plaintiff placed the bag under a rug and was about to lock up the car when he was told by an attendant that he was not allowed to do so. The plaintiff explained to the attendant that the suitcase was rather valuable but he gave him the keys to the car and told him to lock it up as soon as he had moved it. The attendant agreed to do so and gave the plaintiff a ticket. On his return, the plaintiff found the car unlocked and the keys in the ignition. The rug appeared to be in the same position on the back seat. He drove off. Later that evening he discovered that the suitcase was missing. The plaintiff sued the defendant garage company for the loss of the suitcase. The trial judge found that the suitcase had been stolen from the car, whilst unlocked, by one of the attendants. The question in the Court of Appeal was whether the defendant could rely upon the printed terms contained on the back of the ticket and, in particular, upon a clause which purported to protect the defendant from liability "for any loss or damage sustained by the vehicle its accessories or contents however caused". The Court held that the defendant, through the attendant, had expressly promised to lock up the car, which was translated into a promise to ensure that the contents were safe. Such an oral assurance took priority over the printed terms for the following reason:

... [T]he oral promise or representation has a decisive influence on the transaction — it is the very thing which induces the other to contract — and it would be most unjust to allow the maker to go back on it. The printed condition is rejected because it is repugnant to the express oral promise or representation.<sup>46</sup>

The Court, therefore, had no difficulty in concluding that the whole contract was not to be found in the small print on the back of the ticket. There was room for effect to be given to oral assurances made at the time of contracting. All of the factors identified by Professor McLauchlan above favoured denying giving conclusive effect to the writing in this case. There was no formal and detailed contract which had been prepared and signed by both parties. Rather, there was a standard form set of conditions which had been drafted by the defendant purely for its own benefit.

43. *Ibid.*, at 66-67.

44. *Ibid.*, at 73-79.

45. [1970] 1 Q.B. 177.

46. *Ibid.*, at 184 (*per* Lord Denning M.R.).

The other interesting aspect of *Mendelssohn* is that the oral assurance was allowed to override one of the printed conditions. Obviously, it will be easier for a court to give effect to oral terms which are merely in addition to the written part of the contract, but there is no requirement that the oral and written portions must be consistent with each other. The fact of contradiction is just one of the factors in the determination of whether a particular assurance was given and, if so, whether it was intended to have contractual effect and to have survived the inconsistent writing. The particular term contradicted will also be relevant. A court will be especially ready, for example, to hold that a widely-drawn exemption clause must be read subject to some oral undertaking given at the time of contracting.

*Mendelssohn* helps to put into perspective some earlier decisions, such as *Couchman v. Hill*.<sup>47</sup> In that case, the plaintiff purchased, at an auction sale, the defendant's heifer which had been described in the sale catalogue as "unserved". That document also stated that the sale would be subject to the auctioneer's usual conditions and that all lots had to be taken "subject to all faults or errors of description". The auctioneer's usual conditions provided that the lots were sold "with all faults, imperfections and errors of description". At the time of the sale, the plaintiff had asked both the auctioneer and the defendant whether they could confirm that the heifer was unserved and they had each assured him that it was. Later, the heifer was found to be in calf and died as a result of carrying a calf at too young an age. The plaintiff sued the defendant for breach of warranty. The Court of Appeal held that the oral assurances given at the time of the auction took precedence over the printed exclusion clauses. Scott L.J. said:

... [T]here was clearly an oral offer of a warranty which overrode the stultifying condition in the printed terms: that offer was accepted by the plaintiff when he bid, and the contract was made on that basis when the lot was knocked down to him.<sup>48</sup>

The clearest statement delimiting the application of the parol evidence rule, and one entirely in accordance with McLauchlan's analysis, is contained in *J. Evans & Son (Portsmouth) Ltd. v. Andrea Merzario Ltd.*<sup>49</sup> The plaintiff was an importer of machines from Italy. Since 1959, it had contracted with the defendant, which was a forwarding agent, to arrange for the carriage of goods to England. The contract between the parties was on the basis of the printed standard conditions of the forwarding trade. Prior to 1967, the defendant had arranged for the goods to be carried in crates below deck because of the possibility of corrosion if carried on deck. In 1967, the defendant proposed to arrange for the carriage of goods in the future by containers. The plaintiff agreed to such a changeover after being assured by the defendant that its goods would continue to be shipped below deck. Nothing was put into writing concerning the assurance and the parties continued to operate on the basis of the standard conditions. About a year later, a container was carried on deck and a machine belonging to the plaintiff was lost overboard. The plaintiff claimed damages for breach of

47. [1947] K.B. 554 (C.A.). See also, *Harling v. Eddy*, [1951] 2 K.B. 739 (C.A.).

48. *Ibid.*, at 558.

49. [1976] 2 All E.R. 930 (C.A.).

the oral assurance. The defendant argued that it had given no contractual promise that the plaintiff's goods would be carried below deck and relied upon the printed conditions. These conditions gave the defendant complete freedom to choose the means to be followed in the transportation of goods, restricted its liability to cases of wilful neglect or default, and limited its liability to fifty pounds per ton.

The Court of Appeal unanimously held in favour of the plaintiff. Roskill L.J. dealt directly with the problem of the parol evidence rule and rejected the defendant's contention that that rule precluded the admission of evidence concerning the oral assurance:

But that doctrine [the parol evidence rule], . . . has little or no application where one is not concerned with a contract in writing (with respect, I cannot accept counsel for the defendants' argument that there was here a contract in writing) but with a contract which, as I think, was partly oral, partly in writing and partly by conduct. In such a case the court does not require to have recourse to lawyers' devices such as collateral oral warranty in order to seek to adduce evidence which would not otherwise be admissible. The court is entitled to look at and should look at all the evidence from start to finish in order to see what the bargain was that was struck between the parties.<sup>50</sup>

The only issue, therefore, was of delineating the terms of the contract reached between the parties and in determining that issue all evidence was relevant. Roskill L.J. decided that there was every reason to treat the oral assurance as an enforceable contractual promise and not to rely solely upon the printed terms because of the evidence to the effect that the plaintiff was willing to accept the changeover to container transportation only if the defendant promised that such containers would be carried below deck. There was no need to find a collateral contract in order to do justice between the parties. It was possible to find a single contract, composed of both oral and written terms. Roskill L.J. was, however, faced with the contradiction between the oral promise and the printed terms. This was a question of construction which he resolved in favour of the oral assurance because otherwise the defendant's promise would have been "wholly illusory".<sup>51</sup>

In a brief judgment, Geoffrey Lane L.J. took the same approach as Roskill L.J. whilst Lord Denning M.R. used the device of the collateral contract to reach the same conclusion as his brethren. Whichever approach is adopted in the future, the case shows that the English courts will not be precluded by the parol evidence rule from granting relief in appropriate cases for breach of oral promises.

In Canada, the lower courts have followed much the same path as their English counterparts. The collateral contract has been seized upon with alacrity as a means of obviating the rigours of the parol evidence rule. There has even been some acceptance of the notion that such a contract, in an appropriate case, can contradict the terms of a written contract. In *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*,<sup>52</sup> for example, Rutherford J. said at trial:

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50. *Ibid.*, at 934-935.

51. *Ibid.*, at 935.

52. (1978), 85 D.L.R. (3d) 321 (Ont. H.C.); rev'd (1979), 105 D.L.R. (3d) 684 (C.A.); rev'd (1982), 135 D.L.R. (3d) 1 (S.C.C.).



Certainly, I have no doubt that in certain cases, evidence of oral collateral contracts existing apart from a subsequent written agreement may be given effect to even where they are repugnant to the terms of the subsequent agreement.<sup>53</sup>

Occasionally, a Canadian court has overcome the parol evidence rule more directly by finding the contract in question to be partly oral and partly written. Recently, for example, in *Sperry Rand Canada Ltd. v. Thomas Equipment Ltd.*,<sup>54</sup> the New Brunswick Court of Appeal rejected the need to rely upon the device of the collateral contract and was prepared to adopt the reasoning of Roskill L.J. in *Evans v. Merzario*.<sup>55</sup> Stratton J.A. concluded that "oral representations and assurances . . . may be incorporated into an otherwise written contract and that it is necessary to examine the whole of the evidence in the particular case to determine what the bargain was that was struck between the parties."<sup>56</sup> Consistent with *Evans*, the Court also held that such an oral assurance could, and in that case did, take priority over the written terms.

Often the written term contradicted is a widely-drawn exclusion clause and there have been a number of cases where the Canadian courts have held that an exemption clause must be read subject to some oral assurance.<sup>57</sup> Of course, it will not always be appropriate to give an overriding effect to an oral assurance and there are many cases where a written exemption clause has governed the decision. In *Lister*<sup>58</sup> itself, Rutherford J. determined that the plaintiffs should be bound by the written agreement which they had signed which contained a provision to the effect that the written contract constituted the entire contract between the parties. They were experienced business people; they had signed with no undue pressure from the defendant; they understood what they were doing; and, indeed, they had been advised by their solicitor that they were "taking an awful chance" in signing the written agreement. It should be stressed that it was not a strict interpretation of the parol evidence rule which led Rutherford J. to give effect to the exclusion clause. He decided simply that, on the facts, the plaintiffs must be taken to have limited their rights to the written agreement.

Unfortunately, there is in Canada an uneasy tension between the decisions of the lower courts and the pronouncements of the Supreme Court on the effect of the parol evidence rule. In recent years, there has been a trio of Supreme Court cases which have taken a very rigid view of the admissibility of parol evidence and which have ignored developments in both England and the lower Canadian courts. The first case in the line is *Hawrish v. Bank of Montreal*.<sup>59</sup> The bank sued the defendant on a guarantee which he had signed for the indebtedness of a newly formed company. The guarantee was on the bank's usual form and provided that it was to be a continuing

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53. *Ibid.*, at 331-332.

54. (1982), 135 D.L.R. (3d) 197.

55. *Supra* n. 49.

56. *Supra* n. 54, at 214.

57. For example, *Sodd Corporation Inc. v. Tessis* (1977), 79 D.L.R. (3d) 632 (Ont. C.A.); *Roberts v. Montex Development Corporation* (1979), 100 D.L.R. (3d) 660 (B.C.S.C.); *Sperry Rand Canada Ltd. v. Thomas Equipment Ltd.*, *supra* n. 54.

58. *Supra* n.52.

59. (1969), 2 D.L.R. (3d) 600 (S.C.C.).

guarantee and to cover existing as well as future indebtedness of the company up to the sum of six thousand dollars. It also stated that the guarantor could determine his further liability under the guarantee only by notice in writing to the bank and contained a clause to the effect that the guarantor acknowledged that no representations had been made to him on behalf of the bank. The defence was that, when he signed the guarantee, the defendant had received an oral assurance from the plaintiff's assistant branch manager that the guarantee would cover only existing debts of the company and that he would be released from his guarantee when the bank had obtained a joint guarantee from the directors of the company. Such a joint guarantee was acquired some six months after the defendant had executed his guarantee.

The Supreme Court decided in favour of the bank. Such a decision was understandable. There was little reason to feel sympathetic towards the defendant, a solicitor, who had failed even to read the guarantee before signing it. If the Court had concluded simply that the alleged oral assurance had not been made or that its exclusion from the contradictory written guarantee indicated that it was not intended to have contractual effect,<sup>60</sup> the decision would have been quite unexceptional. Unfortunately, the defence was rejected on purely technical grounds. The Court recognized that parol evidence was admissible to establish an independent collateral contract but held, relying on nineteenth century English<sup>61</sup> and Canadian<sup>62</sup> authority, that such a collateral agreement could not be established where it would contradict the main contract. Here the contradictions were numerous.

For more than ten years, *Hawrish* seems to have been regarded as an aberration because it was ignored consistently. In particular, oral assurances were allowed to override written exemption clauses.<sup>63</sup> In 1980, however, the Supreme Court affirmed the position it had taken in *Hawrish* in *Bauer v. Bank of Montreal*.<sup>64</sup> The defendant guarantor guaranteed his company's debts to the plaintiff bank which also took an assignment of the company's book debts. The written guarantee provided that the bank, without releasing the guarantor, could "abstain from taking securities from, or from perfecting securities of," the company. The bank neglected to register the assignment of book debts with the result that the security was lost to other creditors. The bank brought an action to enforce the guarantee and the defendant relied *inter alia* on an oral understanding that the accounts would be preserved for the benefit of the guarantor and would be assigned to him on payment of the company's debts. The Court, following *Hawrish*, held that evidence of such an understanding was inadmissible under the parol evi-

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60. The Court did doubt whether there was any such intention but did not ground its decision on such a conclusion, *ibid.*, at 605.

61. *Lindley v. Lacey*, *supra* n. 18; *Morgan v. Griffith*, *supra* n. 20; *Erskine v. Adeane*, *supra* n. 20.

62. *Byers v. McMillan* (1887), 15 S.C.R. 194.

63. For example, *Francis v. Trans-Canada Trailer Sales Ltd.* (1969), 6 D.L.R. (3d) 705 (Sask. C.A.); *Sodd Corporation Inc. v. Tessis*, *supra* n. 57; *Westridge Developments Ltd. v. Can-Am Development Corp. Ltd.*, [1978] 5 W.W.R. 404 (Alta. S.C.); *Roberts v. Montex Development Corp.*, *supra* n. 57; *dicta* by the Trial Judge in *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*, *supra* n. 52.

64. (1980), 110 D.L.R. (3d) 424.

dence rule because it “would clearly contradict the terms of the guarantee which . . . gave the bank the right to abstain from registration and perfection of security.”<sup>65</sup>

The Supreme Court reiterated its views just two years later in *Carman Construction Ltd. v. Canadian Pacific Ry. Co.*<sup>66</sup> The plaintiff contractor entered into a contract with the defendant for the excavation and removal by the plaintiff of a section of rock. In submitting its bid, the plaintiff had relied upon an oral representation by one of the defendant’s employees as to the quantity of rock to be removed. It transpired that there was a great deal more rock to be removed than had been represented with the result that the plaintiff incurred substantial additional expense. The plaintiff brought an action, *inter alia*, for breach of a collateral warranty as to the quantity of rock to be removed. The defendant relied upon the terms of the written contract and, in particular, on clause 3.1 which provided:

It is hereby declared and agreed by the Contractor that this Agreement has been entered into by him on his own knowledge respecting the nature and conformation of the ground upon which the work is to be done, the location, character, quality and quantities of the material to be removed, the character of the equipment and facilities needed, the general and local conditions and all other matters which can in any way affect the work under this Agreement, and the Contractor does not rely upon any information given or statement made to him in relation to the work by the Company.

Both at trial and on appeal the Ontario courts dismissed the plaintiff’s claim, with no consideration of the parol evidence rule, on the basis that it was bound by that clause. The Supreme Court, however, after deciding that no collateral contract existed because there was no intention to warrant the accuracy of the estimate and because of the exclusion clause, could not resist invoking the parol evidence rule in the defendant’s favour. Martland J., for the Court, said:

There is an additional ground for denying the existence of a collateral warranty. Such a warranty, if it existed, would contradict the express terms of the contract as contained in cl. 3.1. This court has held in *Hawrish v. Bank of Montreal*<sup>67</sup> . . . that a collateral agreement cannot be established where it is inconsistent with or contradicts the written agreement.<sup>68</sup>

The Court also cast doubt on the possibility of finding a contract to be partly written and partly oral. Following *Heilbut, Symons & Co. v. Buckleton*,<sup>69</sup> a collateral warranty was equated with “a contract collateral to the primary agreement.”<sup>70</sup>

This line of Supreme Court authority makes the parol evidence rule a much more formidable barrier to be overcome in Canada than in England by a potential plaintiff. If followed slavishly,<sup>71</sup> there is the danger that such an approach will preclude, on technical grounds, a full examination of all

65. *Ibid.*, at 431-432.

66. (1982), 136 D.L.R. (3d) 193 (S.C.C.); aff’g (1981), 124 D.L.R. (3d) 680 (Ont. C.A.); aff’g (1980), 109 D.L.R. (3d) 288 (Ont. H.C.).

67. *Supra* n. 59.

68. *Supra* n. 66, at 201.

69. *Supra* n. 3.

70. *Supra* n. 66, at 198.

71. It was followed recently in *Bank of Nova Scotia v. Zackheim* (1983), 149 D.L.R. (3d) 555 (Ont. H.C.).

the evidence to determine what the parties have agreed. Moreover, such an approach restricts seriously the availability of contractual liability for pre-contractual misstatements and emphasizes the need for some form of tortious liability in this area.

## 2. Contractual Intention

If a plaintiff can overcome the hurdles posed by the parol evidence rule, he will not necessarily succeed in an action for breach of contract. All pre-contractual representations made by the defendant will not automatically be classified as contractual terms, whether of a single contract or of some collateral contract. The accepted position is that a representation constitutes a term only if such was the intention of the parties. The requirement of a contractual intention was emphasized by the House of Lords in *Heilbut, Symons & Co. v. Buckleton*.<sup>72</sup> The defendants had underwritten a large number of shares in a new company and they instructed their Liverpool manager to ask some of his Liverpool friends to take shares in the company. The plaintiff heard about the availability of the shares and telephoned the manager for further information. The plaintiff said that he understood that the defendants were bringing out a rubber company and the manager replied that they were. Following the conversation, the plaintiff bought shares in the company. When the shares later declined in value, the plaintiff sought damages for breach of warranty on the basis that the company was not technically a rubber company. The House of Lords, relying heavily on a *dictum* ascribed to Holt C.J. that: "An affirmation at the time of the sale is a warranty, provided it appear on the evidence to be so intended",<sup>73</sup> held that there was no "evidence of an intention on the part of either or both of the parties that there should be a contractual liability in respect of the accuracy of the statement."<sup>74</sup> The statement was merely an innocent representation for which no damages could be recovered.

The same decision could have been reached easily without the need to stress the lack of a contractual intention because it was clear that the plaintiff had never relied upon any representation as to the company being a rubber company. The plaintiff's decision to purchase the shares had been influenced rather by the defendants' general reputation. By emphasizing the requirement of a contractual intention, however, *Heilbut, Symons* marks the clear separation of warranty from its tortious roots and its incorporation into contractual theory. Originally, an action on a warranty was a form of action in deceit.<sup>75</sup> A buyer, for example, who bought goods in reliance on the seller's misrepresentations, would succeed if he could establish that the seller had "warranted" the truth of his statements. The action was based not on any promise by the defendant but on the fact that the plaintiff had been misled into acting to his detriment. By making the warranty, the

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72. *Supra* n. 3.

73. *Ibid.*, at 49. See also *Pasley v. Freeman* (1789), 3 T.R. 51 at 57, 100 E.R. 450 at 453 (*per* Buller J.) (K.B.) and the discussion by Greig, *supra* n. 7, at 181-183.

74. *Ibid.*, at 51.

75. See Stevens, "Hedley Byrne v. Heller: Judicial Creativity and Doctrinal Possibility" (1964), 27 Mod. L. Rev. 121 at 161-166; Greig, *supra* n. 7, at 179-184; Waddams, *Products Liability* (2d ed. 1980) 1-11.

defendant had assumed responsibility for the truth of his statements. Initially, the defendant must have said expressly "I warrant" in order to incur liability but later it was sufficient that the defendant had made a statement of fact. As recently as 1901, the English Court of Appeal in *De Lasalle v. Guildford*<sup>76</sup> had stated that "a decisive test" for determining a warranty:

... [I]s whether the vendor assumes to assert a fact of which the buyer is ignorant, or merely states an opinion or judgment upon a matter of which the vendor has no special knowledge, and on which the buyer may be expected also to have an opinion and to exercise his judgment.<sup>77</sup>

Such a test was rejected in *Heilbut Symons*, the only true test being one of contractual intention.

In determining whether a statement was intended to constitute a contractual term, the courts use an objective test. Thus, Denning L.J., as he then was, said in *Oscar Chess, Ltd. v. Williams*:

It is sometimes supposed that the tribunal must look into the minds of the parties to see what they themselves intended. That is a mistake . . . The question whether a warranty was intended depends on the conduct of the parties, on their words and behaviour, rather than on their thoughts. If an intelligent bystander would reasonably infer that a warranty was intended, that will suffice.<sup>78</sup>

In applying the objective test, the courts have isolated a number of factors to assist them in the determination of the parties' intentions. Clearly, the actual words used can be very relevant.<sup>79</sup> Rarely, however, will the maker expressly "warrant" the truth of his statements and so other factors will have to be considered. In the last section, it was seen that if the contract appears to be contained in a document, then the exclusion of oral statements from that document will be strong evidence that they were not intended to form part of the contract. This was clearly an important factor in *Heilbut, Symons*<sup>80</sup> itself where Lord Moulton warned of the danger of "lessening the authority of written contracts by making it possible to vary them by suggesting the existence of verbal collateral agreements relating to the same subject-matter."<sup>81</sup> In *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*,<sup>82</sup> one reason why Rutherford J. at trial refused to regard certain oral assurances as contractual terms was because he felt that they would have been included in the final written agreement if the parties had intended that they be binding. In *Oscar Chess, Ltd. v. Williams*,<sup>83</sup> Denning L.J. said:

If an oral representation is afterwards recorded in writing, it is good evidence that it was intended as a warranty. If it is not put into writing, it is evidence against a warranty being intended.<sup>84</sup>

He agreed, however, that such a factor was not decisive.<sup>85</sup>

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76. [1901] 2 K.B. 215.

77. *Ibid.*, at 221.

78. [1957] 1 All E.R. 325 at 328 (C.A.).

79. *Ibid.*

80. *Supra* n. 3.

81. *Ibid.*, at 47.

82. *Supra* n. 52.

83. *Supra* n. 78.

84. *Ibid.*, at 329.

85. See also *Esso Petroleum Co. Ltd. v. Mardon*, *supra* n. 31, at 824 (*per* Ormrod L.J.) (C.A.).

Another consideration will be the time at which the statement in question was made. The longer the time interval between the making of the statement and the formation of the contract, the less likely is the statement to be regarded as a term of the contract.<sup>86</sup> Again, of course, the length of time elapsed can never be conclusive in any way.<sup>87</sup> Similarly the importance of the topic covered by the statement is relevant. If the plaintiff would not have contracted at all without receiving the assurance in question, then the more likely it is for such an assurance to be regarded as a term.<sup>88</sup>

In practice, the most important consideration has been the skill and knowledge of the respective parties. If the maker of the statement possesses a special skill or knowledge compared with the representee, it will be more reasonable to infer that he was assuming contractual responsibility for its truth. This is especially true where one party asserts as a fact some matter which should be within his own knowledge. In *Oscar Chess Ltd. v. Williams*,<sup>89</sup> for example, the defendant wished to obtain from the plaintiff car dealership a new car on hire-purchase and to offer a secondhand Morris in part exchange. The defendant described the Morris as a 1948 model and produced the registration book to support his claim. The transaction was then concluded. Eight months later, the plaintiff discovered that the car was in fact a 1939 model and sued for breach of contract. A majority of the Court of Appeal held that no warranty should be inferred on those facts. The seller had no personal knowledge of the year of the car but was relying solely on the registration book. In those circumstances, the reasonable inference was that the seller was not intending to assume responsibility for the truth of his statement. Denning L.J. said:

When the seller states a fact which is or should be within his own knowledge and of which the buyer is ignorant, intending that the buyer should act on it and he does so, it is easy to infer a warranty; . . . If, however, the seller, when he states a fact, makes it clear that he has no knowledge of his own but has got his information elsewhere, and is merely passing it on, it is not so easy to imply a warranty.<sup>90</sup>

*Oscar Chess* should be contrasted with *Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd.*,<sup>91</sup> where the defendant car dealer falsely informed the plaintiff, a prospective purchaser, that the car in question had done only 20,000 miles since it had been fitted with a new engine and gearbox. In that case, the Court had no doubt that the defendant's statement constituted a contractual term. The seller was clearly in a better position than the buyer to know or find out whether the representation was true.<sup>92</sup>

In a similar vein, there is the more recent decision of the English Court of Appeal in *Esso Petroleum Co. Ltd. v. Mardon*.<sup>93</sup> Esso negotiated with

86. This was one of the relevant factors in the decision against a warranty in *Howard Marine & Dredging Co. Ltd. v. A. Ogden & Sons (Excavations) Ltd.*, [1978] Q.B. 574 (C.A.).

87. For example, *Ellul v. Oakes* (1972), 3 S.A.S.R. 377 (S.C.).

88. For example, *J. Evans & Son (Portsmouth) Ltd. v. Andrea Merzario Ltd.*, *supra* n. 49 which has been discussed in detail in section II.A.1. of this paper.

89. *Supra* n. 78.

90. *Ibid.*, at 329.

91. *Supra* n. 25.

92. See also *Roberts v. Montex Development Corp.*, *supra* n. 57.

93. *Supra* n. 31.

the defendant for the lease to him of a service station on a newly developed site. During the negotiations, an experienced representative of Esso told the defendant that Esso had estimated that the "throughput" of petrol would reach 200,000 gallons in the third year of operation of the station. This estimate was totally unrealistic. It had been reached two years earlier on the assumption that the service station would front on to a main street. In fact, the local planning authority had insisted upon the station being built "back to front" with the result that it was accessible and could be seen only from side streets. This change falsified Esso's calculations but no revision to the original estimate was ever made. The defendant had doubts about Esso's figures but his misgivings were quelled by the greater experience of the company's representative. He entered a tenancy which proved financially disastrous for him. The annual throughput of petrol scarcely ever exceeded 70,000 gallons. When sued for arrears of rent, the defendant counterclaimed, *inter alia*, for breach of contract. The Court held that Esso had not warranted or guaranteed that the throughput of petrol would be 200,000 gallons per year by the third year of operation. It was reasonable, however, to regard Esso as having warranted that its estimate was sound in the sense that it had been made with reasonable care. Esso was in a position of special knowledge and skill. It had a wealth of experience and expertise at its disposal. It was in a much better position than the defendant to make the forecast and so it was only reasonable to conclude that it had promised that its estimate was reliable.

A consideration of the cases decided since *Heilbut, Symons & Co. v. Buckleton*,<sup>94</sup> suggests that the courts, especially in England, have not been unduly hindered by the requirement of a contractual intention from holding a statement to be a contractual term. The absence for many years of any possibility of tortious relief meant that there was a need to use contract to relieve one party from another's misrepresentations. In many ways, the law has reverted to its nineteenth century position where a misstatement by a party with special knowledge which induced the other party to enter into a contract was likely to be treated as a warranty. In *Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd.*, Lord Denning M.R. said:

... [I]f a representation is made in the course of dealings for a contract for the very purpose of inducing the other party to act on it, and it actually induces him to act on it by entering into the contract, that is prima facie ground for inferring that the representation was intended as a warranty.<sup>95</sup>

In *Esso Petroleum Co. Ltd. v. Mardon*,<sup>96</sup> Lord Denning M.R. reiterated what he had said in *Dick Bentley* and admitted openly that the concept of warranty as expounded in *Heilbut Symons* is often manipulated so as to allow for a remedy in damages to a representee:

Ever since *Heilbut, Symons & Co. v. Buckleton* [1913] A.C. 30, we have had to contend with the law as laid down by the House of Lords that an innocent misrepresentation gives no right to damages. In order to escape from that rule, the pleader used to allege — I often

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94. *Supra* n. 3.

95. *Supra* n. 25, at 67.

96. *Supra* n. 31.

did it myself — that the misrepresentation was fraudulent, or alternatively a collateral warranty. At the trial we nearly always succeeded on collateral warranty . . . Besides that experience, there have been many cases since I have sat in this court where we have readily held a representation — which induces a person to enter into a contract — to be a warranty sounding in damages.<sup>97</sup>

A plaintiff, therefore, can often succeed in an action for breach of contract where the basis of his claim is that he has relied on the defendant's representations to his detriment by entering into a disadvantageous contract rather than that the defendant has guaranteed the truth of his representations.<sup>98</sup> The contractual action is being used to enforce what is fundamentally a tortious claim. In New Zealand, this position has been entrenched by statute. Section 6(1) of the *Contractual Remedies Act 1979*<sup>99</sup> provides:

If a party to a contract has been induced to enter into it by a misrepresentation, whether innocent or fraudulent, made to him by or on behalf of another party to that contract —

- (a) He shall be entitled to damages from that other party in the same manner and to the same extent as if the representation were a term of the contract that has been broken; and
- (b) He shall not, in the case of a fraudulent misrepresentation, or of an innocent misrepresentation made negligently, be entitled to damages from that other party for deceit or negligence in respect of that misrepresentation.

It is understandable to treat representations inducing a contract as contractual terms in order to provide a measure of relief to a representee. As discussed below, however, relief in tort is now available in the majority of these cases<sup>100</sup> and so no longer need the law of contract be strained, whether at common law or by statute, so as to protect a representee. Contractual damages may be inappropriate in such a case. The normal contractual measure of damages is the expectation interest. The plaintiff is entitled to be put into the position in which he would have been if the contract had been performed, namely the representations had been true. He is to be granted the benefit of his bargain. In tort, on the other hand, the plaintiff is entitled to his "out of pocket" losses. He is to be placed in the position he would have occupied if the tort had not been committed, namely the representations had not been made.<sup>101</sup> The tortious measure is clearly the more appropriate where the plaintiff is arguing that the defendant, through his misrepresentations, has caused the plaintiff to suffer loss by entering into a contract.<sup>102</sup>

It is true that courts, where they believe it to be fitting, have been able to award the tortious measure of damages in a contractual action by finding that the term broken was a promise to use reasonable care in making the statements. Such a case was *Esso Petroleum Co. Ltd. v. Mardon*<sup>103</sup> where

97. *Ibid.*, at 817.

98. See generally: Taylor, *supra* n. 10.

99. 1979, No. 11.

100. Tortious relief would not be available in the exceptional case where a plaintiff could not prove negligence on the part of the representor.

101. See Taylor, *supra* n. 10; Treitel, *supra* n. 12, at 266-269.

102. See Taylor, *supra* n. 10; Reiter, *supra* n. 10 at 260-263.

103. *Supra* n. 31.



the English Court of Appeal determined that Esso had not guaranteed that the throughput of petrol would be 200,000 gallons but it had made an estimate upon which it was reasonable for Mardon to rely. The Court, therefore, constructed a warranty consisting of a promise by Esso that it had used reasonable care in formulating its forecast. In this and similar cases, however, it would make more sense to found liability solely in tort and to impose contractual liability only where it is appropriate for the plaintiff to be compensated for his loss of bargain.<sup>104</sup>

## B. Rescission for Misrepresentation<sup>105</sup>

A victim of a pre-contractual misrepresentation may be able to rescind the ensuing contract between the parties and thereby restore the *status quo*. This equitable remedy will rarely, however, prove to be the most satisfactory way of protecting a representee. In the first place, a representee may feel that he is best served by the recovery of damages but, to claim damages, he will have to establish that a breach of contract or a tort has been committed. In rescinding, a representee may be able to claim an indemnity from the representor in respect of obligations created by the contract,<sup>106</sup> but such an indemnity is only a part of the process of rescission and does not resemble damages in any way. In England, by statute, a court may award damages in lieu of rescission,<sup>107</sup> but no such option is available to a Canadian court.

Secondly, rescission may work an injustice on the representor by requiring the setting aside of a transaction for what may be a comparatively minor transgression. It can be a harsher remedy than damages, especially where the parties have performed, or started to perform, the contract between them.

It is because of the potentially severe effects of rescission that various bars exist upon its exercise. In particular, rescission is no longer available if the contract has been affirmed,<sup>108</sup> if innocent third parties have acquired rights under the contract,<sup>109</sup> if substantial restitution of benefits received is impossible<sup>110</sup> and perhaps merely if undue time has elapsed.<sup>111</sup> Moreover, it is often stated that an executed contract cannot be rescinded in the absence of fraud or of *error in substantialibus*.<sup>112</sup> Nobody is quite certain of the operation of this particular bar, which has been abolished in England.<sup>113</sup> It has been avoided on occasions by a generous interpretation of what constitutes *error in substantialibus*<sup>114</sup> and by restricting it to contracts

104. See Taylor, *supra* n. 10 at 141-142.

105. See generally: Furmston, *Cheshire and Fifoot's Law of Contract* (10th ed. 1981) 237-266; Treitel, *supra* n. 12, at 243-291; Waddams, *The Law of Contracts* (1977) 248-257.

106. For example, *Whittington v. Seale-Hayne* (1900), 82 L.T. 49 (Ch.D.).

107. *Misrepresentation Act 1967*, c. 7, s. 2(2) (U.K.).

108. For example, *United Shoe Machinery Co. of Canada v. Brunet*, [1909] A.C. 330 (P.C.).

109. For example, *Lewis v. Averay*, [1972] 1 Q.B. 198 (C.A.).

110. For example, *Thurston v. Sireilen*, [1951] 4 D.L.R. 724 (Man. K.B.).

111. For example, *Leaf v. International Galleries*, [1950] 2 K.B. 86 (C.A.).

112. For example, *Redican v. Nesbitt*, [1924] S.C.R. 135.

113. *Misrepresentation Act 1967*, c. 7, s. 1(b) (U.K.).

114. For example, *Alessio v. Jovica* (1973), 42 D.L.R. (3d) 242 (Alta. S.C., App. Div.).

dealing with the transfer of interests in land.<sup>115</sup> Nevertheless the presence of this and the other bars to rescission means that the equitable remedy is of limited use in protecting the representee against pre-contractual misstatements.

Finally, it should be noted that rescission is available only for misrepresentations in the strict sense, namely false statements of fact, and that it is not available for statements of intention, opinion or law. The courts, however, have been quite ingenious in construing a given statement as one of fact in order to grant relief.<sup>116</sup>

It must be remembered that in the case of a misrepresentation, which has been made neither fraudulently nor negligently and which does not amount to a contractual term, rescission will be the only potential remedy in the hands of the representee.

### III. Tortious Liability

#### A. Fraudulent Misrepresentation

Until the recognition of a tortious liability for negligent misstatement, the only relief in tort available to a plaintiff in respect of pre-contractual misrepresentations lay in deceit. Such an action had, and still has, certain advantages. There is no difficulty, for example, in recovering purely economic loss in such a claim. Indeed, until 1789<sup>117</sup> its application was limited to contracting parties where any loss would almost certainly be economic. Secondly, an action in deceit can be combined with a rescission of the contract. Thirdly, the test for remoteness, at least in England, is broader than in an action for negligence.<sup>118</sup> The fact remains, however, that the tort of deceit can be useful in only a limited number of circumstances because of the necessity of establishing fraud on the part of the defendant. The House of Lords made it clear in *Derry v. Peek*<sup>119</sup> that nothing short of fraud will be sufficient and that the mere absence of a reasonable belief does not itself constitute fraud. Lord Herschell said:

First, in order to sustain an action of deceit, there must be proof of fraud, and nothing short of that will suffice. Secondly, fraud is proved when it is shewn that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false.<sup>120</sup>

Moreover, the tort of deceit is designed to protect parties against misstatements of fact. It is, therefore, especially difficult to establish fraud with respect to prospective statements. Where, for example, one party wrongly forecasts the profitability of a business which is being set up, it will be

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115. For example, *Bevan v. Anderson* (1957), 12 D.L.R. (2d) 69 (Alta. S.C.).

116. See generally: *Furmston*, *supra* n. 105, at 237-240; *Treitel*, *supra* n. 12, at 243-248; *Waddams*, *supra* n. 105, at 249-250.

117. *Supra* n. 73.

118. *Doyle v. Olby (Ironmongers) Ltd.*, [1969] 2 Q.B. 158 (C.A.). There are signs that this decision will be followed in Canada to some extent, see for example, *C.R.F. Holdings Ltd. v. Fundy Chemical International Ltd.*, [1982] 2 W.W.R. 385 (B.C.C.A.).

119. *Supra* n. 2.

120. *Ibid.*, at 374.

almost impossible for the other party to prove that such a forecast constituted in some way a statement of fact made with fraudulent intent.<sup>121</sup> Deceit, therefore, offers little protection to a party induced to enter into a disadvantageous contract through another's misrepresentations.

## B. Negligent Misstatement<sup>122</sup>

### 1. Duty of Care — General Considerations

The recognition of a tort of negligent misstatement causing financial loss by the House of Lords in *Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd.*<sup>123</sup> has cleared the way for the extensive operation of tort principles in the area of pre-contractual misstatements. The Court agreed that liability for negligent words could not be placed on the same footing as liability for negligent acts. Lord Pearce, for example, said:

The reason for some divergence between the law of negligence in word and that of negligence in act is clear. Negligence in word creates problems different from those of negligence in act. Words are more volatile than deeds. They travel fast and far afield. They are used without being expended and take effect in combination with innumerable facts and other words. Yet they are dangerous and can cause vast financial damage.<sup>124</sup>

Liability for negligent misstatements causing financial loss could not, therefore, depend upon broad notions of foreseeability. It had to be more circumscribed. To that end, the Court introduced the limiting principle that a "special relationship" had to exist between the maker and recipient of the statement for a duty of care to arise. *Hedley Byrne* itself concerned the liability of a bank for giving misleading credit references about one of its customers. These references were transmitted to the plaintiffs, through their own bankers, with the result that the plaintiffs incurred a substantial loss. Lords Reid, Devlin and Pearce would have imposed a duty of care on the defendant bank if it had not been for the fact that the references had been accompanied by express disclaimers of responsibility. Lords Hodson and Morris also accepted the possibility of a duty of care in making statements. They thought, however, that, even without the disclaimers, it was unreasonable to require the defendant bank to respond carefully in giving such informal references.<sup>125</sup> Thus, Lord Morris said:

There was in the present case no contemplation of receiving anything like a formal and detailed report such as might be given by some concern charged with the duty (probably for reward) of making all proper and relevant inquiries concerning the nature, scope and extent of a company's activities and of obtaining and marshalling all available evidence as to its credit, efficiency, standing and business reputation. There is much to be said, therefore, for the view that if a banker gives a reference in the form of a brief expression of opinion in regard to credit-worthiness he does not accept, and there is not expected from him, any higher duty than that of giving an honest answer.<sup>126</sup>

121. For example, the trial judgment in *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*, *supra* n. 52.

122. See generally: Schwartz, "Hedley Byrne and Pre-Contractual Misrepresentations: Tort Law to the Aid of Contract?" (1978), 10 *Ott. L. Rev.* 581.

123. *Supra* n. 1.

124. *Ibid.*, at 534.

125. *Ibid.*, at 503-504 (*per* Lord Morris) and at 512-514 (*per* Lord Hodson).

126. *Ibid.*, at 504. Rather than talking of a duty of honesty, it is submitted that it is better to say that, in certain circumstances, the duty of care can be discharged without the informant having, for example, to undertake extensive enquiries. The duty of care is merely a duty to take such care as the particular circumstances of the case require. This point is well made in *Winfield and Jolowicz on Tort* (11th ed. 1979) 265.

It is not easy to extract from the decision the basis upon which a duty of care will be imposed in respect of negligent misstatements causing financial loss.<sup>127</sup> The House of Lords stressed the fact that, for a duty of care to arise, the informant must have assumed responsibility for the exercise of reasonable care in making his statements.<sup>128</sup> On this basis, therefore, the duty of care is not imposed but is undertaken voluntarily by the defendant. Lord Reid, for example said:

So it seems to me that there is good sense behind our present law that in general an innocent but negligent misrepresentation gives no cause of action. There must be something more than the mere misstatement . . . The most natural requirement would be that expressly or by implication from the circumstances the speaker or writer has undertaken some responsibility. . . .<sup>129</sup>

The emphasis upon an assumption of responsibility by the representor means that, in some respects, liability in tort for negligent misstatement is akin to a contractual liability. Lord Devlin made the connection between tort and contract in this context quite explicit:

. . . [T]here is ample authority to justify your Lordships in saying now that the categories of special relationships which may give rise to a duty to take care in word as well as in deed are not limited to contractual relationships or to relationships of fiduciary duty, but include also relationships which in the words of Lord Shaw in *Nocton v. Lord Ashburton*, [1914] A.C. 932 at 972, are 'equivalent to contract,' that is, where there is an assumption of responsibility in circumstances in which, but for the absence of consideration, there would be a contract.<sup>130</sup>

Of course, rarely will a defendant expressly assume responsibility for the accuracy of what he says. The major question to be resolved, therefore, is under what circumstances will it be inferred that a defendant has assumed such a responsibility. In determining this question, a court is in effect deciding whether or not a duty of care should be imposed upon the defendant. As a practical matter, therefore, it makes little difference whether the duty of care is regarded as assumed or imposed, except perhaps when the issue is raised as to the effect of an express disclaimer by the defendant. If the duty is assumed, then a disclaimer must operate to prevent such an assumption of responsibility. If, on the other hand, the duty is imposed, then arguably a disclaimer can operate only as a defence to a breach of duty. In the latter situation, a disclaimer would presumably be subjected to a much more rigorous scrutiny by the courts. Lord Reid gave the broadest view of when the defendant would be under a duty of care in respect of statements made by him. He could see:

. . . [N]o logical stopping place short of all those relationships where it is plain that the party seeking information or advice was trusting the other to exercise such a degree of care as the circumstances required, where it was reasonable for him to do that, and where the other gave the information or advice when he knew or ought to have known that the inquirer was relying on him.<sup>131</sup>

In general, therefore, a defendant will be taken to have assumed a duty of care where it is reasonable for a party to rely on the defendant's statements.

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127. For an excellent discussion of this question, see Feldthusen, "Negligent Misrepresentation: A Closer Look at the Basis of the Defendant's Duty of Care" in *Issues in Tort Law* (Steel and Rodgers-Magnet ed. 1983) 179-217.

128. *Ibid.*, at 192-194.

129. *Supra* n. 1, at 483.

130. *Ibid.*, at 528-529.

131. *Ibid.*, at 486.

The language used by the other Law Lords was not as broad as that of Lord Reid but it is very much to the same effect. Lord Morris, for example, said:

My Lords, I consider that it follows and that it should now be regarded as settled that if someone possessed of a special skill undertakes, quite irrespective of contract, to apply that skill for the assistance of another person who relies upon such skill, a duty of care will arise. The fact that the service is to be given by means of or by the instrumentality of words can make no difference. Furthermore, if in a sphere in which a person is so placed that others could reasonably rely upon his judgment or his skill or upon his ability to make careful inquiry, a person takes it upon himself to give information or advice to, or allows his information or advice to be passed on to, another person who, as he knows or should know, will place reliance upon it, then a duty of care will arise.<sup>132</sup>

To a large extent, the House of Lords was content to recognize generally the existence of a tort of negligent misstatement but to leave its precise scope to be drawn by later decisions. The House of Lords did, however, draw a distinction between statements made on social or informal occasions and those made in a professional or business connection. Lord Pearce said that: "To import . . . a duty the representation must normally, I think, concern a business or professional transaction whose nature makes clear the gravity of the inquiry and the importance and influence attached to the answer."<sup>133</sup>

This common sense distinction, however, was employed by the majority of the Privy Council in *Mutual Life and Citizens' Assurance Co. Ltd. v. Evatt*<sup>134</sup> to restrict severely the potentially very broad principle laid down in *Hedley Byrne*. The plaintiff, who was a policy holder in the defendant insurance company, sought advice from the defendant as to the financial stability of a closely associated company. In reliance upon that advice, the plaintiff did not realize upon certain investments existing in that associated company and indeed invested further sums of money. The advice was unreliable and the plaintiff lost his money. The plaintiff's claim under *Hedley Byrne* was dismissed on the ground that the plaintiff had not alleged that the defendant either carried on the business of advising on investments or in some other way had claimed to possess the necessary skill and competence to do so and was prepared to exercise the necessary diligence to give reliable advice. The majority judgment was based on the notion that a duty of care in this context was the same as a "duty to conform to an ascertainable standard of skill and competence in relation to the subject-matter of the advice."<sup>135</sup> *Hedley Byrne* liability, therefore, could be attracted in the main only by those who carry on a "business or profession which involves the giving of advice which calls for special skill and competence"<sup>136</sup> and where the advice given is in pursuance of that business or profession. In that way, the adviser has let it be known that "he claims to possess the standard of

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132. *Ibid.*, at 502-503.

133. *Ibid.*, at 539. See also Lord Reid, *ibid.*, at 482-483. *John Bosworth Ltd. v. Professional Syndicated Developments Ltd.* (1979), 97 D.L.R. (3d) 112 (Ont. H.C.) is a recent illustration of a court denying a duty of care in respect of statements made on a social occasion.

134. [1971] A.C. 793 (P.C.) (N.S.W.).

135. *Ibid.*, at 803.

136. *Ibid.*, at 805.

skill and competence and is prepared to exercise diligence which is generally shown by persons who carry on the business of giving advice of the kind sought."<sup>137</sup> The majority also recognized that it would be possible for an adviser to let it be known in some way other than the carrying on of a business or profession that:

... [H]e claims to possess skill and competence in the subject-matter of the particular inquiry comparable to those who do carry on the business or profession of advising on that subject-matter and is prepared to exercise a comparable skill and competence in giving the advice.<sup>138</sup>

The effect of the majority decision, therefore, was to restrict *Hedley Byrne* liability to those professing to have some special skill. The vigorous dissenting judgment of Lords Reid and Morris castigated the reasoning of the majority. They said:

We can see no ground for the distinction that a specially skilled man must exercise care but a less skilled man need not do so. We are unable to accept the argument that a duty to take care is the same as a duty to conform to a particular standard of skill. One must assume a reasonable man who has that degree of knowledge and skill which facts known to the inquirer (including statements made by the adviser) entitled him to expect of the adviser, and then inquire whether such a reasonable man could have given the advice which was in fact given if he had exercised reasonable care.<sup>139</sup>

This dissenting judgment was all the more powerful because both Lord Reid and Lord Morris had delivered leading judgments in *Hedley Byrne* itself.

If it had been applied strictly, *Evatt* would have operated as a very serious limitation on *Hedley Byrne* liability in general and would have made it especially difficult to impose tortious liability in respect of pre-contractual misstatements.<sup>140</sup> Fortunately, *Evatt* has not been treated with the greatest of respect.<sup>141</sup> In two decisions, the English Court of Appeal has indicated that it views itself as quite free to reject the Privy Council decision. In *Esso Petroleum Co. v. Mardon*,<sup>142</sup> Ormrod L.J. said quite explicitly that he would apply the minority view in *Evatt*. He thought that if "the majority view were to be accepted, the effect of *Hedley Byrne* would be so radically curtailed as to be virtually eliminated."<sup>143</sup> It is true, that Lord Denning M.R. did approve of the majority judgment in *Evatt* but his judgment undoubtedly extended the majority judgment in *Evatt*. In particular, he widened *Evatt* to include those with special knowledge as well as those with special skill. Only two years later, however, in *Howard Marine & Dredging Co. Ltd. v. A. Ogen & Sons (Excavations) Ltd.*,<sup>144</sup> Lord Denning M.R. stated unequivocally that he preferred the reasoning of the minority in *Evatt*.<sup>145</sup> Shaw L.J. agreed with Lord Denning M.R. on this point.<sup>146</sup>

137. *Ibid.*, at 804.

138. *Ibid.*, at 806.

139. *Ibid.*, at 812.

140. See generally: Schwartz, *supra* n. 122.

141. See Irvine, Annot. (1980), 13 C.C.L.T. 202.

142. *Supra* n. 31.

143. *Ibid.*, at 827.

144. *Supra* n. 86.

145. *Ibid.*, at 591.

146. *Ibid.*, at 600.

*Evatt* has not been received markedly more favourably in Canada. It does have its adherents. In *J. Nunes Diamonds Ltd. v. Dominion Electric Protection Co.*,<sup>147</sup> for example, it was apparently approved of by the majority of the Supreme Court of Canada under Pigeon J..<sup>148</sup> In that case, however, there were many other grounds for the ultimate decision and a strong minority clearly did not favour the *Evatt* restriction. In other cases *Hedley Byrne* liability has been expressly limited to experts or specialists, although *Evatt* has not been cited specifically.<sup>149</sup>

The majority of cases have simply left the issue of the applicability of *Evatt* undecided because it was unnecessary to reach a definite conclusion on the facts of a particular case. Reliance has often been placed upon the Supreme Court judgment in *The Pas v. Porky Packers Ltd.*,<sup>150</sup> where Spence J., for the majority, said:

I quote the statement in *Charlesworth on Negligence*, 5th ed., para. 49, p. 32, as being a proper statement of the principle applied in [*Hedley Byrne*]:

The House of Lords has thus expressed the opinion that if in the ordinary course of business including professional affairs a person seeks advice or information from another who is not under any contractual or fiduciary obligation to give it, in circumstances in which a reasonable man so asked would know that he was being trusted or that his skill or judgment was being relied on, and such person then chooses to give the requested advice or information without clearly disclaiming any responsibility for it, then he accepts a legal duty to exercise such care as the circumstances require in making his reply; for a failure to exercise that care, an action for negligence will lie if damage or loss results.<sup>151</sup>

There is no suggestion in that quotation from Charlesworth nor in the remainder of Spence J.'s judgment that the *Evatt* qualification is applicable.

Some Canadian cases have rejected *Evatt* quite explicitly. At trial, in *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*,<sup>152</sup> for example, Rutherford J. refused to apply the *Evatt* restriction.<sup>153</sup> Most recently, in *Nelson Lumber Co. Ltd. v. Koch*,<sup>154</sup> the Saskatchewan Court of Appeal has lent its weight to the view that *Evatt* should not be followed in Canada. Bayda J.A. stressed that a court should not lose sight of the original principle laid down in *Hedley Byrne* itself by a rigorous application of any subsequent test such as that laid down in *Evatt*. The original principle was a broad and flexible one and *Hedley Byrne* should be interpreted broadly and not in a restrictive manner. In the same case, Brownridge J.A. adopted Spence J.'s judgment in the *Porky Packers* cases which, as Brownridge J.A. observed, contained none of the qualifications introduced by *Evatt*.

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147. [1972] S.C.R. 769.

148. *Ibid.*, at 775-776.

149. For example, *Beebe v. Robb* (1977), 81 D.L.R. (3d) 349 (B.C.S.C.); *Kerr v. Gingras* (1980), 24 B.C.L.R. 372 (S.C.).

150. [1977] 1 S.C.R. 51. See for example, *Faunatlantic Ltd. v. Province of New Brunswick* (1977), 20 N.B.R. (2d) 128 at 148 (Q.B.); *Grand Restuarants Ltd. v. City of Toronto* (1981), 32 O.R. (2d) 757 at 771-772 (H.C.); *aff'd* (1982), 140 D.L.R. (3d) 191 (C.A.).

151. *Ibid.*, at 63.

152. *Supra* n. 52.

153. *Ibid.*, at 336.

154. (1980), 111 D.L.R. (3d) 140.

The *Evatt* restriction, therefore, has failed to gain a foothold in Canadian jurisprudence. It is also interesting to note that *Evatt* is not being applied in recent Australian authorities.<sup>155</sup>

The majority in *Evatt* suggested another basis upon which a duty of care could be founded, namely where the representor had a financial interest in his advice.<sup>156</sup> Lord Diplock, in making this suggestion, was thinking of section 552 of the *Restatement of the Law of Torts (2d)*<sup>156a</sup> which provides as follows:

552(1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

Lord Diplock's *dictum* has been followed by a few Commonwealth cases as a way of avoiding some of the strictures of the majority judgment in *Evatt*, especially in the context of pre-contractual misstatements where potentially it can have the greatest impact.<sup>157</sup> Often, however, it has been ignored as an independent means of establishing a duty of care and has been regarded as just one factor in the determination of whether a special relationship exists between the parties.<sup>158</sup>

The financial interest of the representor has been strenuously advanced as a means of extending *Hedley Byrne* liability to pre-contractual misstatements.<sup>159</sup> In view of the generally unwelcome reception given to the majority judgment in *Evatt*, however, it is submitted that there is no need to rely upon the representor's financial interest as an independent basis for the imposition of a duty of care. *Hedley Byrne* is a sufficient basis in itself and can be, and has been, extended quite easily to pre-contractual misstatements. There is no Canadian case which has applied the *dictum* of Lord Diplock. In *Nelson Lumber Co. Ltd. v. Koch*,<sup>160</sup> an argument could easily have been raised that the defendant had a financial interest in its advice. In that case the plaintiff wanted to buy a packaged home from the defendant but needed someone to build it for him. Representatives of the defendant recommended one Handford who, to their knowledge, was an undischarged bankrupt. The plaintiff suffered loss because Handford did not complete the job and he sued the defendant for negligent misstatement. As Bayda J.A. pointed out, "it was . . . undoubtedly to the financial advantage of Nelson to insure that Mr. Koch found a contractor."<sup>161</sup> The Court determined that the defendant owed a duty of care to the plaintiff, but it rested its decision not on the defendant's financial interest in the transaction but upon a broad reading of *Hedley Byrne*.

155. For example, *L. Shaddock & Associates Pty. Ltd. v. Parramatta City Council* (1981), 55 A.L.J.R. 713 (H.C.).

156. *Supra* n. 134 at 809.

156a. American Law Institute (Washington, D.C.: The Institute, 1976).

157. For example, *Capital Motors Ltd. v. Beecham*, [1975] 1 N.Z.L.R. 576 (S.C.).

158. For example, *Presser v. Caldwell Estates Pty. Ltd.*, [1971] 2 N.S.W.L.R. 471 (C.A.); *Ellul v. Oakes*, *supra* n. 87.

159. Schwartz, *supra* n. 122, at 605-613.

160. *Supra* n. 154.

161. *Ibid.*, at 146.



## 2. Duty of Care in respect of Pre-Contractual Misstatements

After *Hedley Byrne* had been decided, the question arose as to whether the principle laid down by the House of Lords in that case could be applied to misrepresentations inducing the formation of a contract between the representor and representee. This would, in effect, do away with the rule that there could be no damages for what contract would regard as a purely innocent misrepresentation.<sup>162</sup> *Hedley Byrne*, itself, did not solve this question. Lord Reid, for example, implied that *Hedley Byrne* could not apply to contracting parties because the question there would be simply whether the particular statement amounted to a contractual term.<sup>163</sup> Lord Hodson went further and said:

... [T]hat it may in certain cases appear to be strange that, whereas innocent misrepresentation does not sound in damages, yet in the special cases under consideration an injured party may sue in tort a third party whose negligent misrepresentation has induced him to enter into the contract.<sup>164</sup>

It seems implicit in this statement that *Hedley Byrne* does not apply as between the people who ultimately enter into a contract. On the other hand, Lord Devlin said that "wherever there is a relationship equivalent to contract, there is a duty of care."<sup>165</sup> As one commentator has pointed out, the relationship between parties in the process of contracting must be one which is equivalent to contract.<sup>166</sup>

In the aftermath of *Hedley Byrne*, some writers expressed serious doubts as to the applicability of that decision to pre-contractual negotiations. Professor Glasbeek, for example, said that, when the parties are negotiating about a contract, then "it is fair to postulate that neither of the parties is willing to assume responsibility for anything he does not in fact specifically endorse by inclusion in the contract."<sup>167</sup> In other words, negotiating parties are assumed to be operating at arm's length and are seeking to extract the best possible bargain from the other side. They are willing to take responsibility only for those obligations expressed in the contract. There is, therefore, little room for the operation of tort principles in this context. In those cases where it can be said that a representor has assumed responsibility for the truth of his representation, his statement will almost certainly be treated as a contractual term and hence a contractual remedy will lie.<sup>168</sup> Professor Honoré made this point succinctly:

If in the circumstances it can be inferred that one party assumes responsibility for the truth of a statement made to the other, the law of contract, independently of *Hedley Byrne*, imposes a liability sounding in damages. If, on the other hand, a statement is treated as a mere representation . . . this is because there is no such inference implicit in the circumstances of the case.<sup>169</sup>

162. For example, Stevens, *supra* n. 75, at 155-160.

163. *Supra* n. 1, at 483.

164. *Ibid.*, at 511.

165. *Ibid.*, at 530.

166. Weir, "Liability for Syntax", [1963] Camb. L.J. 216 at 220.

167. Glasbeek, "Limited Liability for Negligent Misstatement" in *Studies in Canadian Tort Law* (Linden ed. 1968) 115 at 131.

168. *Ibid.*, at 131-132.

169. (1965), 8 J.S.P.T.L. 284 at 296-297. See also Coote, "The Effect of *Hedley Byrne*" (1967), 2 N.Z.U.L. Rev. 263 at 276-277.

On this theory, therefore, *Hedley Byrne* has a negligible effect on liability for pre-contractual misstatements. It will be limited to what Professor Honoré sees as the rare situation where the representor assumes a duty of care but does not guarantee the truth of what he says.

It is true that for about 10 years *Hedley Byrne* was not seized upon by the courts as a means of imposing liability for pre-contractual misstatements. Even in those cases which accepted the possibility of *Hedley Byrne* liability being imposed in the pre-contractual context, it was recognized that *Hedley Byrne*'s sphere of operation would necessarily be limited. In *Dillingham Constructions Pty. Ltd. v. Downs*,<sup>170</sup> for example, the plaintiffs entered into a contract with the defendant, the New South Wales Government, for the deepening of a harbour. The contract took much longer to complete than expected because initial blasting to break up the harbour floor was ineffective and other procedures had to be used. The plaintiffs later discovered that there were disused coal workings under the harbour and concluded that the blasting had been ineffective because its effect had been dissipated throughout the underground workings. The defendant had known of these disused coal workings all the time. The plaintiffs sued the defendant *inter alia* for negligent misrepresentation inducing them to enter into the contract. The Court determined that the mere fact that the parties were in a pre-contractual relationship did not automatically preclude the application of *Hedley Byrne*. In particular, the nature and extent of the specialized knowledge in the defendant's possession, which would have been of vital importance to the plaintiffs, rendered *Hedley Byrne* potentially applicable. In the final analysis, the plaintiffs' claim was dismissed because, on the facts, the defendant had not assumed responsibility for providing the plaintiffs with accurate or full information as to special site conditions nor with advice as to difficulties likely to arise in the carrying out of the project. Also, the plaintiffs had not relied upon the defendant to supply any such information or advice. For present purposes, the importance of the judgment lies in the fact that the Court indicated that a pre-contractual relationship would not normally qualify as a special relationship within *Hedley Byrne* because a "person in pre-contract negotiations is entitled to and usually does seek to make the most advantageous deal he can. The other party does likewise; thus each is at liberty to have regard solely to his own interests."<sup>171</sup>

It is wrong to deny *Hedley Byrne* a role to play in a pre-contractual relationship or to conclude that it is unnecessary to rely upon *Hedley Byrne* in that context because the contractual remedies are adequate. The problems with establishing contractual liability in respect of pre-contractual misstatements have already been observed in the first part of this paper. Traditionally, there have been difficulties with overcoming both the parol evidence rule and the strict test of contractual intention as laid down in *Heilbut, Symons & Co. v. Buckleton*.<sup>172</sup> More recently, some courts have been prepared to invent collateral warranties in order to protect a represen-

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170. [1972] 2 N.S.W.L.R. 49 (S.C.).

171. *Ibid.*, at 55. See also *Ellul v. Oakes*, *supra* n. 87 at 380 (*per* Bray C.J.) (S.C.).

172. *Supra* n. 3.

tor who has relied upon pre-contractual misstatements. Lord Denning M.R., in *Esso Petroleum Co. Ltd. v. Mardon*, made this point very clearly:

... [T]here have been many cases since I have sat in this court where we have readily held a representation — which induces a person to enter into a contract — to be a warranty sounding in damages.<sup>173</sup>

Where the basis of a plaintiff's claim is that the defendant, through his misrepresentations, has caused the plaintiff to suffer loss by entering into a contract, it makes little sense to invent a contractual remedy where a tortious one is at hand. The plaintiff's claim is fundamentally a tortious one and should be recognized as such. Moreover, by allowing an action in tort, a court is less likely to award an inappropriate measure of damages, namely the expectation measure. One of the leading cases where contractual damages were awarded is *Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd.*<sup>174</sup> The English Court of Appeal held that a pre-contractual statement by a car dealer to a prospective purchaser that the car in question had done only 20,000 miles since it had been equipped with a new engine and gearbox constituted a contractual term. In determining that it was reasonable to construe the defendant's statement as a warranty, the Court applied a test much more in accordance with *Hedley Byrne* than *Heilbut, Symons*. Lord Denning M.R. said:

Here we have a dealer, Mr. Smith, who was in a position to know, or at least to find out, the history of the car. He could get it by writing to the makers. He did not do so. Indeed it was done later. When the history of this car was examined, his statement turned out to be quite wrong. He ought to have known better. There was no reasonable foundation for it.<sup>175</sup>

The need for *Hedley Byrne* to apply to pre-contractual misstatements is all the greater in Canada because of the absence of a statutory remedy such as that contained in section 2(1) of the English *Misrepresentation Act 1967*<sup>176</sup> which provides:

Where a person has entered into a contract after a misrepresentation has been made to him by another party thereto and as a result thereof he has suffered loss, then, if the person making the misrepresentation would be liable to damages in respect thereof had the misrepresentation been made fraudulently, that person shall be so liable notwithstanding that the misrepresentation was not made fraudulently, unless he proves that he had reasonable ground to believe and did believe up to the time the contract was made the facts represented were true.

This statutory remedy has definite advantages over a common law claim under *Hedley Byrne*. There is no need for the plaintiff to establish that a special relationship exists between himself and the defendant. Moreover, the section places the burden on the defendant to show that he had reasonable grounds to believe that his representation was true.<sup>177</sup> On the other hand, the statutory remedy applies only, it seems, to misstatements of fact and will not be available where no contract is in fact formed between the parties.

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173. *Supra* n. 31, at 817.

174. *Supra* n. 25.

175. *Ibid.*, at 67.

176. 1967, c. 7 (U.K.).

177. The defendant failed to discharge this burden, for example, in *Howard Marine and Dredging Co. Ltd. v. A. Ogdon & Sons (Excavations) Ltd.*, *supra* n. 86.

Over the years, the anomaly has been perceived that a person could be liable under *Hedley Byrne* if his misstatement induced the plaintiff to enter into a contract with some third party,<sup>178</sup> but not if his misstatement induced the plaintiff to enter into a contract with the representor himself. The Canadian position was complicated, however, by certain *dicta* of Pigeon J. in *J. Nunes Diamonds Ltd. v. Dominion Electric Protection Co.* to the following effect:

... [T]he basis of tort liability considered in *Hedley Byrne* is inapplicable to any case where the relationship between the parties is governed by a contract, unless the negligence relied on can properly be considered as 'an independent tort' unconnected with the performance of that contract...<sup>179</sup>

The true scope of this statement is far from clear. It does suggest that liability should not normally be imposed as between contracting parties. Its major effect has been felt in the area of tortious liability for the negligent performance of a contract. *Nunes Diamonds* itself dealt with a post-contractual rather than a pre-contractual misstatement and Pigeon J. himself mentioned the fact that it was "not a case of misrepresentation leading to the making of a contract."<sup>180</sup> This point was stressed recently by the Saskatchewan Court of Appeal in *Nelson Lumber Co. Ltd. v. Koch*.<sup>181</sup>

The first application in Canada of *Hedley Byrne* to pre-contractual misstatements was made by the trial judge in the British Columbia decision of *Sealand of the Pacific Ltd. v. Ocean Cement Ltd.*<sup>182</sup> In that case the defendant was held liable in tort for the negligent misstatement of its employee that a certain product called "zonolite" was suitable for the plaintiff's purposes in connection with renovations being proposed for the plaintiff's oceanarium. A contract was later formed between the parties for the supply of zonolite and the defendant was also held to be in breach of this contract. The Judge had no difficulty in applying *Hedley Byrne* to this pre-contractual misstatement. *Nunes Diamonds* was distinguished on the simple basis that that case had not dealt with a pre-contractual misstatement. Unfortunately, the Court of Appeal did not discuss the defendant's tortious liability except to say that there might be problems with such a claim.<sup>183</sup> It did not say what those problems might be, but contented itself with finding the defendant liable in contract.

The trial decision in *Sealand* was followed quickly in New Zealand in *Capital Motors Ltd. v. Beecham*,<sup>184</sup> where it was held that a prospective seller of goods was vicariously liable to the prospective buyer for the negligent misstatements of its salesman made in the course of pre-contractual

178. This was the situation in *Hedley Byrne* itself. See also *Dodds and Dodds v. Millman* (1964), 45 D.L.R. (2d) 472 (B.C.S.C.) where the plaintiff was able to recover against a real estate agent who had induced the plaintiff into buying an apartment building through misstatements as to the projected revenue and expenses of that building.

179. *Supra* n. 147, at 777-778.

180. *Ibid.*, at 777.

181. *Supra* n. 154. See also the very similar case of *Beaver Lumber Co. Ltd. v. McLenaghan*, [1983] 2 W.W.R. 171 (Sask. C.A.).

182. (1973), 33 D.L.R. (3d) 625 (B.C.S.C.); var'd (sub nom. *Sealand of the Pacific Ltd. v. Robert C. McHaffie Ltd.*), [1974] 6 W.W.R. 724 (C.A.).

183. [1974] 6 W.W.R. 724 at 725.

184. *Supra* n. 157.

negotiations.<sup>185</sup> The turning-point, however, was the decision of the English Court of Appeal in *Esso Petroleum Co. Ltd. v. Mardon*,<sup>186</sup> the facts of which have already been given.<sup>187</sup> The Court was in no doubt that *Hedley Byrne* applied to pre-contractual misstatements and, as an alternative ground for decision, Esso was liable in the tort of negligent misstatement. Lord Denning M.R. made the following statement of the law which has frequently been relied upon in later decisions:

... [I]f a man, who has or professes to have special knowledge or skill, makes a representation by virtue thereof to another — be it advice, information or opinion — with the intention of inducing him to enter into a contract with him, he is under a duty to use reasonable care to see that the representation is correct, and that the advice, information or opinion is reliable. If he negligently gives unsound advice or misleading information or expresses an erroneous opinion, and thereby induces the other side to enter into a contract with him, he is liable in damages.<sup>188</sup>

*Esso* turned the tide in Canada and led to widespread acceptance of the proposition that *Hedley Byrne* could apply to pre-contractual misstatements.

The most influential Canadian decision to date to apply *Hedley Byrne* in this context is that of the Ontario Court of Appeal in *Sodd Corp. Inc. v. Tëssis*.<sup>189</sup> In that case, the Court held that the defendant, a chartered accountant and licensed trustee in bankruptcy, owed a duty of care for representations made to the plaintiff as to the retail value of certain stock of a bankrupt which was being sold by tender. These representations induced the plaintiff to submit the tender which was ultimately successful. *Nunes Diamonds* was distinguished on the basis that it did not concern a pre-contractual misrepresentation.<sup>190</sup> The Supreme Court of Canada has not, as yet, expressed a definitive view on whether *Hedley Byrne* can apply to pre-contractual misstatements,<sup>191</sup> but it is submitted that it would now be too late for that Court to oppose the tide of recent developments.<sup>192</sup>

It must be stressed that in many of the cases where the applicability of *Hedley Byrne* to pre-contractual negotiations was recognized the plaintiff in fact lost because it was also held that the defendant had either excluded the assumption of a duty of care or had excluded liability for breach of such a duty by means of an exemption clause in the later contract between the parties.<sup>193</sup> There are serious questions to be answered as to the extent

185. See also *Peters v. Parkway Mercury Sales Ltd.* (1975), 58 D.L.R. (3d) 128 (N.B.S.C. App. Div.).

186. *Supra* n. 31.

187. See text *supra*, at n. 93.

188. *Supra* n. 31, at 820.

189. *Supra* n. 57.

190. Both *Esso* and *Sodd* were relied upon at trial both in *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*, *supra* n. 52 and *Carman Construction Ltd. v. Canadian Pacific Rlwy. Co.*, *supra* n. 66 and in *Roberts v. Montex Development Corp.*, *supra* n. 57.

191. In *Carman Construction Ltd. v. Canadian Pacific Rlwy. Co.*, *ibid.*, the Supreme Court was able to avoid this issue by finding that anyway the defendant had disclaimed effectively any assumption of responsibility.

192. It must be conceded that there have been a few isolated cases which have continued to rely upon a narrow view of *Nunes Diamonds* to the effect that *Hedley Byrne* liability is automatically excluded once the parties have entered into a contract as, for example, *Beebe v. Robb*, *supra* n. 149 and *Sperry Rand Canada Ltd. v. Thomas Equipment Ltd.*, *supra* n. 54.

193. For example, the trial judgment in *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*, *supra* n. 52; *Carman Construction Ltd. v. Canadian Pacific Rlwy. Co.*, *supra* n. 66.

to which such a clause can, and should be able to, protect a defendant from the consequences of his misrepresentations. These questions are not the subject of the present paper. For the moment, suffice it to say that a court should be wary of allowing a defendant too readily to avoid the consequences of his own misstatements when they have induced the plaintiff to enter into the very contract upon which the defendant is relying to protect himself.

Finally, there are still some unanswered questions as to the extent to which *Hedley Byrne* can operate in the pre-contractual context. In particular, can there be liability for a negligent pre-contractual misstatement which does not in fact lead to the formation of a contract? This question arose for consideration in the New Zealand case of *Holman Construction Ltd. v. Delta Timber Co. Ltd.*<sup>194</sup> In that case, the defendant offered to supply the plaintiff with timber at a set price for a building project to be carried out by the plaintiff. The plaintiff relied on that offer and entered a building contract. The defendant then realized that it had miscalculated and revoked its offer. The plaintiff was forced to accept the next lowest tender and he sued the defendant in *Hedley Byrne* for the difference between the two tenders. The plaintiff's action was dismissed on the basis that no duty of care was owed by the defendant in these circumstances. The Court said that to allow the action to succeed would be to subvert the rules of offer and acceptance. The offeree should either have accepted the offer or have ensured in some way that it could not be revoked. Henry J. said:

Even if one treats the offer in a manner most favourable to the plaintiff it is only advice to the plaintiff that the defendant is prepared, if the plaintiff accepts the offer, to supply timber on the terms stated. It is not a representation that a careful or even an honest assessment of the price asked has been made. It is not advice that the offer will remain open for any specified time. It is no more than the expression of an intention to become bound by contract if the offer be accepted. The offeror can be under no duty to make vis-a-vis the offeree a careful estimate of the price he seeks. It is for the offeree to judge the worth of the offer and to accept it while it is still capable of acceptance if he wishes to create any duty on the offeror. It is then no more than a contractual duty in terms of the contract.<sup>195</sup>

Despite the developments which have taken place since this case was decided, it is submitted that the decision is still a good one for the reasons given by the Judge. A person should be able to make any offer he likes, however foolish and however negligently prepared. Only if his offer is accepted, should he have to bear the consequences of his stupidity or carelessness.

In other situations, it may be entirely appropriate to award damages under *Hedley Byrne* even though no contract in fact follows. Such a situation was presented in *Box v. Midland Bank Ltd.*,<sup>196</sup> where the plaintiff was advised by the defendant's branch manager that his application for a loan would have to be referred to Regional Head office for approval but

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194. [1972] N.Z.L.R. 1081 (S.C.).

195. *Ibid.*, at 1082.

196. [1979] 2 Lloyd's Rep. 391 (Q.B.).

that there would be no difficulties with a loan being granted. This was not the case, as the branch manager should have known, and the loan was refused. The plaintiff sought to recover from the defendant losses incurred as a result of relying upon the branch manager's negligent advice. The Court held that the defendant was liable on the basis of *Hedley Byrne*. It was held that, on the facts of the case, the plaintiff had reasonably relied upon the branch manager's prediction as to the outcome of the application for a loan.

#### IV. Conclusion

The position has thus been reached that a party, induced to enter into a contract by another's misrepresentations, is potentially protected in both contract and tort. Through a combination of both contractual and tortious remedies, there are very few situations in which a deserving plaintiff will fail. Traditionally, there were gaps in a representee's contractual protection which could be filled only by distorting principles of contract law through the invention of contractual terms. The availability of relief in tort, however, has rendered such distortion unnecessary. Contract can thus be used where the basis of the plaintiff's claim is that the defendant has guaranteed that a certain event will occur or that a certain statement is true. Tort can be used where the basis of the plaintiff's claim is that he has relied to his detriment upon the defendant's negligent misrepresentations by entering into a disadvantageous contract.

