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Book Review: Contract Law and Contract Practice: Bridging the Gap between Legal Reasoning and Commercial Expectation, by Catherine Mitchell

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Book Review

CONTRACT LAW AND CONTRACT PRACTICE: BRIDGING THE GAP BETWEEN LEGAL REASONING AND COMMERCIAL EXPECTATION, by Catherine Mitchell[1]

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"A CONTRACT IS A PROMISE THAT THE LAW WILL ENFORCE."[2] Behind this aphorism lies the idea that a well-functioning contract law system will protect the expectations of contracting parties, ensure the advancement of economic interests, and, as a result, improve society. But, what goes into the contract and the promise? How do law and expectations interact when issues of contract interpretation and enforcement must be decided? Practitioners involved in day-to-day commercial practice will agree that there are often differences between the law applicable to a contract and the actual conduct and expectations of contracting parties.

Catherine Mitchell's well-researched book *Contract Law and Contract Practice: Bridging the Gap between Legal Reasoning and Commercial Expectation* considers the friction between the classical legal approach to contract interpretation and

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1. (Oxford, UK: Hart Publishing, 2013) 288 pages.
2. Among the prominent sources for this maxim, see *e.g.* Samuel Williston, *The Law of Contracts* (New York: Baker, Voorhis & Co, 1924) vol 1 ("A contract is a promise, or set of promises, to which the law attaches legal obligation" at 1).

an approach that emphasizes the contextual facts that surround and imbue the contractual relationship. Mitchell argues for an adaptable approach, founded in relational contract law, that leads to more just and complete results and that, in doing so, upholds and enhances the relevance of commercial contract law to business.[3] This method requires the courts to refrain from beginning their analysis "with a particular conception of the law of contract … [that] largely determines their conclusions"[4] and to consider the norms of the contractual relationship:

> The point of relational contract law is to achieve some overall sense of how *the parties* understood their agreement. … What relational theory demands is sensitivity to a range of contracting circumstances and a denial of the traditional binary lines along which debates are often drawn. Pragmatism, context and flexibility are the hallmarks of a relational approach to contractual agreements.[5]

Mitchell describes three avenues of legal reasoning in contract interpretation. The formalistic, classical method is text-based—"a literal or plain meaning method to understanding the words of the contract," which are assumed to form a relatively complete and "supreme statement of the parties' obligations."[6] This method is contrasted with a neoclassical approach, which "would differ in that it might permit enquiries outside the documents to decide what the parties meant by the words they have used, although this might achieve the same result as [the] literal method."[7] Finally, there is a fully contextual approach, which "would not

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3. *Supra* note 1 ("There will be costs involved in developing a relational contract law, but the institutional costs in not developing it, particularly in terms of our confidence in contract law's capacity to facilitate commercial dealing and commercial expectations in all their forms, are likely to be greater" at 266).
4. *Ibid*.
5. *Ibid* at 265-66 [emphasis in the original].
6. *Ibid* at 10. Classicism has a cousin in literary theory. The "New Criticism" posits that the text alone is the proper focus of literary analysis. Other information related to the text—its epoch, the author's biography and intention, genre—is irrelevant. For a more in-depth description of the New Criticism, see MH Abrams, *A Glossary of Literary Terms,* 7th ed (Boston, Mass: Heinle & Heinle, 1999) at 180 (describing the New Criticism as "insisting that the proper concern of literary criticism is not with the external circumstances or effects or historical position of a work, but with a detailed consideration of the work itself as an independent entity"). See also WK Wimsatt, Jr & MC Beardsley, "The Intentional Fallacy" (1946) 54:3 Sewanee Rev 468 (claiming "the design or intention of the author is neither available nor desirable as a standard for judging the success of a work of literary art… " at 468).
7. *Ibid* at 10-11.

begin the interpretative task by attention to the documents at all, but would examine other aspects of the contractual relationship."[8]

Examples of these contrasting approaches are found throughout case law and in commercial dealings, for example when: (i) legal principles (*e.g.*, four corners of the contract and entire agreement clauses) clash with equitable principles (*e.g.*, promissory estoppel, implied terms, rectification, restitution, laches, and acquiescence);[9] (ii) one party who "dots all I's and crosses all T's" is at odds with another who "begs forgiveness"; (iii) the objective stands against the subjective;[10] (iv) one party wants to fit the facts to the rules instead of finding intent through the facts and enforcing it; and (v) the real social world and trust oppose the artifice of the legal world and legislation.[11] Without oversimplifying or overstating the matter, these examples are behavioural representations of philosophical poles within the law. The courts, the jurisprudence, and legislative reactions to commercial issues cannot help but reflect these tensions, since these tensions play out in the human psyche and in human relationships. The struggle between self-interest and cooperation, or to use Duncan Kennedy's terminology, individualism and altruism,[12] is fundamental to much legal theorizing.

Mitchell does not, however, seek to frame the contending approaches to contract law as a set of pure dichotomies that can be broadly labelled as

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8. *Ibid* at 11 (adding, "The use of contextualism in such a method may reveal that the written documents were not that important to the parties at all and may be manifestly unreliable as a statement of their understandings about their agreement").
9. See also *ibid* at 15 ("it is clear to anyone with more than a cursory appreciation of the law that the rigid classical model of contract law has been undermined in many different ways and that contract law is not completely isolated from commercial expectations and practices").
10. See generally Grant Gilmore, *The Death of Contract* (Columbus: Ohio State University Press, 1974) (noting, "Holmes and his successors substituted an 'objectivist' approach to the theory of contract for the 'subjectivist' approach…" at 35 [citation omitted]).
11. See Mitchell, *supra* note 1 at 256 (arguing "[t]he disposition of the *Total* case appears precisely to rely upon a juxtaposition between the social and the legal; between the real world and the legal world; between 'documents' and 'understandings', completely overlooking that there was a way to make these two 'worlds' consistent"). See *Total Gas Marketing v Arco British,* [1998] UKHL 22.
12. "Form and Substance in Private Law Adjudication" (1976) 89:8 Harv L Rev 1685 at 1685. Kennedy states:

> there are two opposed rhetorical modes for dealing with substantive issues, which I will call individualism and altruism. There are also two opposed modes for dealing with questions of the form in which legal solutions to the substantive problems should be cast. One formal mode favors the use of clearly defined, highly administrable, general rules; the other supports the use of equitable standards producing ad hoc decisions with relatively little precedential value.

contextualist or formalist. She does not start with the assumption that there is in fact a misalignment between law and commercial expectations. But she does end with that conclusion. To reach this conclusion of misalignment, Mitchell first examines the nature of commercial expectations, noting that there is no single denotative or connotative meaning to that term. What does commercial expectation mean and how does it differ from existing contract law concepts? How does an expectation become relevant in general terms as opposed to transaction- or dispute-specific evidentiary terms? Any attempt to assign meaning must take into account commercial values, and these values are themselves multilayered[13] expectations capable of being "derived from different starting points."[14]

While values inform any attempt to define commercial expectations, other factors that can underlie expectations must also be considered, including commercial practice standards—"recurring pattern[s] of behaviour"[15] between parties or within a particular industrial context. In fact, identifiable standards "may mean more to the parties than the finer points of classical contractual theory"[16] and, therefore, may reduce the impact of classical legal reasoning on commercial arrangements. Business cooperation is another factor: the relationship between the values immanent in commercial law[17] and the "reluctance of the law to embrace an overriding concept of good faith."[18] Commercial expectation is also shaped by the way that changing economics have led to the use of networks, master or umbrella agreements, and letters of intent. In short, commercial expectation is not a static concept. Taking those definitional challenges into

13. Mitchell, *supra* note 1 at 28 [citation omitted] ("Broadly speaking, an expectation ... might be grounded in one's experience (empirically based), … grounded on some normative commitment thought valuable, or … derived from or protected by some social institution").
14. *Ibid.*
15. *Ibid* at 30.
16. *Ibid* at 33, citing JH Baker, "From Sanctity of Contract to Reasonable Expectation" (1979) 32:1 Current Leg Probs 17 at 23.
17. See generally *ibid* at 39, n 29, citing Roy Goode, "The Codification of Commercial Law" (1988) 14:3 Monash UL Rev 135 at 148 (arguing there are "eight principles which together make up the philosophy of commercial law": party autonomy, predictability, flexibility, good faith, the encouragement of self-help, the facilitation of security interests, the protection of vested interests, and the protection of innocent third parties).
18. Mitchell, *supra* note 1 at 42. Mitchell's book was published prior to the Supreme Court of Canada's ruling in *Bhasin v Hrynew*, which recognized a general duty of honest performance. See *Bhasin v Hyrnew*, 2014 SCC 71 at para 92, Cromwell J (CanLII) (concluding "that at this point in the development of Canadian common law, adding a general duty of honest contractual performance is an appropriate incremental step, recognizing that the implications of the broader, organizing principle of good faith must be allowed to evolve according to the same incremental judicial approach").

consideration, Mitchell concludes that there is, at first blush, an argument that contract law should, in some way, "consider its degree of alignment with the norms, practices and implicit dimensions that lie outside the express contract terms and also outside the rules and principles of contract law."[19]

Is there in fact a misalignment between contract law and what the business community does and expects? In addressing this question, Mitchell discusses a number of empirical studies that support this conclusion. These studies show that parties to contracts place more value on "normative and institutional structures, such as trust, reasonable expectations and informal sanctioning" than on the written word when entering into contracts and assessing the performance of obligations by one another.[20] Conversely, Mitchell notes that other empirical studies have been used to support the opposite position.[21] While there is acknowledgement that "all contracts are socially embedded," the degree of importance of actual conduct when developing and applying rules of contract law is debatable.[22] Mitchell concludes that "[d]isagreement centres over whether norms constituting the 'real deal' exist, how they are to be identified, what justifies their use and the circumstances in which legal recognition and enforcement of these is appropriate."[23]

With appropriate caution, empirical studies can be used as sources of information about expectations and practices and to see "whether it is possible to make any generalisations from the findings concerning the design of contract law rules and legal reform."[24] Trade associations that develop standard forms and processes are arguably more influential than the applicable law in defining how business is done, particularly where commerce is impaired or hindered by "competing and inconsistent 'customary' understandings… ."[25] Some critics

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19. *Ibid* at 63.
20. *Ibid* at 1. Mitchell notes that empirical studies of contracting behaviour have shown that the acceptance of norms in the commercial context is based more on relationship and industry than on legal principles (*ibid* at 64-68).
21. *Ibid* at 65 ("empirical studies have been used to support two opposing lines of argument concerning the design of contract law rules").
22. *Ibid* at 2.
23. *Ibid*.
24. *Ibid* at 68.
25. *Ibid* at 80 ("Here it is traders themselves, rather than lawyers, that have created bodies of functioning rules in order to facilitate trade and resolve problems of co-ordination, security and certainty"). Mitchell cites Art 9 of the *United Nations Convention on Contracts for the International Sale of Goods* (*ibid* at 76-77, n 47). One can also consider the international derivative and swap master agreement model for use in the over-the-counter derivatives industry. See International Swaps and Derivatives Association (ISDA), *2002 Master Agreement*.

dispute the very existence of trade customs and oppose the consideration of relational details in the legal reasoning process, citing a lack of normative universality, a lessening of trust between contracting parties, and the cost of enforcement where disputes arise over what is or is not a properly normative consideration.[26]

Mitchell rejects the idea that relational considerations inherently dilute the leadership role that the law can take: "The essence of legality is not just in imposing sanctions but in channelling behaviour."[27] In fact, the law already engages in an internal dialogue between the relational and the classical in those instances where it takes a standards-based approach to recognize and protect expectations of contracting parties under the guise of equity-based principles. So, classic contract law may already possess the internal flexibility to "stay connected to commercial expectations."[28] Whether this is so is a question of the degree to which the law can examine trade practices, implied terms, and understandings to achieve a just result that accords with contracting parties' expectations: "For every commercial contract case that displays some appreciation of the informal norms and expectations that surround the legal agreement, there are counter-examples that display a more attenuated commitment to recognising and enforcing the 'real deal.'"[29]

Mitchell outlines some examples in which the courts have considered evidence of parties' expectations that are external to the written contract terms.[30] The justifications for a strict application of written terms (*e.g.*, evidentiary, imposition of external order, hindering effect on uncertain claims regarding obligations and performance) are contrasted with instances where courts make decisions that appear to contradict the written word, "motivated seemingly by equitable considerations of fairness and balance."[31] Mitchell concludes that the law's requirement for certainty is not always commensurate with the parties' relationship, the subject matter of the contract, external requirements, and other factors, so flexible terms may be written in an express fashion (*e.g.*, the requirement to behave "reasonably") to achieve an outcome that may not be

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26. Mitchell, *supra* note 1 at 82, nn 76-77, citing Lisa Bernstein, "Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms" (1996) 144:5 U Pa L Rev 1765 at 1768; Lisa Bernstein, "The Questionable Empirical Basis of Article 2's Incorporation Strategy: A Preliminary Study" (1999) 66:3 U Chicago L Rev 710.
27. *Ibid* at 86.
28. *Ibid* at 100.
29. *Ibid.*
30. *Ibid* at 100-137 (observing that "the interpretation of the contract within the law does not involve interpreting the *contractual agreement,* but the *contract text*" at 104 [emphasis in the original]).
31. *Ibid* at 107.

known or capable of clear definition.[32] In some cases, themes emerge in the case law whereby the legal framework adapts to contractual performance, rather than the other way around.

Mitchell also contemplates whether or not there is support for narrowing the gap between law and commercial expectation based on efficiency or incentivization and rights-based or promissory contract law theories, "the two dominant accounts of the underpinning justification for contract law."[33] Mitchell does not express a preference for one theory or the other per se; while either approach can arguably be applied to close the gap between law and commercial expectation, neither can be conclusively favoured. Given the importance of actions and performance to commercial parties,[34] Mitchell concludes that relational theory might be the best approach. Promissory theory has its weaknesses, but it does have the larger goal in mind that what the parties understood about their deal is what should be enforced. Efficiency theory has its problems as well, including enforcement costs, the challenge of determining terms when attempting to take account of the parties' expectations, and the possibility of excessive reliance on wealth maximization at the expense of contextual factors.

The conclusion is that in those instances where the law subsumes the "individualism and dynamism" of relational contract theory, the arguments against contextualization based on unpredictability, particularization, and discord with perceived values of commercial law melt away.[35] The contextual approach itself addresses those problems. Mitchell argues,

> The main benefit of a relational and commercial-expectations approach to contract law is that it seeks to draw out and apply the internally generated norms of the business relationship to questions concerning the scope of contractual obligations or dispute resolution. This is preferable to an approach which champions a set of external standards whose assumptions and expectations are a poor fit with the actual practice that the law is supposed to regulate and facilitate. In this respect the contextual factors that may be examined as part of the legal reasoning process will be

32. *Ibid* at 136-37.
33. *Ibid* at 138-39.
34. *Ibid* at 169 (adding that "[f]or these contractors it is performance of obligations that is sought and that is an indicator of reputation, not ability to satisfy court judgments through the payment of damages").
35. *Ibid* at 264.

> familiar to the parties because they constitute and inform the environment in which they make and perform their agreement.[36]

The relational approach stabilizes the legal system when the courts grant "remedies for breach that mesh consistently with the context of the parties' agreement, its aims and purposes."[37] While there are different ways to establish relational theory within legal reasoning, Mitchell concludes that this is not new ground in contract law and that placing more emphasis on it "may offer better support for the parties' commercial expectations than alternatives."[38] But the courts generally apply a contract law that is "adversarial and competitive … evinc[ing] a preference for the contract text as the main source of evidence about obligations."[39]

Mitchell examines how relational theory "might yield a theory about legal reasoning in commercial contracts that is more sensitive to commercial expectations"[40] and "stresses the importance of the social embeddedness, or social context, of all exchange behavior."[41] As she succinctly puts it,

> A better supporting theory for the commercial-expectations approach would be one that places central importance on the idea that commercial contract law should, where appropriate, track the norms and behaviours of actual contracting parties. Such an alternative is presented by the relational theory of contract.[42]

This is Mitchell's preferred approach.[43] Contextualizing builds a platform that makes legal reasoning more attentive to commercial reality and takes it away

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36. *Ibid*. Mitchell adds,

> Such a law can be castigated as unpredictable and ad hoc, but to the extent that its hallmark is close attention to context, its method is entirely predictable and from this starting point outcomes may be broadly predictable also. The indeterminacy simply reflects the complexity of the phenomenon that is subject to the legal controls (*ibid*).

37. *Ibid*.
38. *Ibid*. Mitchell adds, "The law already demonstrates considerable capacity to take an individualistic approach to contract dispute resolution. Commercial courts pride themselves, rightly or wrongly, on being able to reach outcomes which either reflect specific commercial practices, or are motivated by business common sense" (*ibid*).
39. *Ibid* at 265.
40. *Ibid* at 171.
41. *Ibid.*
42. *Ibid.*
43. Mitchell extensively discusses the work of Ian Macneil in chapter six. Macneil's relational theory is "rooted in an understanding of contract as essentially a social as opposed to an exclusively legal or economic phenomenon, although 'social' naturally incorporates these two perspectives" (*ibid* at 172). See *e.g.* Ian Macneil, *The Relational Theory of Contract: Selected Works of Ian Macneil*, ed by David Campbell (London: Sweet & Maxwell, 2001).

from classical law's characterization of contracting parties as "atomistic, rational, self-interested individuals of roughly equal bargaining power who agree on contract terms and then commence performance."[44] Relational theory analyzes contracts within "the wider span of social relationships in which transactions take place."[45] In the absence of this broader context, a strictly legal focus on the relationship will not lead to the just and complete result between parties.

The relational approach is not without its challenges. But it starts with context, rather than express terms. Moreover, there are some universal norms, such as reciprocity.[46] Mitchell concludes that

> the central insights of relational theory—that context is important, that indeterminacy in contract circumstances is rife, that classical law is manifestly unsuitable for some forms of contractual relationship—support the idea that commercial contract law should reflect commercial practice, since the theory demands that a range of considerations, not any single value, be factored into any analysis of exchange relationships.[47]

The tendency within the law to emphasize formalism and objectivity can be an impediment; this may be a result of the rules having their origin in litigation. Mitchell queries "whether an adversarial dispute resolution process, beset by criticism relating to time and costs, can ever be a suitable forum within which to discover, let alone implement, the parties' (non-contractual) commercial expectations."[48] If relational factors are assumed *ab initio* to be external to the contract, how do those factors penetrate the barrier and become evidence to be considered equally with the written document (or perhaps as even more important than it)? In Mitchell's view, while there may be a preference among litigants for formalism, the law needs to be "a facilitative institution, [and] any perceived incapacity on the part of the law to become more relationally constituted should be a cause for concern."[49] In her view, there is reason to be optimistic. As she notes,

> While the limitations and context of the litigation process provide some barriers to the development of a contract law more aligned with commercial expectations, this does at least suggest that it is litigation processes and case management that prevents development of a relationally constituted contract law, not anything internally related to the law of contract itself.[50]

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44. Mitchell, *supra* note 1 at 173.
45. *Ibid*.
46. *Ibid* at 193.
47. *Ibid* at 199.
48. *Ibid* at 235.
49. *Ibid* at 236.
50. *Ibid*.

Catherine Mitchell's stated goal in *Contract Law and Contract Practice: Bridging the Gap between Legal Reasoning and Commercial Expectation* is to "fill a gap in contract law scholarship and to contribute to understanding the relationship between contract law and commercial contracting practice … that appears inadequately covered in the literature concerning the existence of the 'real deal' and its effect in the 'non-use' of contract law."[51] It must be noted that the book has a British focus, but this does not diminish its utility in the Canadian setting. I recommend the book to anyone who negotiates, administers, or litigates commercial contracts from formation to performance to termination. Commercial lawyers will find that this book illuminates many of the inchoate, intuitive conclusions that they have reached after time spent in day-to-day practice. All of us should endeavor to think broadly about the nature and purpose of commercial contracts and their components. Mitchell's book forms a welcome addition to the canon.

51. *Ibid* at 7.