Mistaken Assumptions in Equity: Sound Doctrine or Chimera?

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MISTAKEN ASSUMPTIONS IN EQUITY:
SOUND DOCTRINE OR CHIMERA?

John D. McCamus*

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I. INTRODUCTION

The law of mistaken assumptions enables courts to treat as unenforceable agreements that have been entered into on the basis of erroneous assumptions concerning the context of the agreement in question where enforcement of the agreement would inflict an injustice on one of the parties. The law of mistaken assumptions is to be distinguished from cases of misunderstanding where the parties have failed to reach an adequate *consensus ad idem*. The

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1. Although various terms are used by different writers to refer to the various categories of mistake that may affect a transaction, there is a broad consensus that there exists a basic division between mistakes that prevent formation of the agreement,
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A classic illustration of misunderstanding is *Raffles v. Wichelhaus*, in which the parties contracted to buy and sell 125 bales of cotton on board the ship "Peerless". Unfortunately, the parties had different ships "Peerless" in mind. As a result, no *consensus ad idem* had been reached and the agreement was not enforceable. In a mistaken assumptions case, on the other hand, the parties reach agreement on the terms of their contract but share an error with respect to some important contextual circumstance. The parties might not appreciate, for example, that goods that are the subject-matter of a sale had been destroyed by fire prior to the entering into of the agreement. In determining whether an agreement should be considered unenforceable by reason of the mistaken assumption that infects its creation, courts must engage in a delicate exercise of balancing the competing values of contractual stability and the provision of relief in cases of severe injustice.

Students of contract well know that the leading English decisions in the law of mistaken assumptions are the 1932 decision of the House of Lords in *Bell v. Lever Brothers* and the 1949 decision in the Court of Appeal in *Solle v. Butcher*. In the latter case, Denning L.J. famously sought to confine the common law doctrine of mistaken assumptions articulated in *Bell v. Lever Brothers*, which rendered agreements void on the basis of mistaken assumptions, and supplement it, or, indeed, to some extent supplant it by an equitable doctrine of mistaken assumptions which would render agreements voidable on the same or similar grounds. For admirers of Lord Denning, this is one of his more attractive and successful contributions to the evolution of contracts jurisprudence. For his detractors, this was perhaps yet another typical exercise in historical

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revisionism and inappropriately muscular reform of the private law of obligations.

In Great Peace Shipping Ltd. v. Tsavliris Salvage (International) Ltd., the English Court of Appeal was afforded an opportunity to reconsider mistaken assumptions doctrine more generally and, in particular, the tension between Bell v. Lever Brothers and Solle v. Butcher. As will be seen, the Court of Appeal in this case decided to reject what some would consider to be the improvements to the doctrine effected by Solle v. Butcher and to restore the doctrine to that envisaged by Lord Atkin in Bell v. Lever Brothers. It will be argued here that this is a most unfortunate development and one that ought not be followed by Canadian courts. In order to support this thesis, it will be necessary to consider briefly the history of common mistaken assumptions doctrine in English law and it will be helpful, in my view, to provide a brief account of American law on this topic before turning to a more detailed account of and critique of the decision in The Great Peace.

II. MISTAKEN ASSUMPTIONS AT COMMON LAW

As we shall see, much controversy surrounds the common law doctrine rendering contracts void on the basis that the agreement in question has been entered into by the parties on the basis of a common and mistaken assumption concerning a material fact. Nonetheless, it is clear that relief in this form is available in two classes of cases. The first, referred to as res extincta, holds agreements for the sale of goods void in circumstances where the parties are unaware that the goods had ceased to exist at the time of contracting. The most frequently cited illustration of this proposition is Couturier v. Hastie, a case holding void a contract for the sale of a cargo of corn which, unbeknownst to the parties, had ceased to exist at the time of contracting. This common law doctrine was enshrined by Sir MacKenzie Chalmers in the English sale of goods legislation. Relief would not be available, however, if the seller had explicitly or implicitly warranted the existence of the

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goods. The second category, cases of *res sua*, are those in which a purchaser later discovers that at the time of contracting he or she already owned the subject-matter of the sale. Such agreements are also void at common law. Interestingly, the authority most frequently cited for this proposition is in fact a decision of a court of equity. In *Cooper v. Phibbs*, a lease of a fishery was set aside on the ground that the lessee, at the time of entering the lease, was already entitled to an equitable life estate in the property. As we shall see, the precise significance to be attached to the equitable nature of this authority has been a matter of some controversy. Nonetheless, it appears to be well accepted that, in a case of *res sua*, the contract is void at common law.

Beyond these two categories, the scope of the common law doctrine has been, and indeed remains, rather unclear. Certainly, however, common law courts have held agreements void in a range of circumstances beyond those of *res extincta* and *res sua*. The difficulty lies, however, in articulating the basis on which other types of circumstances will ground a holding that the agreement is void for mistake. The various versions of the requirements articulating the test for operative mistake may be characterized as being either narrow or broad. Though the narrow versions of the test appear more restrictive or difficult to apply than the broader and seemingly more flexible versions, it may well be that the precise nature of the test will not be dispositive of the outcomes in particular cases. The narrow conception of the common law doctrine is applicable only where, by way of extension of the doctrine of *res extincta*, it can be said that the “subject-matter” of the agreement “ceases to exist” because of a mistake. In *Strickland v. Turner*, for example, it was held that the purchase of an annuity where the annuitant was in fact already dead at the time of sale was void. This result can be explained on the basis that the subject-matter of the agreement — an annuity on the life of a living person — had ceased to exist at the time of contracting.

A similar explanation can be offered for *Scott v. Coulson*, a case in which the sale of a life insurance policy on the life of one A.T. Death was held void when it was discovered that, by the time of contracting, Death had in fact died. The value of the policy was thus

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9. (1867), L.R. 2 H.L. 149.
10. (1852), 7 Ex. 208, 155 E.R. 919.
11. [1903] 2 Ch. 249 (C.A.).
very different from what the parties had initially assumed. If one defines the subject-matter of the agreement to be “a life insurance policy on the life of a living person”, the agreement could be held void on the basis that that subject-matter did not exist at the time of contract. Similarly, in the colourful and much taught American case of Sherwood v. Walker, the sale of a cow, Rose 2d of Abalone, which, although assumed by the parties to be barren, was with calf at the time of contracting, could be held to be void on the basis that the subject-matter of the agreement, a barren cow, did not exist at the time of entering the agreement. In reply, of course, it would be argued that the subject-matter of the contract is a cow or, indeed, Rose 2d herself. As these decisions illustrate, the “non-existence of the subject-matter” test is a highly manipulable one. One can artfully characterize the subject-matter of the contract in such a way as to either deny relief or make it available. The test thus offers little guidance as to when the common law doctrine will apply.

Other judges tend to articulate a broader test in terms that stress the “basic” or “fundamental” nature of the mistake in question. Thus, in Scott v. Coulson itself, Vaughan Williams L.J. explained the result on the basis that

both parties entered into this contract upon the basis of a common affirmative belief that the assured was alive; but as it turned out that this was a common mistake, the contract was one which cannot be enforced. This is so at law . . . if the basis which both parties recognised as the basis is not true.14

Romer L.J. reasoned that the defendant

must be taken to have known that the basis upon which the contract had been entered into, and the common belief upon which both parties had acted, did not exist. That was a circumstance which went to the root of the matter, and rendered it improper to insist upon the completion of the contract.15

Although Romer L.J.’s reference to the fact that the basis for the agreement did not exist shows traces of the non-existence of the subject-matter test, the emphasis placed on the mistake being required to be one with respect to a matter that forms the basis of the agreement appears somewhat broader than the subject-matter test.

12. Such an explanation of the result in Scott v. Coulson was offered by Greer L.J. in the Court of Appeal decision in the leading case of Bell v. Lever Brothers. See sub nom. Lever Bros Ltd. v. Bell, [1931] 1 K.B. 557 at p. 595.
15. Ibid., at p. 253.
A similar approach was taken by Blackburn J. in *Lord Kennedy v. Panama, New Zealand and Australian Royal Mail Co.*,\(^{16}\) a case involving a purchase of shares on the basis of a prospectus that falsely stated that the company had secured an attractive agreement with the government of New Zealand to provide mail services. Blackburn J. articulated the test for holding the agreement void for mistake in the following terms:

> the difficulty in every case is to determine that the mistake or misapprehension is as to the substance of the whole consideration, going, as it were, to the root of the matter, or only to some point, even though a material point, an error as to which does not effect the substance of the whole consideration.\(^ {17}\)

Applying this test to the circumstances of the case, Blackburn J. concluded that although the mistake had formed a material part of the motive for applying for the shares, the mistake did not prevent the shares from "being in substance those [the plaintiff] applied for".\(^ {18}\) These broader tests in terms of fundamental error may be supported on the basis that they are more flexible in the sense that they avoid the verbal manipulations inherent in the narrower tests. On the other hand, they may be thought to suffer from an unattractive degree of generality or vagueness.

On the basis of such authorities, then, the doctrine of mistaken assumptions at common law had obviously remained in a rather unsatisfactory state. There appears to have been no clear consensus as to the nature of the test to be applied. Moreover, the reasoning in the cases does not provide a convincing explanation for either the granting or the withholding of relief. The difference between *Strickland v. Turner* and *Lord Kennedy's* case appears to be that the purchaser in the latter case assumed the risk that the description of the company’s business in the prospectus might not be perfectly accurate, whereas the purchaser in the former case did not assume the risk that the annuity being purchased might be valueless. The one fact that appears to be common to the actual cases granting relief is that the mistaken assumption has led to a drastic miscalculation of the value being acquired by one of the parties to the agreement. However, considerations such as these, while no doubt present to the minds of the judges deciding these cases, found no explicit basis in the articulated tests for determining that

\(^{16}\) (1867), L.R. 2 Q.B. 580 (Q.B.).

\(^{17}\) *Ibid.*, at p. 588.

the contracts are void from mistake at common law. The mistake must relate to the existence "or substance" of the subject-matter of the contract or, in some sense, to a matter which is the "basis" of the agreement into which the parties have entered. Such was the unsatisfactory state of the law prior to the decision of the House of Lords in the leading case of Bell v. Lever Brothers. 19

III. BELL V. LEVER BROTHERS

In this famous case, Lever Brothers had entered into agreements to terminate the employment contracts of two senior employees in order to facilitate a proposed reorganization of the employer's corporate structure. As it was the employer's view that the employees had both provided valuable services, the arrangements reached were generous in nature. When, however, after receiving the moneys, one of the employees disclosed that they had both been trading in cocoa on their own account, Lever Brothers sought to set aside the agreements on the basis that had it been aware of the circumstance, the employees could have been dismissed for cause. At trial, the jury held that although this misconduct had not been present to the minds of the employees at the time of negotiating the agreements, Lever Brothers, on the other hand, if it had been aware of these circumstances, would have exercised its right to dismiss the employees summarily and without compensation. At trial, Wright J., as he then was, quoted with approval20 the test articulated by Blackburn J. in Lord Kennedy's case21 and held that the mistake went to the substance of the whole consideration and that the agreement was either void at common law or could be set aside in equity. In the Court of Appeal, however, both the narrow and the broader versions of the test attracted some support. Scrutton L.J. framed the test in terms of a mistake that relates to "the continuance of a particular state of things [that] is in the contemplation of both parties fundamental to the validity of the contract". 22 He suggested, however, that the application of the test could be expressed either as an implication of the term in

20. Supra, footnote 12, at p. 566.
21. Quoted in the text at footnote 17.
22. Supra, footnote 12, at p. 584.
the agreement or as the application of an "assumed foundation" test. He explained as follows:

One may describe the result as either that the contract is void because of an implied term that its validity shall depend on the existence at the time of the contract, and during its term of performance, of a particular state of facts, or (which is only another way of putting the proposition) that there is a mutual mistake of the parties, who make the contract believing that a particular foundation to it exists, which is essential to its existence, a fundamental reason for making it. In either case the absence of the assumed foundation makes the contract void.23

This suggestion that the doctrine can be formulated in the alternative form of an implied term was to be taken up by Lord Atkin in the House of Lords. The other members of the Court of Appeal flatly contradicted each other on the relevance of the non-existence of the subject-matter test. Greer L.J. conceded that “[i]t is quite true that in nearly all, if not all the cases, in which an agreement has been held void from mutual mistake, the mistake has been one as to the existence of the subject matter or its identity”.24 He went on, however, to observe that “it is not, in my judgment, the law that the only mutual mistakes that will avoid an agreement are mistakes as to the existence or identity of the subject matter of the contract”.25 For Greer L.J., the mistake must be “as to the fundamental character of the subject matter of the contract”26 or “as to some fact which affects the fundamental basis of the contract”.27 Lawrence L.J., on the other hand, offered the view that “the present case falls within that general class of cases where the subject matter of a contract has been held to be non-existent”.28 All members of the Court of Appeal were, however, satisfied that the test had been met on the present facts and that the appeal should be dismissed.

On further appeal to the House of Lords, however, the appellants enjoyed success. The leading opinion of Lord Atkin appears to adopt what might be considered a variation of the narrower version of the test. Lord Atkin began with a survey of the existing doctrine concerning cases of res extincta and res sua, characterizing the former as a “mistake as to the existence of the subject-matter”29 and the

23. Ibid., at p. 585.
24. Ibid., at p. 595.
25. Ibid.
26. Ibid.
27. Ibid., at p. 596.
28. Ibid., at p. 590.
29. Supra, footnote 1, at p. 218.
latter as "mistake as to title". In such cases, he stated, the agreement is "void" rather than "voidable". Neither category of these cases being applicable to the facts at hand, Lord Atkin went on to consider the doctrine applicable to a case where the mistake relates to the quality of the subject-matter of the agreement rather than its existence or ownership. He reasoned as follows:

Mistake as to quality of the thing contracted for raises more difficult questions. In such a case a mistake will not affect assent unless it is the mistake of both parties, and is as to the existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be.

Although this test moves away from the literal language of the "non-existence of the subject-matter" test, the movement is not dramatic. Under Lord Atkin's test, one must establish not that the subject-matter fails to exist but rather that it has become something essentially different from what it was believed to be. Like the non-existence of the subject-matter test, however, Lord Atkin's new version of the test appears to be a highly manipulable one. A pregnant cow is essentially different, one could say, from a barren cow. Indeed, as we shall see, Lord Atkin's opinion itself offers some evidence of this feature of the test.

Curiously, having apparently opted for a narrow version of the test for operative mistake, Lord Atkin then introduced a note of ambiguity in his opinion by embracing the more open-textured approach adopted in the Court of Appeal by Scrutton L.J. Like Scrutton L.J., Lord Atkin suggested that there was an "alternative mode of expressing the result of a mutual mistake". Drawing support from the now discredited implied contract theory of frustration doctrine, Lord Atkin indicated his agreement with the following proposition formulated by counsel:

Whenever it is to be inferred from the terms of a contract or its surrounding circumstances that the consensus has been reached upon the basis of a particular contractual assumption, and that assumption is not true, the contract is avoided: i.e., it is void ab initio if the assumption is of present fact and it ceases to bind if the assumption is of future fact.

In Lord Atkin's view, few would disagree with this statement, but he cautioned that care must be taken with the meaning of the terms

30. Ibid.
31. Ibid.
32. Ibid., at p. 224.
33. Ibid., at p. 225, quoting Sir John Simon.
"basis" and "contractual assumption". In determining whether a particular assumption is a condition of a contract, Lord Atkin quoted from the "important judgment of Scrutton L.J. in the present case" and found the expressions "[i]n the contemplation of both parties fundamental to the continued validity of the contract" and "a foundation essential to its existence" to be helpful. A third phrase employed by Scrutton L.J., "a fundamental reason for making it", could, in Lord Atkin's view, be "misleading", as one's motive for entering into an agreement could be mistaken in some respect without giving rise to a finding that "the new state of facts makes the contract something different in kind from a contract in the original state of facts". Moreover, such a term is not to be implied unless it was necessary to do so in order to give, in the language of the traditional test for implying terms, "business efficacy to the transaction". Oddly, then, Lord Atkin appears at one and the same time both to adopt the broader language of the test formulated by Scrutton L.J. in the Court of Appeal and, as well, to equate that test to what appears to be the narrower test of requiring the mistake to be of such nature that the contract itself is different in kind from the contract as initially contemplated.

The narrow versions of the test articulated by Lord Atkin thus appear to include the initial suggestion that the mistake is as to a "quality that makes the thing without the quality essentially different from the thing as it was believed to be", a test which appears to apply to the subject-matter of the agreement, and the later suggestion that the mistake must make the agreement itself "different in kind". It may or may not be that these versions are intended by Lord Atkin to be overlapping or indeed co-extensive. Although the two tests appear to be applied interchangeably by Lord Atkin, no guidance on this point is forthcoming. In any event, the difficulty one encounters in applying the latter version of the test is manifest in the following passage from Lord Atkin's opinion:

Is an agreement to terminate a broken contract different in kind from an agreement to terminate an unbroken contract, assuming that the breach has given the one party the right to declare the contract at an end? I feel the

34. Ibid., at p. 226.
35. Ibid.
36. Ibid. (emphasis added).
37. Ibid.
38. Ibid., at p. 218.
39. Ibid., at p. 226.
weight of the plaintiffs' contention that a contract immediately determinable is a different thing from a contract for an unexpired term, and that the difference in kind can be illustrated by the immense price of release from the longer contract as compared with the shorter. And I agree that an agreement to take an assignment of a lease for five years is not the same thing as to take an assignment of a lease for three years, still less a term for a few months. But, on the whole, I have come to the conclusion that it would be wrong to decide that an agreement to terminate a definite specified contract is void if it turns out that the agreement had already been broken and could have been terminated otherwise. The contract released is the identical contract in both cases, and the party paying for release gets exactly what he bargains for.40

One can sympathize with the sentiment that applying the "difference in kind" test to the facts of Bell v. Lever Brothers is in the nature of a tough call. Indeed, it may be that whatever test is employed to determine the scope of operative mistake, its application to the facts of Bell v. Lever Brothers will involve a difficult decision. Nonetheless, the real problem with the "difference in kind" test is not that it is difficult to apply but rather, that it does not raise for consideration the criteria or factors that appear to be relevant to the choice to be made.

The real dilemma confronted by the court in Bell v. Lever Brothers is to determine whether or not the risk of the kind of error that occurred should be considered to have been assumed by an employer in the context of negotiating a termination agreement. One could justify the result in Bell v. Lever Brothers on the basis that generally, employers negotiating such agreements should make whatever enquiries they deem fit prior to entering such an agreement and that, in the absence of fraud or other misleading conduct by the employees, employers should be considered to have taken the risk that their enquiries were inadequate. Once the agreement has been entered, the time for such enquiries has passed. As a general matter, employers are aware of the risk of such errors and one could reasonably hold that the risk of inadequate inquiry is assumed by the employer in these circumstances.

Alternatively, if so general a proposition was found unattractive by the deciding court, the result in Bell v. Lever Brothers could be justified on the basis that on the particular facts, the employer's generosity in recognizing the valuable contribution made by these particular employees led the employer effectively to waive proper enquiries and make what, in retrospect, may appear to be, in effect,

40. Ibid., at p. 223-24.
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a somewhat foolhardy gift. In such circumstances, again, the risk of error may be considered to have been assumed by the employer. In any event, the important point for present purposes is that it is considerations such as these that are plainly relevant to the making of the decision in this case. Yet they are not directly required or indeed even encouraged to be considered by the "difference in subject-matter" or "different in kind" test.

Whether one finds Lord Atkin's analysis satisfactory or not, however, it can fairly be said that his opinion is not free of ambiguity. In particular, it is not entirely clear what role Lord Atkin had in mind for a formulation of the test adverting to mistaken assumptions "fundamental to the continued validity of the contract." Greater clarity cannot be easily purchased by examining the other opinions written in this case. The panel divided three to two and can be fairly described as having reached no definitive conclusion on the precise nature of the test for operative mistake. Thus, Lord Thankerton, who concurred with Lord Atkin, found attractive the analysis offered in Lord Kennedy's case and articulated the nature of the requisite mistake as being with respect to a matter that the parties "accepted in their minds as an essential and integral element of the subject-matter [of the contract]." The third member of the majority, Lord Blanesburgh, was content to decide the case on the basis that "mutual mistake had not been pleaded." In dissent, Lord Warrington, with whom Viscount Hailsham concurred, offered a further definition of operative mistake, indicating that the error must be "of such a fundamental character as to constitute an underlying assumption without which the parties would not have made the contract they in fact made" and concluded that the actual error in Bell v. Lever Brothers "was as fundamental to the bargain as any error one can imagine."

In summary, then, it would not appear to be correct to suggest that Lord Atkin's "difference in the subject-matter" or "difference in kind" test clearly expressed the opinion of the House of Lords on this occasion. Although it is perhaps true to state that the majority appeared to share Lord Atkin's preference for a narrow test, his particular articulation of it does not appear to be plainly adopted by

41. Ibid., at p. 226.
42. Ibid., at p. 235.
43. Ibid., at p. 189.
44. Ibid., at p. 208.
45. Ibid.
either a majority of the panel or, indeed, by any other member of the panel. Apart from Lord Blanesburgh, the other members of the panel appeared to prefer a more flexible formula of the kind offered in Lord Kennedy's case by Blackburn J. Perhaps it is not surprising, then, that many editions of Anson on Contract have offered the view that "where the parties contract under a false and fundamental assumption, going to the root of the contract, and which both of them may be taken to have had in mind at the time they entered into it as the basis of their agreement, the contract may be void".46

IV. MISTAKEN ASSUMPTIONS IN EQUITY: SOLLE V. BUTCHER

In 1949, in the decision of the Court of Appeal in Solle v. Butcher,47 Denning L.J. was afforded an opportunity to consider the effect of Bell v. Lever Brothers and the role played by the mistaken assumptions doctrine in the equitable context. The opportunity was seized with apparent relish. In essence, Denning L.J. offered a restrictive interpretation of the scope of the common law mistake doctrine and suggested that a more flexible doctrine for setting aside agreements on the basis of mistaken assumptions was available in equity. Denning L.J.'s summary of the effect of Bell v. Lever Brothers was as follows:

The correct interpretation of that case, to my mind, is that, once a contract has been made, that is to say, once the parties, whatever their inmost states of mind, have to all outward appearances agreed with sufficient certainty in the same terms on the same subject-matter, then the contract is good unless and until it is set aside for failure of some condition on which the existence of the contract depends, or for fraud, or on some equitable ground. Neither party can rely on his own mistake to say it was a nullity from the beginning, no matter that it was a mistake which to his mind was fundamental, and no matter that the other party knew that he was under a mistake.48

It is evident that Denning L.J. is here giving the narrowest possible interpretation of the effect of Bell v. Lever Brothers. The only justification for so narrow a reading in the opinions in that case is to be found, of course, in Lord Atkin's suggestion that, unless the mistake makes the contract or its subject-matter different in kind from the original contract or its subject-matter, the mistake is inoperative.

47. Supra, footnote 4.
48. Ibid., at p. 691.
If, notwithstanding the mistake, the subject-matter of the contract remains the same or the kind of contract remains the same, Lord Atkin appears to suggest that the contract must be binding. Hence the arguable legitimacy of Denning L.J.'s suggestion that if the parties agree “in the same terms on the same subject-matter”, the common law doctrine is inapplicable.

Applying this test to the facts of Solle v. Butcher, the common law doctrine was, in Denning L.J.'s view, inapplicable. Solle and Butcher had collaborated on the renovation of a building owned by Butcher containing five flats. Acting on Solle's advice that the renovations were of a sufficient extent to render the rent control legislation inapplicable, Butcher rented one of the flats to Solle at a rental rate considerably in excess of that which would otherwise have been permissible under the legislation. If applicable, the legislation would have obliged Butcher to comply with the necessary statutory formalities for the increase in prior rent. After a falling out between the parties, Solle took the position that the legislation did in fact apply and that he had been charged an unlawful amount of rent under the agreement. In due course, it was held that the legislation did, in fact, apply. The parties had thus entered the lease under a common mistake as to their respective rights under the rent control legislation. Though the error was induced by Solle, the error was innocent on his part in the sense that he had received professional advice on the point before passing on this view to Butcher. For Denning L.J., common law mistake doctrine did not apply in such circumstances. Although the lease may have been entered into on the basis of a shared assumption concerning a fundamental matter, nonetheless the parties had agreed in the same terms on the same subject-matter and the lease was therefore enforceable at common law.

For Denning L.J., however, that was not the end of the matter. He then turned to “consider mistakes which render a contract voidable, that is, liable to be set aside on some equitable ground”. Controversially, Denning L.J. asserted that there existed a well-established equitable jurisdiction to set aside agreements that were enforceable at common law. Drawing support from the res sua case, Cooper v. Phibbs, Denning L.J. claimed that a court of equity

49. Ibid.
50. Ibid., at p. 692.
51. Supra, footnote 9.
could relieve for common mistake "so long as it could do so without injustice to third parties . . . whenever it was of opinion that it was unconscientious for the other party to avail themselves of the legal advantage which he had obtained". 52 Denning L.J. indicated that the notion of what would be considered "unconscientious" had developed over time and he summarized various grounds for setting aside agreements in equity, adding to this list a doctrine of equitable mistake in the following terms:

A contract is also liable in equity to be set aside if the parties were under a common misapprehension either as to facts or as to their relative and respective rights, provided that the misapprehension was fundamental and that the party seeking to set it aside was not himself at fault. 53

This doctrine was available to the tenant in the present case. Indeed, in Denning L.J.'s view, the injustice of allowing the tenant to take advantage of the mistake which he had, albeit innocently, induced was so obvious that if the rules of equity were so rigid that they could not remedy such an injustice, "it is time we had a new equity to make good the omissions of the old" but fortunately, in his view, "the established rules are amply sufficient for this case". 54

There are two particularly controversial features of this reasoning. First, it is sometimes said that Denning L.J.'s reading of the common law doctrine is unduly restrictive. 55 Second, it is sometimes argued that historically there simply was no separate definition of operative mistake in equity and that Denning L.J.'s assertion in this regard is simply false. 56 As we shall see, these criticisms of Denning L.J.'s reasoning came to preoccupy the Court of Appeal in its recent decision in The Great Peace. 57 For the moment, however, it should be noted that Denning L.J. was not reticent about his reasons for wanting to constrain or, indeed, replace common law mistake doctrine with an equitable version of the rule. In Denning L.J.'s view, the common law doctrine was unsatisfactory from a policy prospective as it created a potential for severe injustice for third parties who innocently acquired for value the subject-matter transferred

52. Solle v. Butcher, supra, footnote 4, at p. 692.
53. Ibid., at p. 693.
54. Ibid., at p. 695.
57. Supra, footnote 5.
by the initial void contract. This point was spelled out quite plainly in the following terms:

In order to see whether the lease can be avoided for this mistake it is necessary to remember that mistake is of two kinds: first, mistake which renders the contract void, that is, a nullity from the beginning, which is the kind of mistake which was dealt with by the courts of common law; and, secondly, mistake which renders the contract not void, but voidable, that is, liable to be set aside on such terms as the court thinks fit, which is the kind of mistake which was dealt with by the courts of equity. Much of the difficulty which has attended this subject has arisen because, before the fusion of law and equity, the courts of common law, in order to do justice in the case in hand, extended this doctrine of mistake beyond its proper limits and held contracts to be void which were really only voidable, a process which was capable of being attended with much injustice to third persons who bought goods or otherwise committed themselves on the faith that there was a contract.\(^5^8\)

As an illustration of the harmful effects of the common law doctrine Denning L.J. referred to *Cundy v. Lindsay*,\(^5^9\) the famous mistake of identity case, in which an innocent third-party purchaser of the subject-matter of the original sale was held liable in conversion to the original seller for its value. Equity, on the other hand, would protect the *bona fide* purchaser for value in such a case by withholding the remedy of rescission from the initial purchaser. The fusion of law and equity, in Denning L.J.'s view, made it possible to reverse this historical process of extending inappropriately the doctrines of the common law. Accordingly, at common law "only those contracts are now held void in which the mistake was such as to prevent the formation of any contract at all".\(^6^0\)

From a policy perspective, these views appear to be undeniably sound. Void for mistake is simply a bad idea and its restriction in *Solle v. Butcher* is surely a welcome development. Moreover, the constraint of void for mistake is an approach that has surfaced in other contexts. Thus, in *Saunders v. Anglia Building Society*,\(^6^1\) the House of Lords restricted the reach of the doctrine of *non est factum* by holding that one who is careless in signing a document cannot rely on that defence. Again, the concern motivating the adjustment in the doctrine is plainly that of protecting innocent third party purchasers of the subject-matter of the original agreement. The effect of confining the availability of the defence leaves the

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\(^{58}\) Supra, footnote 4, at pp. 690-91.
\(^{59}\) (1878), 3 App. Cas 459 (H.L.).
\(^{60}\) Supra, footnote 4, at p. 691.
victim of the misleading conduct to equitable rescissionary remedies, with the result that the *bona fide* third party purchaser is protected. Similarly, in the context of mistake of identity, the decision of the English Court of Appeal in *Lewis v. Averay* restricts the scope of the common law mistake of identity rule, thereby leaving the mistaken party to equitable rescissionary relief. In these contexts, as well, transactions that were originally treated as void at common law are now to be considered valid at common law but unenforceable in equity. These developments appear inescapably to represent progressive development of English mistake doctrines.

The remedy fashioned by Denning L.J. in *Solle v. Butcher* is also controversial. Purporting to rely on the flexibility in fashioning rescissionary remedies said to be manifest in *Cooper v. Phibbs*, Denning L.J. conditioned rescission on a willingness of the landlord to offer a lease for the unexpired portion of the term at the rate that could have been secured by compliance with the rent control legislation, and further, on the condition that the tenant would pay a fair and economic rent for the occupation of the premises enjoyed thus far. Bucknill L.J. agreed with the terms of the proposed order but, apart from observing that he had read Denning L.J.‘s reasons, offered no view on the nature of the relationship between common law and equitable mistake doctrine. Jenkins L.J. dissented on the ground that the mistake was one of law and that an error of this kind could not be the foundation for the right to rescind.

In assessing the significance of Denning L.J.‘s opinion in *Solle* for purposes of English and Canadian common law, then, one must examine the reception accorded to his views in subsequent English and Canadian decisions, a matter to which we will shortly turn. Before doing so, however, it will be useful to indicate briefly the limitations of Denning L.J.‘s analysis and, having done so, turn to a brief account of American law concerning common mistaken assumptions. The strength of Denning L.J.‘s opinion in *Solle v. Butcher* is its effect in restricting the scope of the common law doctrine of void for mistake and supplanting it with an equitable doctrine that affords protection to the interests of innocent third parties. Indeed, it is not obvious that Denning L.J., at least, would apply common law doctrine beyond the well established categories of *res exticta* and *res sua*, these being cases, it should be noted, in which

true owner claims against a third party do not typically arise. Non-existent goods are not likely to be resold to a third party who would, in any event, not take possession of the goods. Goods already owned by the purchaser can, of course, be successfully transferred for value to third parties.

The weakness of the opinion, however, is that it appears to offer very little guidance with respect to the test for operative mistake to be applied in equity. Beyond the suggestion that there must be a "common and fundamental misapprehension" either as to facts or as to relative and respective rights, the opinion offers virtually no guidance as to the factors to be taken into account to determine whether or not such a misapprehension is present in a particular fact situation. In order to develop a sense of the kinds of guidelines that could be articulated, it will be useful to consider briefly the American jurisprudence on these issues.

V. THE AMERICAN LAW AT A GLANCE

For a brief account of the American law on common mistaken assumptions, there can be no better source than the relevant sections of the *Restatement of Contracts, Second*. The basic rule is set out in § 152.

§152. When Mistake of Both Parties Makes a Contract Voidable

(1) Where a mistake of both parties at the time a contract was made as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances, the contract is voidable by the adversely affected party unless he bears the risk of the mistake under the rule stated in § 154.

(2) In determining whether the mistake has a material effect on the agreed exchange of performances, account is taken of any relief by way of reformation, restitution, or otherwise.

The key criteria for application of the test set out in the first subparagraph, then, are, first, that the mistake has had a "material" affect on the agreed exchange of performances and second, that the adversely affected party does not bear the risk of the error that has occurred. The suggestion that the effect of the error on the exchange need only be "material" may alarm English and, perhaps,
Canadian readers as it may be taken to suggest that relief may be available in circumstances where the error need not be in some sense “basic or fundamental”. It must be remembered, however, that “material” appears to have a significantly different meaning in American contract law than it does, say, in the Anglo-Canadian law of misrepresentation. Thus, what might be referred to in the Anglo-Canadian system as a “repudiatory breach” of contract entitling the innocent party to terminate the agreement and sue for damages is referred to in American law as a “material” breach.  

Similarly, in the context of §152, the Commentary to § 152 states:

> The mere fact that those parties are mistaken with respect to ... an assumption [with respect to an existing fact] does not, of itself, afford a reason for avoidance of the contract by the adversely affected party. Relief is only appropriate in situations where a mistake of both parties has such a material affect on the agreed exchange of performances as to upset the very basis for the contract ... . It is not enough for [the affected party] to prove that he would not have made the contract had it not been for the mistake. He must show that the resulting imbalance in the agreed exchange is so severe that he can not fairly be required to carry it out.

As § 152(1) indicates, the requirement that the adversely affected party does not bear the risk of the error in question is further explicated in § 154:

> § 154. When a Party Bears the Risk of a Mistake
> A party bears the risk of a mistake when
> (a) the risk is allocated to him by agreement of the parties, or
> (b) he is aware, at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient, or
> (c) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so.

Subsections (a) and (b), it might be said, identify situations where the affected party may reasonably be held to an understanding that the risk has been assumed. Subparagraph (c), however, is apparently intended to deal with situations where, although an inference of this kind is unwarranted, the circumstances are nonetheless such that the affected party ought to be held to have assumed the risk of error. The illustrations of this last proposition offered in the

Restatement would not alarm or, indeed, surprise an English or Canadian reader. Thus, Illustration 3 offers a variation of Scott v. Coulson and suggests that the annuitant is not dead at the time of contracting but, rather, suffers from an incurable, fatal disease. In such a case, the illustration concludes, a court would hold that the purchaser had assumed the risk of that kind of error. Other illustrations indicate that contractors will be taken to have assumed the risk that subsoil conditions are such as to render a construction contract more expensive to complete or that increased costs resulting from a contractor’s mistaken estimate of the amount of labour required increase the cost to complete a particular project.

More generally, the illustrations to these two sections of the Restatement, in my view at least, would not look unfamiliar to an English or Canadian reader. The illustrations are based on American and, to some extent, English decisions and, of course, a particular reader may or may not agree with the outcome of a particular case. Nonetheless, the more important point for present purposes — and this occasions no surprise in the context of material that has fallen from the pen, initially at least, of Allan Farnsworth — is that the test set forth in the Restatement appears to hit the nail more cleanly on the head than the kinds of tests articulated thus far in the English and Canadian cases. If one revisited the facts of Bell v. Lever Brothers under §§ 152 and 154, one would be directed to consider whether the error led to a material effect on the exchange, which is undoubtedly the case, but one would then be directed to consider what, in my view, is the critical issue in Bell v. Lever Brothers, which is whether an employer either generally or on the particular facts of this case should be taken to have assumed the risk of error resulting from what might be considered to be the inadequate investigation concerning the performance of the particular employees. As intimated above, I would suggest that the decision in Bell v. Lever Brothers can be defended on the basis that the risk of such errors was indeed assumed by Lever Brothers.

Finally, it should be noted that the Restatement and the underlying American doctrine appears to support the type of remedial

68. Ibid., at p. 405.
69. Ibid., Illustration 4.
70. Ibid., Illustration 6.
71. Farnsworth served as a Co-Reporter of the Restatement of Contracts, Second and assumed principal responsibility for chapter 6, which includes §§ 152 and 154.
flexibility asserted by the English Court of Appeal in Solle v. Butcher. Thus, Illustration 3 to § 152 reads:

A contracts to sell and B to buy a tract of land. B agrees to pay A $100,000 in cash and to assume a mortgage that C holds on the tract. Both A and B believe that the amount of the mortgage is $50,000, but in fact it is only $10,000. The contract is voidable by A, unless the court supplies a term under which B is entitled to enforce the contract if he agrees to pay an appropriate additional sum, and B does so ....

If the court of equity is restricted to either granting or withholding rescission, the unattractive result in such a case is that either the contract will be enforced as is, with resulting unjust enrichment of the purchaser B who pays 40% less than anticipated for the land, or the contract is rescinded, in which case B is unfairly deprived of the opportunity to purchase the property at the agreed price. The ability of the court to condition rescission upon the enabling of B to enforce the agreement by paying the additional $40,000 provides a solution about which neither A nor B can reasonably complain.

VI. CANADIAN AND ENGLISH RECEPTION OF SOLLE V. BUTCHER

The equitable mistake doctrine articulated by Denning L.J. in Solle v. Butcher appears to have been accepted into the fabric of Canadian contract law and, at least prior to the decision in The Great Peace, into the fabric of English law as well. Although it is true that in English law a number of the early decisions involved Lord Denning himself, the doctrine has now been applied on a number of occasions and most recently by decisions of the Court of Appeal in which Lord Denning played no part. In Grist v. Bailey, an agreement for the sale of land was set aside by Goff J., as he then was, on the basis that the parties had erroneously believed that the land was subject to an existing tenancy. Free of the tenancy, the land was worth more than double the contract price. In Magee v. Pennine Insurance Co., an agreement of compromise under which an insured paid a claim under an accident insurance policy was set aside on the ground that the parties shared an erroneous belief that the policy was valid and binding. In Laurence v. Lexcourt Holdings Ltd., a long-term lease of property for use as business premises

72. Supra, footnote 63, at p. 387.
was set aside as the parties had failed to appreciate that the zoning permitted this use of the premises only for the first two years of the term. In *Associated Japanese Bank (International) Ltd. v. Crédit du Nord S.A.*, a guarantee of a debt secured by a sale and leaseback of non-existent goods was held void at common law on the basis that the *res extincta* analogy was a close one. Steyn J., as he then was, went on to observe that “[t]oday it is clear that mistake in equity is not circumscribed by common law definitions. A contract affected by mistake in equity is not void but may be set aside on terms.” Further, Steyn J. indicated that if it was incorrect to hold the guarantee void at common law, he would have considered it to be voidable in equity. For Steyn J. “a narrow doctrine of common law mistake (as enunciated in *Bell v. Lever Bros. Ltd.*), supplemented by the more flexible doctrine of mistake in equity (as developed in *Solle v. Butcher* and later cases), seems to me to be an entirely sensible and satisfactory state of the law . . . .” Interestingly, Steyn J. further observed that before setting aside an agreement either at law or in equity, one must first consider “whether the contract itself, by express or implied condition precedent or otherwise, provides who bears the risk of the relative mistake”.  

The importance of risk allocation analysis was also emphasized by Hoffmann L.J., as he then was, in *William Sindall Plc v. Cambridgeshire County Council* in which the Court of Appeal refused to apply the equitable doctrine, which it assumed to be well established, to set aside a sale of land for development purposes where the parties had failed to appreciate the existence of a sewer running under the land. In the view of the Court of Appeal, the existence of an express term subjecting the transaction to easements precluded application of equitable mistake doctrine. Within the past few years, the existence of the doctrine has been assumed in two decisions of the English Court of Appeal and a decision at trial.

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76. *Supra*, footnote 55.  
77. *Ibid.*, at p. 266.  
79. *Ibid.*, at p. 268  
Although the list of Canadian decisions applying the equitable doctrine is not as lengthy, the correct view would be that the doctrine has been accepted as a feature of Canadian law. One of the leading cases, *Toronto Dominion Bank v. Fortin*, like *Magee v. Pennine Insurance Co.*, applies the doctrine to an agreement of compromise. In the Canadian case, the agreement of compromise was held to be voidable on the ground that the agreement was based on a common and erroneous assumption concerning the validity of the initial claim. The court distinguished, quite correctly, a decision of the Supreme Court of Canada which enforced a compromise based on a similar mistaken assumption where, however, the parties had each sought legal advice on the very issue in question. In other cases, the doctrine was held applicable to circumstances where the parties to a real estate transaction mistakenly assumed that the property was twice as large as it in fact was, where it was discovered that the monthly payments agreed upon in the context of the long-term agreement for the purchase and sale of land and chattels would never retire the balance the purchase price, and where, in the context of a real estate transaction, the parties had mistakenly believed that a dwelling house was located on the lot in question.

Prior to the decision of the English Court of Appeal in *The Great Peace*, then, to which we will now turn, one would have opined rather confidently in both England and in common law Canada that the equitable mistake doctrine articulated in *Solle v. Butcher* was a recognized feature of the law. In passing, it is of interest to note that in virtually all of these English and Canadian cases, literal performance of the contract remained possible. Thus, if one were to


attempt to apply to these cases the version of the doctrine articulated by Lord Atkin in *Bell v. Lever Brothers*, it would be necessary to manipulate the concept of the "subject-matter of the contract" in each case in order to be able to conclude that the subject-matter of the contract was different from that assumed because of mistake. Such arguments could be made, of course, with varying degrees of artificiality in these various fact situations.

**VII. THE GREAT PEACE**

In *The Great Peace*, both the trial judge and the Court of Appeal had occasion to reconsider the existence of the equitable jurisdiction to avoid agreements on the basis of mistaken assumptions articulated by Denning L.J. in *Solle v. Butcher*. The trial judge, Toulson J., reached the "bold conclusion" that the views expressed by Denning L.J. in *Solle* were incorrect. In Toulson J.'s view, equity simply did not possess a jurisdiction to set aside agreements on such grounds. The Court of Appeal agreed with these views and concluded that the equitable jurisdiction invoked by Denning L.J. and by subsequent English courts was a mere "chimera". The lengthy reasons offered by the Court of Appeal for this conclusion offered a detailed analysis of the history of mistaken assumptions doctrine, placing considerable emphasis on a detailed dissection of the reasoning in *Bell v. Lever Brothers* and *Solle v. Butcher* itself. After briefly describing the reasons provided for the Court of Appeal by Lord Phillips M.R., a critique of the decision and its implications for English law will be offered.

The facts of the case are uncomplicated. En route from Brazil to China, a vessel, The Cape Providence, suffered serious structural damage with consequent risk to both the vessel and its crew. The defendant salvor was retained to provide assistance. The defendant sought assistance from a third party, Marint, in locating a tug. When it appeared that the tug would only be available in five or six days, Marint was asked to try to locate another vessel in the vicinity of The Cape Providence that might be prepared to offer assistance with the evacuation of the crew, should that become necessary. Marint advised that The Great Peace, a vessel owned by the plaintiffs, was the vessel closest to the current location of The Cape Providence and

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that it should be able to rendezvous with The Cape Providence in about 12 hours. Acting on the instructions of The Cape Providence, the defendant commenced negotiations with the plaintiff for suitable arrangements by which The Great Peace would alter its course and proceed to the location of The Cape Providence. Within a few hours, such arrangements were reached and The Great Peace altered its course. The arrangements included a term permitting the defendant to cancel the agreement on payment of a minimum five-day fee.

Within a few hours, it became apparent that The Great Peace was actually 410 miles, rather than the initially estimated 35 miles, away from The Cape Providence. At this point, the defendants advised Marint that they were expecting to cancel The Great Peace but would not do so yet, as they wished to determine whether a closer vessel could be identified. Shortly thereafter, having learned that The Cape Providence had been passed by a vessel called the Nordfarer, the defendants contracted with the owners of the Nordfarer for similar assistance and instructed Marint to cancel the arrangements with the plaintiffs. Marint then confirmed the cancellation and indicated that it would recommend, in the circumstances, the payment of a lesser cancellation fee of two days’ hire. The defendants were unwilling, however, to pay any sum at all to the plaintiff with respect to the cancellation of the agreement.

In response to the plaintiff’s claim for the five-day cancellation fee payable under the agreement, the defendants argued, both at trial and in the Court of Appeal, that the agreement had been entered into on the basis of a shared fundamental assumption that The Great Peace was “in close proximity”92 to The Cape Providence whereas, in fact, she was not. Accordingly, the agreement was either void at common law or, at least, voidable in equity and subject to rescission. These defences were rejected both at trial and on appeal and the claim enjoyed success. On behalf of the Court of Appeal, Lord Phillips M.R. began his reasons with a careful examination of the reasoning at all levels in Bell v. Lever Brothers. Lord Phillips quoted at particular length from the opinion of Lord Atkin, which he considered to represent a consensus of the majority of the panel. Lord Phillips observed that the matter had been considered both at common law and in equity at trial and further, that Lord Atkin had indicated that the result in Cooper v. Phibbs,93 the principal

92. Ibid., at p. 696.
93. Supra, footnote 9.
authority upon which Denning L.J. had relied upon as evidence of the existence of an equitable jurisdiction, should have been that the agreement was void at common law rather than voidable in equity. Accordingly, Lord Phillips suggested that Denning L.J.'s conclusion in Solle v. Butcher that the House of Lords in Bell v. Lever Brothers had simply not considered the possible application of an independent equitable jurisdiction to relieve for mistake was simply "not realistic".94

With particular reference to Denning L.J.'s reliance on Cooper v. Phibbs, Lord Phillips accepted the view advanced by Matthews95 that it might well have been a case in which a contract valid at common law was rescinded in equity for mistake.96 The plaintiff's perceived need to resort to equity may have rested on the ground that the plaintiff's life estate was equitable in nature and might well not have been recognized by a court of common law. Nonetheless, the type of mistake that the court appeared to recognize in Cooper v. Phibbs as providing a basis for rescission was an instance of res sua in which a party agrees to purchase a title that he already owns. The court was merely applying the common law doctrine of res sua to the purchase of an equitable interest. The width of the jurisdiction in equity would not therefore appear to be remarkable. Further, Lord Phillips quoted passages from the opinions in Norwich Union Fire Insurance Society Ltd. v. Wm. H. Price Ltd.97 in support of the proposition that in Bell v. Lever Brothers, the House of Lords had equated "the test of common mistake in Cooper v. Phibbs with one that renders a contract void at common law".98 Accordingly, it was simply "not correct to state that Cooper v. Phibbs as interpreted by Denning L.J. was 'in no way impaired by Bell v. Lever Bros Ltd.' or that it had been 'fully restored' by Norwich Union".99

Lord Phillips then turned to consider the various subsequent decisions of the lower courts and of the Court of Appeal which purported to follow and apply Solle v. Butcher. The collective support offered by those authorities for the notion that the doctrine of Solle v. Butcher had become a recognized proposition of English law was undermined by Lord Phillips on three grounds. First, on a

94. Supra, footnote 5, at p. 722.
96. Supra, footnote 5, at pp. 715-18.
98. Supra footnote 5, at p. 723.
99. Ibid., at p. 722.
careful parsing of the decisions, it was his view that these cases do not “define satisfactorily different qualities of mistake, one operating in law and one in equity”. The subsequent cases “have merely emphasized the confusion of this area of our jurisprudence”. Further, Lord Phillips observed, “If coherence is to be restored to this area of our law, it can only be by declaring that there is no jurisdiction to grant rescission of a contract on the ground of common mistake where the contract is valid and enforceable on ordinary principles of contract law.”

Second, Lord Phillips appeared to offer some scepticism with respect to the appropriateness of the results in at least some of the subsequent cases. There was, in his view, a common factor in Solle v. Butcher and in the later cases in that the “effect of the mistake has been to make a contract a particularly bad bargain for one of the parties”. Lord Phillips appeared sceptical as to whether equity had adopted a principle which would enable equitable rescission in circumstances where the common law has produced this result. Indeed, it appears to have been his view that an equitable doctrine correcting the common law in this respect would be an inappropriate exercise of the historical jurisdiction of equity. The proper scope of equity is merely to “supplement or mitigate” the common law. The inappropriate effect of Solle v. Butcher was to say that Bell v. Lever Brothers was wrongly decided.

Third, it was his view that the difficulties with Solle v. Butcher had not been fully canvassed in the decisions that appear to accept its legitimacy. He concluded as follows:

In this case we have heard full argument, which has provided what we believe has been the first opportunity in this court for a full and mature consideration of the relation between Bell v. Lever Bros Ltd and Solle v. Butcher. In the light of that consideration we can see no way that Solle v. Butcher can stand with Bell v. Lever Bros Ltd. In these circumstances we can see no option but to so hold.

In the view of Lord Phillips, the fact that the Court of Appeal had itself purported to apply the doctrine on previous occasions did not preclude a holding to this effect.

100. Ibid., at p. 728.
101. Ibid., at p. 729.
102. Ibid., at p. 729.
103. Ibid., at p. 728.
104. Ibid., at p. 729.
105. Ibid., at p. 730.
If the equitable doctrine is thus dispatched, it must be asked what version of the common law doctrine would, in the view of the Court of Appeal, remain in place. The answer is that the common law doctrine of mistaken assumption is perceived by the Court of Appeal in *The Great Peace* as being very restrictive in nature. Lord Atkin’s views did not escape unscathed. Thus, Lord Phillips questioned whether there was a solid jurisprudential basis for the “quality of the subject-matter” test fashioned by Lord Atkin. It was Lord Phillips’ view that a surer footing could be found in analogous principles in the law of frustration. Thus, after a review of the evolution of frustration doctrine from its origins in implied contract theory to the more modern statement in the *Davis Contractors* case, he concluded: “The avoidance of a contract on the ground of common mistake results from a rule of law under which, if it transpires that one or both of the parties have agreed to do something which it is impossible to perform, no obligation arises out of that agreement.”

Thus building on a rather restrictive view of the doctrine of frustration, Lord Phillips articulated the test for operative mistake at common law in the following terms:

the following elements must be present if common mistake is to avoid a contract:

(i) there must be a common assumption as to the existence of a state of affairs;

(ii) there must be no warranty by either party that that state of affairs exists;

(iii) the non-existence of the state of affairs must not be attributable to the fault of either party;

(iv) the non-existence of the state of affairs must render performance of the contract impossible;

(v) the state of affairs may be the existence, or vital attribute, of the consideration to be provided or circumstances which must subsist if the performance of the contractual adventure is to be possible.

The conclusion that mistake will be operative only where performance of the contract has become impossible appears to offer very little scope for the operation of the doctrine. On the other hand, like the “non-existence of the subject matter” test, it may be possible to manipulate the concept of the “contractual undertaking”

106. Ibid., at p. 705.
108. Supra, footnote 5, at p. 708.
109. Ibid., at pp. 708-09.
in such a way as to be able to conclude that although literal performance of the agreement remains possible, performance of the true “contractual undertaking” has become “impossible”. Indeed, Lord Phillips appears to envisage this sort of manipulation:

In consideration whether performance of the contract is impossible, it is necessary to identify what it is that the parties agreed would be performed. This involves looking not only at the express terms but at any implications that may arise out of the surrounding circumstances. In some cases, it will be possible to identify details of the “contractual adventure” which go beyond the terms which are expressly spelled out, in others it will not.\footnote{110}

Nonetheless, the narrowness of the conception of common law mistake doctrine envisaged by Lord Phillips is underlined by his suggestion that it may be difficult to reconcile \textit{Bell v. Lever Brothers} with \textit{Scott v. Coulson}, the case involving the sale of a life insurance policy on a person who, contrary to the parties’ assumptions, was deceased at the time of contracting. In Lord Phillips’ view, this decision is often erroneously treated as being on all fours with \textit{Strickland v. Turner}, the case applying mistake doctrine to the sale of an annuity on the life of a deceased person. The annuity in \textit{Strickland} was “self-evidently a nullity”, whereas this could not be said of the life insurance policy in \textit{Scott v. Coulson}. Although Lord Phillips did not explicitly suggest that \textit{Scott v. Coulson} should no longer considered to be good law, he suggested that the decision could only be explained on the basis that “a life policy before decease is fundamentally different from a life policy after decease, so that the contractual consideration no longer existed”.\footnote{115}

In such a case, presumably, it may be argued that it has become “impossible” to perform the contractual undertaking.

Finally, then, it remained for the Court of Appeal to apply this test to the present facts. Unsurprisingly, the court concluded that the mistake as to the distance between the two vessels did not “render the contractual adventure impossible of performance”.\footnote{116}

The fact that the boats were farther apart than first assumed did not render the services “essentially different” than those originally

\footnotesize{\begin{itemize}
\item \footnote{110. Ibid., at p. 708.}
\item \footnote{111. Supra, footnote 1.}
\item \footnote{112. Supra, footnote 11.}
\item \footnote{113. Supra, footnote 10.}
\item \footnote{114. Supra, footnote 5, at p. 711.}
\item \footnote{115. Ibid.}
\item \footnote{116. Ibid., at p. 730.}
\end{itemize}}
envisaged. Curiously, although the Court of Appeal quoted, with apparent approval, passages from the judgment of Steyn J. in the Associated Japanese Bank case\(^{117}\) and Hoffmann L.J. in William Sindall Plc\(^{118}\) to the effect that an appropriate first step in the analysis of a mistaken assumptions problem is to attempt to determine whether the parties have allocated the risk of the kind of error which has occurred to one of them, the Court of Appeal did not apply this analysis to the facts of this case. Had the Court of Appeal done so, it may well be that the fact that the parties had included a termination provision in their agreement which permitted termination by the hirer only upon the payment of five days' hire might have been considered to have assigned the risk of early termination to the hirer. In the final paragraph of the judgment Lord Phillips adverted to the importance of the termination clause in the following terms:

The parties entered into a binding contract for the hire of the Great Peace. That contract gave the parties an express right to cancel the contract subject to the obligation to pay the "cancellation fee" of five-days' hire. When they engaged the Nordfarer they cancelled the Great Peace. They became liable in consequence to pay the cancellation fee. There is no injustice in this result.\(^{119}\)

It is most unfortunate that the court did not consider whether, in the light of this provision, the risk of early termination for whatever reason had been implicitly assigned to the hirer by the agreement.

**VIII. CRITIQUE**

Although one must concede that there is some truth in the Court of Appeal's suggestion\(^{120}\) that in *Solle v. Butcher* Denning L.J. attempted to confine the doctrine of mistaken common law as articulated by Lord Atkin in *Bell v. Lever Brothers*, the decision in *The Great Peace* appears to be an unfortunate one for a variety of reasons. First, the test for operative mistake defined by the Court of Appeal in *The Great Peace* appears unduly restrictive and is likely, therefore, to lead to the manipulations characteristic of the earlier narrow versions of the test. Moreover, by failing to address the very problem identified by Denning L.J. in *Solle v. Butcher* —

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the impact of the common law void for mistake doctrine on the interests of third parties — the Court of Appeal has breathed renewed life into a doctrine that is quite unattractive from a policy perspective. Further, the attempted suppression of the equitable doctrine carries with it, at least for the purposes of English law, the suppression of the remedial flexibility afforded by that doctrine. The result is to leave mistaken assumptions doctrine in a very unsatisfactory state as, indeed, the Court of Appeal appears to concede in this case. Finally, the handling of matters of precedent and the impression the reader is given of the Court of Appeal’s sense of the appropriate role of an appellate court in dealing with matters of this kind may appear troubling to some observers. Each of these points may be briefly addressed in turn.

1. The Test for Operative Mistake: One Step Forward and Two Steps Back

One of the alleged strengths of the common law is its ability to renew itself through the modification and improvement of doctrine over time. Although the rate of change may be more glacial than meteoric, there can be no doubt that such change does occur. Through time-honoured devices such as the ironing out of anomalies, the realignment of rules in closer correspondence to their underlying rationales and, indeed, in the overruling of doctrine that has plainly become unsatisfactory as, for example, where the exceptions to the rule threaten to overwhelm the rule altogether, the common law gradually replaces the flawed insights of earlier generations of jurists and adjusts to changing social and economic circumstances. From this perspective, the essential deficiency of mistaken assumptions doctrine is that it appears to have failed to

121. Ibid., at p. 730.
122. For a recent statement to this effect, see Kleinwort Benson Ltd. v. Lincoln City Council, [1998] 4 All E.R. 513 (H.L.) at p. 534, per Lord Goff.
articulate its underlying rationale and align the black letter rule to that underlying set of concerns. American experience strongly suggests that the competing tensions of contractual stability and relief for egregious error are best reconciled by attempting to determine whether the parties have explicitly or implicitly allocated the risk of error in their agreement and, if not, in considering whether the presence of error has given rise to a severe and surprising imbalance in the values being exchanged under the affected transaction.

Against this background, the Court of Appeal in *The Great Peace* has made a valuable contribution by reaffirming that it is critical in situations where the possibility of applying mistaken assumptions doctrine is being considered that a court attempt to make an assessment of the risk allocation effected by the agreement itself. Although the Court of Appeal, unhelpfully in my view, has commingled the risk allocation analysis with the determination of whether performance has become “impossible,” it is nonetheless an important step forward for the court to assert that it is necessary to “determine whether on true construction of the contract one or other party has undertaken responsibility for the subsistence of the assumed state of affairs.” As Steyn J. observed in the *Associated Japanese Bank* case, “[i]t is at this hurdle that many pleas of mistake will either fail or prove to have been unnecessary”. As noted above, however, it is unfortunate that the Court of Appeal did not apply this test to the facts of *The Great Peace*, as it appears that the existence of a cancellation fee provision provided a satisfactory basis for inferring that the risk of early termination for whatever reason was assumed by the hirer.

If this reaffirmation of the importance of risk allocation is an important step forward, there are other features of the test articulated in *The Great Peace* that represent the opposite of progress. Thus, to return to the rigidity of a test that essentially requires one

126. For a brief account of which see the text at footnotes 63-72.
to establish that a performance has become impossible more or less returns the analysis to one of being required to determine whether the subject-matter of the contract is no longer in existence, in some sense, and therefore cannot be delivered. The evidence of the English and Canadian case law on mistaken assumptions establishes beyond doubt, I would suggest, that courts are drawn to relieve for common mistake in circumstances beyond cases of what might be referred to literally as non-existence of the subject-matter of the contract. Accordingly, if this is the test that must be met, courts will, as history indicates, manipulate the concept of "the subject-matter of the agreement" in such a way as to permit relief. Similarly, if courts are required to assert that performance has become impossible, it seems very likely that in a case where relief appears warranted, a court will find that the nature of the contractual undertaking is such that its performance has become "impossible".

As noted above, the Court of Appeal appears to envisage this kind of manipulation by explaining that the nature of the contractual adventure may be determined, in an appropriate case, by looking beyond the four corners of the agreement to its surrounding circumstances. A rule that requires artificial analyses of this kind obfuscates rather than clarifies legal analysis. While an open-textured rule drawn in terms of "fundamental" or "basic" error may be unappealingly vague, a vague rule that permits the courts to weigh the relevant factors unimpeded by circumlocution appears to be the preferable approach. The return in The Great Peace, then, to a much narrower and restrictive definition of the test thus appears quite unhelpful.

Further, the suppression by the Court of Appeal of the relevance of the impact of the error on the values being exchanged appears to direct the analysis away from what must surely be a relevant criterion or factor. What could one mean by "fundamental" or "basic" error other than that the error has had a severe or devastating impact on the equivalency of the exchange? It is ironic, then, as Daniel Friedmann has observed, that "the element that the parties (and possibility also the jury) usually consider to be the most important, is, under the common law, totally irrelevant". As we

131. Ibid., at pp. 708-09, quoted in the text above at footnote 110.
132. Ibid., at pp. 728-29.
have seen, American law certainly does not treat this factor as irrelevant and appears to gain coherence from its willingness to address this consideration more openly than does English law. In short, a test along the American lines of requiring first, that the error not be one the risk of which has been allocated to one of the parties and, second, that the surprising facts have had a drastic effect on the values being exchanged is a far better explanation for the granting of relief than the traditional "non-existence of the subject-matter test" or the "impossibility of performance" variant proposed in The Great Peace.

2. New Legs for Void for Mistake

One of the more disappointing features in the reasoning of The Great Peace is that it simply fails to address the considerations underlying the shift from common law mistake doctrines to equitable mistake doctrines offered by Denning L.J. in Solle v. Butcher. As indicated above, Denning L.J. plainly indicated that the point of engaging equitable jurisdiction in place of that of the common law was to provide protection for innocent third parties who may have purchased the subject-matter of the original agreement in good faith. If the initial transaction is void at common law, no property will pass to the original purchaser and the original purchaser will fail to pass title on to the third party. Equitable rescissionary doctrine, on the other hand, will withhold rescission of the original transaction if doing so is necessary in order to afford appropriate protection to the interests of the bona fide third-party purchaser. As noted above, this shift from void at law to voidable in equity parallels developments in other areas of mistake doctrine which have also restricted the application of common law doctrine in order to afford greater protection to third parties. In The Great Peace, the Court of Appeal failed to discuss this issue and, by reviving the common law doctrine and killing off its equitable counterpart, the decision in The Great Peace returns to centre stage the problem of harm being visited on innocent third parties without justification.

134. See the text at footnotes 63-72.
135. Supra, footnote 4, at pp. 690-91, a passage quoted in the text at footnote 58.
136. See the discussion in the text at footnotes 61-62. Moreover the shift from void to voidable in the context of mistake of identity has recently been reaffirmed by the House of Lords in Shogun Finance Ltd. v. Hudson, supra, footnote 62.
3. The Hardening of the Remedies

In *Solle v. Butcher*, it will be recalled,137 Denning L.J., relying on *Cooper v. Phibbs*,138 held that the equitable rescissionary decree had the useful advantage of enabling the court to condition the granting of rescissionary relief on terms. On the particular facts of that case, Denning L.J. held that the granting of rescission at the instance of the landlord ought to be conditioned on the landlord’s willingness to renew the lease to the tenant for the unexpired portion of the term at the rate that would have been agreed to but for the error. In *The Great Peace*, Lord Phillips — again, it must be conceded, with accuracy — suggested139 that no such wide-ranging discretion is manifest in the order of the court in *Cooper v. Phibbs*. Indeed, the terms imposed in that case simply provide for restitutionary recovery of the value of benefits conferred by each party on the other, a well-established feature of a rescissionary decree. Restitutionary relief would also be possible in the context of an agreement that is void at common law. In principle, the party who has conferred benefits under a contract for mistake should be entitled to bring a common law quasi-contractual claim for the value of benefits conferred.140 Thus, the proposed termination of the equitable jurisdiction to relieve for mistake would appear to have the effect, principally, of cutting off the judicial ability to fashion the kinds of conditions, such as the required offering of a renewal of the lease, that Denning L.J. himself imposed in *Solle v. Butcher*.

Again, the Court of Appeal did not direct any attention to the question of whether or not such remedial flexibility is attractive from a policy perspective. As noted above,141 such remedies do appear to have the capacity of effecting a just result in particular circumstances. Moreover, similar remedies have been allowed in the context of rectification claims, especially so in the Canadian cases.142 Thus, where an agreement is entered into in circumstances where

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137. See the discussion in the text after footnote 62.
141. See the text at footnotes 72-73.
one party is or ought to be aware that the other party is mistaken as to the content or terms of the agreement, the mistaken party may be entitled to rectify the agreement, provided that the non-mistaken party will have the opportunity to rescind the agreement if that party would prefer not to go forward on the basis of the other party's terms. In this fashion, neither party is forced into an agreement to which they did not freely consent. *The Great Peace*, by creating what is, in effect, an absolute bar to the granting of relief of this kind in common assumption cases appears to have inflicted a further injury on the English law of mistaken assumptions.

4. The Call for Statutory Reform

By restoring the law of mistaken assumptions more or less to the account offered by Lord Atkin in *Bell v. Lever Brothers*, it is argued here that the English law has been restored to an unsatisfactory state. It may therefore be considered to be the crowning irony of the judgment in *The Great Peace* that the Court of Appeal itself appears to concede the force of Denning L.J.'s reservations concerning the common law doctrine articulated in that case. Having jettisoned Denning L.J.'s attempted improvements of the doctrine, Lord Phillips observed as follows:

> We can understand why the decision in *Bell v. Lever Bros Ltd.* did not find favour with Denning L.J. An equitable jurisdiction to grant rescission on terms where a common fundamental mistake has induced a contract gives greater flexibility than a doctrine of common law which holds the contract void in such circumstances. Just as the Law Reform (Frustrated Contracts) Act 1943 was needed to temper the effect of the common law doctrine of frustration, so there is scope for legislation to give greater flexibility to our law of mistake than the common law allows.¹⁴³

This call for legislative reform to give the doctrine greater flexibility, on the heels of a determination that the flexibility afforded by equitable mistake doctrine is a "chimera", appears unhelpful for a number of reasons. First, it is very likely that any legislative reform that might be contemplated would simply give statutory expression to the basic approach in *Solle v. Butcher* that common mistaken assumptions should give rise only to the remedy of equitable rescission rather than to voidness at common law.¹⁴⁴ Second, it may

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be questioned whether the legislature is the ideal instrument for refashioning as subtle and complex an area of private law doctrine as the law of mistaken assumptions. It is at least a possible view of the division of responsibility between the legislature and the judiciary that the latter is, as a general matter, the appropriate instrument for the gradual refinement and modification of common law doctrine that is a hallmark of the common law system.

Be that as it may, from a Canadian perspective, a call for statutory reform of the law of mistaken assumptions is particularly unrealistic. With nine common law provinces, virtually none of which manifests substantial interest in legislative reform of the details of the private law of obligations, it is unrealistic to expect that all or, indeed, any of the provinces would address legislation to the resolution of these complex doctrinal difficulties.

5. Matters of Precedent and the Role of the Court of Appeal

Two aspects of the Court of Appeal’s handling of the doctrine of precedent in The Great Peace appear to be contentious. First, the court’s account of Bell v. Lever Brothers appears designed to lead one to the conclusion that it had little choice but to sweep aside the pronouncements of Denning L.J. in Solle v. Butcher and restore the law to the position advanced by Lord Atkin in Bell. With respect, this is somewhat misleading. While it is fair to suggest that Lord Atkin’s views appeared to enjoy general support of the three-member majority in Bell v. Lever Brothers, it was nonetheless the case that Lord Thankerton expressed the rule in slightly different terms than did Lord Atkin, that Lord Blanesburgh was content to decide the case on a pleading point and, further, that Lord Atkin himself introduced sufficient ambiguity into the discussion of the test for mistake that it would be an exaggeration to suggest that it serves as a model of clarity. Accordingly, it is surely not the case that subsequent courts are driven as a matter of technical necessity by the doctrine of stare decisis to conclude that the law was as laid down by Lord Atkin in that case.

145. There are, of course, occasional interventions — see, e.g., Law Reform Act, S.N.B. 1993, c. L-1.2, s. 4 (overruling the doctrine of privity of contract) — but these exceptions merely prove the rule that legislative reform across the provinces on matters of private law doctrine is simply not a realistic option.

146. See the text at footnote 42.

147. See the text at footnote 43.

148. See the text at footnotes 32-41.
Moreover, although Denning L.J. was candid about his desire to curtail, if not reverse, the expansion of common law doctrines in this area, his suggestion that when parties agree on the same terms on the same subject-matter that the contract is enforceable at common law is not so far removed from Lord Atkin’s suggestion that the common law doctrine was limited to cases where the mistake leads to a change in the nature of the subject-matter as to be beyond the pale. One could, in other words, as other Court of Appeal judges have done in recent years, simply accept the existence of the equitable doctrine without doing great violence to the fabric of the common law method. The Court of Appeal had a choice to make in *The Great Peace*, a choice that was not driven by the mechanics of the doctrine of precedent. To be sure, the Court of Appeal expressly made that choice on the basis that, in its view, the equitable doctrine had proven itself to be unsatisfactory and, of course, reasonable persons can differ as to whether or not reversion to the common law doctrine of Lord Atkin is an improvement of the doctrine. Nonetheless, it is disappointing that so little emphasis appears to have been placed in the reasoning of the court on the policy considerations favouring different versions of the common mistake doctrine.

Secondly, it is not entirely clear that the Court of Appeal was correct in taking the view that it was free to disregard its own previous decisions applying the doctrine in *Solle v. Butcher*. S.B. Midwinter has argued persuasively that careful examination of the jurisprudence of the Court of Appeal would suggest the court was not free to do so. Whether or not the Court of Appeal should assert a jurisdiction to depart from its own previous decisions is, of course, another matter. Again, however, if the court had been minded to simply acquiesce in the existence of the equitable doctrine, the doctrine of precedent may well have provided an additional reason for so doing.

Related to these two concerns is a larger concern about the Court of Appeal’s sense of its role in the common law’s continuing exercise in doctrinal reform. Lord Denning had a clear, if controversial, view of the importance of this aspect of an appellate court’s mandate during his tenure on the Court of Appeal. And while, of

course, it is the ultimate court of appeal, the House of Lords, that must assert such leadership as it considers appropriate in matters of this kind, so few cases eventually make their way to the ultimate appellate tribunal in any particular jurisdiction, that it would be unfortunate, in my view, if the intermediate court of appeal assumed little or virtually no responsibility for engaging in this process. It would be both inappropriate and unfair to assume from the reasoning of the Court of Appeal in *The Great Peace* that it has adopted an unduly restrictive view of its own participation in jurisprudential development. On the other hand, the decision does suggest the possibility, at least, that the Court of Appeal may have adopted an unduly cramped vision of its role as an appellate court.

**IX. CONCLUSION**

*The Great Peace.* As Sir Otto Kahn-Freund is alleged to have said of *The Halley* — that flawed classic of English conflicts jurisprudence — "Oh, how I wish that ship had never set sail!"\(^{153}\) It is no easy matter, of course, to craft rules that will effectively reconcile the need for contractual stability and the desirability of relieving for fundamental error in the context of mistaken assumptions cases. Such cases arise only infrequently. The history of the doctrine is arcane and complex. The decision to grant or withhold relief in particular circumstances may be subtle and difficult. On the other hand, American experience demonstrates that it is possible to speak more plainly about these issues than has the traditional English doctrine.\(^{154}\) In *The Great Peace,*\(^ {155}\) the Court of Appeal was afforded an opportunity to either reshape mistaken assumptions doctrine in a constructive way or, more simply, to leave it alone. Unfortunately, the court of chose the path of restoring the doctrine to the unsatisfactory state of the law articulated by Lord Atkin in *Bell v. Lever Brothers.* Indeed, the Court of Appeal itself acknowledged the unsatisfactory state of the law in that form and called upon the legislature to engage in statutory reform of the law of mistaken assumptions.

As a matter of precedent, it should be emphasized that the lengthy analysis of equitable mistake doctrine offered by the Court

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153. I am indebted to my colleague, Professor Reuben Hasson, a former student of Kahn-Freund, for this illustration of Kahn-Freund’s classroom charm.
154. See the text at footnotes 63-72.
155. *Supra,* footnote 5.
of Appeal in *The Great Peace* does not appear to be necessary to
the decision. As the court itself notes, analysis of a mistaken
assumptions case should begin with a careful construction of the
agreement in order to determine whether the risk of the error that
has occurred has been assigned by the agreement to one of the par-
ties. As indicated above, when one undertakes such an analysis of
the agreement in *The Great Peace*, one is drawn to the conclusion
that the stipulation of a termination fee of a few days' hire
assigned the risk of early termination to the hirer. It was thus
unnecessary to consider whether the agreement, though valid at
law, was voidable in equity. Indeed, the Court of Appeal does not
give a clear indication of its view as to whether, if the equitable
doctrine existed, it would embrace these particular facts. Thus, it
is not at all clear that the court believed that it had before it a case
where the equitable doctrine, if it existed, would apply. If it was
not such a case, the discussion of the very existence of the equi-
table doctrine is not necessary to the decision. Whether or not *The
Great Peace* stands as good authority on the state of English law,
however, it does not, of course, constitute an authoritative statement
of Canadian common law.

The reader will not be surprised by my conclusion that it would
be most unfortunate indeed if Canadian courts were to embrace the
reasoning of the Court of Appeal in *The Great Peace*. Canadian
courts have welcomed *Solle v. Butcher* into the fabric of Canadian
mistake doctrine and, in so doing, have, in my view, much
improved upon the law as articulated by Lord Atkin in the *Bell*
case. Moreover, the Court of Appeal's call for legislative reform is
particularly unrealistic in the Canadian context. It is unlikely,
surely, that any province will take up the task of reforming the law
of mistaken assumptions. The most optimistic prognosis would be
that a few provinces might do so, with resulting complexity and
inconsistency in a patchwork of reform and non-reform across the
common law provinces. In short, Canadian courts would be wise to
retain the equitable jurisdiction to treat contracts as voidable on the
basis of mistaken assumptions. Canadian courts minded to improve
the doctrine will find helpful guidance, in my view, in the more
coherent and rational doctrine that has developed in the American

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156. See the discussion in the text at footnotes 78-81 and 126-30.
157. See the discussion in the text at footnotes 83-87.
158. See the discussion in the text at footnotes 143-45.
jurisprudence on these issues. The recognition signalled in *The Great Peace* of the importance of risk allocation analysis in this context is, indeed, a useful and important step in this direction. Courts less attracted by the American model would be well advised, I suggest, to simply leave the Canadian law of mistaken assumptions in its current state.

159. See the discussion in the text at footnotes 63-72.