EXCLUSION CLAUSES AND STANDARD FORM CONTRACTS, A COMPARATIVE STUDY OF ENGLISH AND MALAYSIAN LAW

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CONTENTS

ABSTRACT

Malaysia is one of the most developed country amongst the developing countries. The government has announced 'Vision 2020' - which aims at Malaysia becoming a fully industrialized country by that year. Surely commercial activities in Malaysia will increase tremendously to achieve that target. However, the need for protecting the interests of consumers has also assumed great importance.

The problem of exclusion clauses in standard form contracts has long been haunting the public at large. As pointed out by Atiyah, it is important not to underestimate the magnitude of this problem and the extent to which these exemption clauses in standard form contracts are undermining the theory that contracts depend on mutual agreement or that there is freedom to contract. "The average citizen will certainly find that the vast majority of the most important contracts he makes in his life are made on terms more or less imposed on him."

In Malaysia, March 15 is celebrated as the World Consumer Rights Day. This year the event is celebrated for the second time. It was celebrated with the view to enhancing public consciousness of their rights as consumers.

This dissertation deals with the question of protecting of consumer interests vis-a-vis exclusion clauses. It is a comparative study of English and Malaysian law. The relevant statutory provisions and judicial decisions have been examined critically.

Chapter 1 is an introductory discussion of the conceptual background of exclusion caluses and limitation clauses in standard form contracts. The problems posed by the exclusion clauses are brought out. Chapter 2 contains a brief discussion of the historical background of the standard form contracts. Chapter 3 shows how the judiciary in England and Malaysia devised various techniques to contain the mischief of these clauses and how far did they succeed in their endeavour.

Chapter 4 deals with the statutory measures adopted in England and Malaysia to carry forward the task of controlling these clauses when judiciary failed to make much head way. Chapter 5 is a comparative analysis of the position in England and Malaysia. The similarities and differences in the two systems are brought out. Chapter 6 is a brief discussion of recent case law dealing with exclusion clauses vis-a-vis third parties.

Finally, Chapter 7 contains some suggestions which the researcher has made to improve the position of the present law, particularly in Malaysia. A brief bibliography is appended at the end of this dissertation.

TABLE OF CASES

A

C

E

G

O

Odernamall & Co. v American President Lines Ltd and Penang Harbour Board (No. 1) [1956] MLJ 6

Olley v Marlborough Court, Ltd
[1949] 1 K.B. 532

P

Parker v South - Eastern Railway Co.
(1877) CA

Photo Production Ltd v. Securicor Transport, Ltd.
[1980] A.C. 827

Port Swettenham Authority v TW Wu & Co. Sdn Bhd [1978] 2 MLJ 137

Pyrene Co. Ltd v Scindia Navigation Co. Ltd [1954] 2 Q.B. 402

S

Schroeder v Music Publishing Co
[1977] 1 W.L.R 1308

Schroeder Publishing Co Ltd v Macaulay [1974] 1 W.L.R 1308

Scruttons Ltd v Midland Silicones Ltd. [1962] A.C. 446

Sharikat Lee Heng Sdn Bhd v. Port Swettenham Authority
(1971) 1 MLJ 110

Suisse Atlantique Case
[1967] 1 AC 361

T

The Aliakmon [1986] A.C. 785

The Eurymedon [1975] A.C. 154

The New York Star [1981] 1 W.L.R 138

Theresa Chong v Kin Khoon & Co

Tites Dental & Photo Supply Sdn. Bhd. v Empresa Lineas

Maritimes Argentinas & Ors [1977] 2 MLJ 13

Thornton v Shoe Lane Parking Ltd [1971] 2 QB 163

TABLE OF STATUTES

14. The Unfair Contract Terms Act 1977

15. The Supply of Goods & Services Act 1982

CHAPTER ONE

THE CONCEPTUAL BACKGROUND

A. STANDARD FORM CONTRACTS

One of the most important developments in the sphere of contract during the last hundred years has been the appearance of the standard form contract, or 'contract of adhesion' as it is sometimes called.[1] Contracts are often made on standard terms prepared by one party and presented by him to the other.[2] Usually such terms are set out in a printed form, which is either the contractual document or one to which reference is made at the time of contracting.[3] Many contracts, especially 'standard-form contracts', contain exemption clauses whose purpose is to negative the terms which would normally be implied in favour of a buyer.[4]

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1 A.G. Guest, Anson's Law of Contract, 137, (1987)

2 G.H. Treitel, An Outline of The Law of Contract, 72, (1989)

3 Ibid

4 P.S Atiyah, The Sale of Goods, 205, (1990)

During the laissez-faire era of the early nineteenth century, exemption clauses were tolerated, if not actually encouraged, under the all-pervasive doctrine of freedom of contract.[5] By exclusion clause here is meant, as a general guide, any term in a contract restricting, excluding or modifying a remedy or a liability arising out of a breach of a contractual obligation.[6] In a wider sense, the term "exemption clause" is used by lawyers to denote a clause in a contract or a term in a notice which appears to exclude or restrict a liability or a legal duty that would otherwise arise.[7] The demands of the industrial revolution, gathering momentum as it did during the middle years of the last century, created mass production using the new technology that would produce limitless numbers of standard articles by standardised processes.[8] Such production methods required similarly standardised mass produced contracts and this, in turn, resulted in mass produced exclusion clauses.[9] These new contracts are referred to as being, for obvious reasons, standard form.[10]

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5 David Yates, Exclusion Clauses in Contracts, 1, (1982)

6 Ibid

7 Ibid

8 Ibid

9 Ibid

10 Ibid

The idea of an agreement freely negotiated between the parties has given way to the necessity for a uniform set of printed conditions which can be used time and time again, and for a large number of persons.[11] Each time an individual travels upon a ship, bus or train, buys a motor car, takes his clothes to the dry-cleaner, deposits his luggage in a railway cloak-room, or even, in some cases, takes the lease of a house or flat, he will receive a standard form contract, devised by the supplier, which he must either accept in toto or, theoretically, go without.[12] In fact he has little alternative but to accept; he does not negotiate, but merely adheres.[13]

A standard form contract, once its contents have been formulated by a business firm, is likely to be used in every contract concerning the same product or service with every client or customer.[14] The individuality of the parties becomes irrelevant.[15] Once the usefulness of these contracts became apparent and perfected in the transport, insurance and banking business, their use spread into all other fields of large scale business enterprise, such as national and international trade, supplies by the statutory undertakers, consumer sales and credit

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11 Supra Note 1 at 138

12 Ibid

13 Ibid

14 Supra Note 5

15 Id. at 2

agreements.[16]

Such terms are meant to govern a whole class of contracts, only the individual details being completed in each case.[17] The practise has obvious advantages.[18] In so far as the reduction of production and distribution costs which such agreements achieve is reflected in reduced prices, society as a whole may ultimately benefit from the use of standard form contracts.[19] The standard form contract is also a tool of commercial convenience. A business that deals with many customers, or suppliers, or holders of dealer franchises, does not ordinarily find it feasible either to negotiate with, or evaluate the business acumen and sincerity of, the other party to any degree.[20] Further, if the dealing is anticipated to extend over a long period, changes of personnel, company or trading policy or, indeed, the market, may make it difficult to predict how the other party is likely to behave in the future.[21] It is thus more convenient to require adhesion to a contract that commits a business, legally, to performance at a lower level than it is expected to be able to render, and to qualify promises by conditions that will

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16 Ibid

17 Supra Note 2

18 Ibid

19 Supra Note 5 at 2

20 Ibid

21 Ibid

not be insisted upon unless good business relations break down.[22] By utilising a standard form of agreement, time spent negotiating separate agreements is saved and, unless relations between the parties turn sour, their legal agreement need not be looked at again, aside perhaps from minor alterations to price or specification clauses, for many months or even, on occasion, years.[23]

In Schroeder Publishing Co. Ltd. v. Macaulay,[24] Lord Diplock analysed standard form contracts (at p. 1316) as falling either into a class of carefully negotiated commercial agreements, used to facilitate the conduct of trade, such as charter parties, insurance policies and commodity sales contracts, or into a class of consumer contracts.[25] The first group were, by and large, presumed to be fair and reasonable because of the equality of the bargaining power of the parties concerned, whereas the second were not because of the frequently near-monopolistic character of the parties putting them forward.[26]

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22 Id. at 3

23 Ibid

24 [1974] 1 W.L.R. 1308

25 Supra Note 5 at 5

26 Ibid

B. THE DIFFERENCE BETWEEN EXCLUSION CLAUSE AND LIMITATION CLAUSE

Some clauses may be in a form which purports to excuse the defendant from any liability incurred as a result of his breach; others may appear to limit or define the circumstances in which the proferens will be bound under the contract.[27] Where it is held that an exemption clause is incorporated in a contract, important and difficult questions of construction may arise.[28] for many years before the enactment of the Unfair Contract Terms Act 1977 the courts had tended to use strained methods of construction to avoid giving effect to what they regarded as unreasonably wide exemption clauses.[29]

The first case to reach the House of Lords after the passing of this Act, though it was in fact governed by the pre-Act law, was Photo Productions Ltd v Securicor Transport Ltd.[30] In this case the House of Lords made it clear that they deprecated the use of such artificial methods of construction, now that legislative methods were available for the striking down of some unreasonable exemption clauses.[31] This is a welcome development,

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27 Id. at 33

28 Supra Note 4 at 207

29 Ibid

30 [1980] A C 827

31 Supra Note 4 at 207

which should help free the law of much artificiality.[32] It eliminates the fiction of 'interpreting' clauses in ways which are almost certainly contrary to their true intent, and keeps separate the two distinct questions of, on the one hand, interpretation or construction, and on the other hand, the striking down of unfair clauses, properly interpreted.[33]

Unfortunately, since that decision, the House of Lords appears to have endorsed, in Ailsa Craig Fishing Co Ltd v Malvern Shipping Co Ltd,[34] a distinction which is likely to perpetuate these artificial modes of construction in certain cases.[35] In the Ailsa Craig case, the House appears to have distinguished between a limitation clause, and a complete exemption or exclusion clause.[36]

A limitation clause is a clause which limits the liability of a contracting party while an exclusion clause totally excludes any liability at all from arising.[37] In the case of a limitation clause, it was stressed, the clause ought to be given its natural meaning, without

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32 Ibid

33 Ibid

34 [1983] 1 All ER 101

35 Supra Note 4 at 207

36 Ibid

37 Id. at 208

straining.[38] No doubt, clear words are still necessary to protect a contracting party from the normal results of a breach of contract, but 'one must not strive to create ambiguities by strained construction...The relevant words must be given, if possible, their natural plain meaning.[39] On the other hand, 'Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion: this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives, and possibly also the opportunity of the other party to insure.'[40] The implication then is that complete exclusion clauses remain subject to stricter, and perhaps still artificial, rules of construction.[41]

This is, however, not very satisfactory for several reasons.[42] First, the distinction between a limitation clause and an exclusion clause is often just a matter of degree.[43] If a clause limits a party's liability to a trivial sum which bears no relationship at all to the amount of damage actually suffered, it is surely absurd to treat this as something wholly different from an exclusion

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38 Ibid

39 Ibid

40 Ibid

41 Ibid

42 Ibid

43 Ibid

clause.[44] Secondly, exclusion clauses and limitation clauses are often entwined together, as indeed they were in both the Photo Production case and the Ailsa Craig Case.[45] In both cases there were clauses which protected the defendants from all liability of a certain kind, and limited their liability for other kinds of loss or damage.[46] This sort of mix is quite normal with certain kinds of exclusion/limitation clauses and once again it seems absurd to distinguish between the two effects.[47] Thirdly, it must be said that if the distinction survives, it will simply complicate the law unnecessarily because counsel will be driven to argue in many cases first, whether the clause is of the one kind or the other, and secondly that different rules of construction apply in the two cases.[48]

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[44] Ibid

[45] Ibid

[46] Ibid

[47] Ibid

[48] Ibid

C. THE PROBLEMS FACED

During the past forty or fifty years consumer hostility to exemption clauses has grown, and has gone hand in hand with judicial and legislative law reform.[49] The clauses in question appear in many cases highly objectionable.[50] They are frequently drafted in the widest possible terms, and they are frequently contained in standard-form contracts which the individual member of the public apparently has no choice but to accept.[51]

We have already emphasized that in many such contracts it is a fiction to regard the detailed terms of the contract as based on agreement, even if the contract itself may be the outcome of a genuine agreement.[52] Nowhere is this more apparent than in dealing with these exemption clauses.[53] Nobody in his senses would agree to a contract which permitted the other party to commit negligence with impunity-unless, perhaps, by doing so he were to get the goods or services offered at a cheaper price.[54] Especially where a body supplying the public

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49 P.S. Atiyah, An Introduction to the Law of Contract, 209, (1989)

50 Ibid

51 Ibid

52 Ibid

53 Ibid

54 Ibid

with goods or services is able to dictate its own terms because it has an effective monopoly, the blunt truth is that the ordinary law of contractual and tortious liability can simply be set aside at the pleasure of this body.[55]

It has been widely thought that changing business and commercial practice has often rendered these exemption clauses unnecessary as a protection to the companies using them.[56] If the individual whose right of action is excluded has to bear the loss or injury himself, the burden may be a grievous one, and he is unlikely to be insured against the eventuality which has occurred.[57] Where, however, a company supplying goods or services to the public is liable for loss or damage, the company will in most cases have insured itself against these liabilities.[58]

The use of standard form contract has, however, another aspect, which has become increasingly important.[59] Standard form contracts are typically used by enterprises with strong bargaining power.[60] The weaker party, in need of goods or services, is frequently

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55 Ibid

56 Ibid

57 Ibid

58 Ibid

59 Supra Note 5 at 2

60 Ibid

not in a position to shop around for better terms, either because the supplier has a monopoly, or because all competitors use the same clause because it is embodied in a contract produced by a professional or trade association.[61] The "consumer's" contractual intention and expectation is subjected, more or less voluntarily, to terms imposed by the economically stronger party.[62] These terms may be understood only in a vague way, if at all.[63] So, standard form contracts are frequently contracts of adhesion: they are put forward on "take-it-or-leave it" terms.[64]

Another problem is that the possibility of contracts freely negotiated securing a fair market equilibrium became more of an illusion the more the economy became consumer-orientated.[65] The exclusion clause in the standard form contract became a potent weapon for the exploitation of economic power.[66] The courts and the legal system still hung on to the old ideas of freedom of contract.[67] The judges continued to support the "commercial" interest, the pure profit-interests of industry, the entrepreneur and

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61 Ibid

62 Ibid

63 Ibid

64 Ibid

65 Id. at 4

66 Ibid

67 Ibid