

SMITH V. HUGHES

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ABSTRACT

Smith v. Hughes is a venerable and often cited case which is as familiar as it is foundational to students' understanding of Contract Law. It is frequently alluded to as the best exemplar of the Objectivity Test in practice. The case revolves around a dispute over sale of oats. An objective approach was applied where the fact that the parties were 'ad idem' and at cross purposes to the terms of the case were considered to be of the most importance, regardless of subjective considerations. The Jury spoke about the 'Caveat Emptor' Rule – Let the Buyer Beware wherein the element to void the contract is that the jury should not merely find that the seller is selling old oats but also that the buyer shall believe that he is buying old oats as the seller contracted to sell old oats. The consensus ad idem of parties in the contract was missing. The case draws a picture wherein it requires to accept an incoherent approach of Contract law which confidently asserts the dominance of objective test in ascertaining contracting parties' intentions but might permit a switch to subjective approach occasionally.

The author will elaborate, on the principle of objectivity approach as well as the switch to subjectivity approach which deals with the intention of parties, in the paper.

INTRODUCTION

Smith v. Hughes¹, an English contract law case wherein Justice Blackburn set out the objective interpretation of a contract or interpreting the intention of contracting parties objectively. This case subtly talks about the rule of Caveat Emptor too.

Mr. Smith was a farmer who dealt in oats whereas Mr. Hughes was a racehorse trainer. Mr. Smith was to bring Mr. Hughes a sample of oats after which he ordered 40 to 50 quarters at a fixed price. When Mr. Smith sent the first lot of the order, Mr. Hughes did not accept them and stated these were not the oats he thought they would be. He wanted old oats (so as to feed the racehorses) but he was delivered the new oats (also popularly known as green oats). Mr. Smith has showed him a sample of green oats and then taken the order but Mr. Hughes refused to pay and also sued Mr. Smith for damages for breach of contract, for all the oats, delivered and to be delivered.

The jury held in favour of Mr. Hughes as they found Mr. Hughes to be in mistake but if Mr. Smith knew of this, it was his fault. Mr. Smith appealed and the Queen's Bench then decided the fate of this case.

The trouble with this was the ambiguity of the judgment. The trial court did not take into account seller's knowledge that would make the contract void. The contract is void only if the buyer believed that the seller was promising for oats to be old but not if buyer merely believed that the olds were old when they were not². The lack of evidence for the former made the latter appeal to the appellate court.

The Court of the Queen's Bench found that the jury had been misdirected and ordered a retrial. Leaning in Mr. Smith's favour, they held that the question was not merely whether the parties were at consensus ad idem, but what they had communicated by their conduct and words to one another. Mr. Smith was held to be under no duty to inform Mr. Hughes of his possible mistake about the kind of oats, reaffirming the old idea of Caveat Emptor.

If one of the parties intends to make a contract on one set of terms, and the other intends to make a contract on another set of terms, or, as it is sometimes expressed, if the parties are not

¹ (1871) LR 6 QB 597

² Mindy Chen-Wishart, Objectivity and Mistake: Oxymoron of Smith v. Hughes, 2009

ad idem, there is no contract, unless the circumstances are such as to preclude one of the parties from denying that he has agreed to the terms of the other.³

Justice Blackburn, in his judgment mentioned, If, whatever a man's real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party's terms.⁴

Justice Diplock formulation was different, the promisee's actual knowledge and beliefs are relevant. She must reasonably understand that the promisor's intention is that alleged by her, and a promisee who knows otherwise, or indeed ought to know otherwise, cannot so reasonably understand. A fortiori if it is established that she shared the promisor's intention at the time of the alleged contract.⁵

It is admitted that the cases given in which the Caveat Emptor rule applies would appear to most people to impose an unjust hardship on one of the parties. They are to be supported on the ground that “it is of paramount importance that contracts should be observed”⁶.

QUESTIONS RAISED

The questions that arise are –

- i) The meaning of objective test to contractual intention.

The objective test determines whether the parties reached agreement and what their agreement was for and the meaning to the parties' conduct.

- ii) The conception of objective test to cases of so-called mistake of terms.

To consider *Smith v. Hughes* as authority for both, objective intention of parties and to void a contract where one knows of the subjective mistake of others is an oxymoron.

³ *Freeman v. Cooke*, 18 LJ (Ex) at p 119

⁴ (1871) LR 6 QB 597

⁵ *Ibid*

⁶ Lord Atkin, *Fender v. Mildmay*, 1937 3 All ER at p. 406

ANALYSIS

i) The meaning of objective test to contractual intention

A party's intention can be determined in two ways, subjective approach and objective approach. Subjective approach refers to the party's actual intention regardless of what he or she appears to intend from his or her conduct, whereas objective approach refers to what a reasonable person would interpret as a party's intention through his or her conduct in all circumstances⁷. *Smith v. Hughes* affirmed the dominance of the objective approach. In Justice Blackburn's words –

“if, whatever a man's real intention may be, he so conducts himself that a reasonable man was assenting to terms proposed by the other party, and the other party upon that belief enters into the contract, the man thus conducting himself would be equally bound as if he had intend to agree the other party's terms.”⁸

A party's conduct may signify consent to a contract when he or she did not really consent or consent was believed to be given on different terms. Contract law primarily deals with subjective intention but the reasons for objective intention to be the alternative are one, accessibility, with regard to the actual intention of parties which cannot be proved and second, to avoid fraud. Objectivity is intrinsic to contracting.⁹ Making a contract is essentially an exercise in communication and communication is impossible without objectivity.¹⁰ Lord Justice May in *Ove Arup v. Mirant Asia Pacific Construction Ltd.* said, “Subjective Intention or understanding, unaccompanied by some overt objectively ascertainable expression of that intention or understanding is not relevant”.¹¹

While defining objectivity, it I important to understand objectivity from different perspectives. The first one is *Detached Objectivity*, also known as the *Fly on the Wall Approach*, wherein the viewpoint of a reasonable person independent of either party. The second perspective is the promisor's perspective, which adopts the viewpoint of the reasonable person seeking to avoid the contract. The third perspective is that of the promisee's, which is the viewpoint of the

⁷ Supra 3

⁸ Supra 6

⁹ Id 13

¹⁰ Id 14

¹¹ 2004 BLR 49 CA 62

reasonable person seeking to enforce the contract. Detached objectivity provides certainty and protects third parties who rely on such contracts and may be affected.

Objectivity has two versions to itself – the traditional formal objectivity and the modern contextual objectivity. Formal objectivity is related to detached objectivity whereas contractual objectivity depends on contractual documents and party's conduct. Lord Hoffman in *Investors Compensation Scheme v. West Bromwich Building Society*¹² and *Mannai Investments Co. Ltd. v. Eagle Star Life Assurance Co. Ltd.*¹³ stresses over contractual interpretation, he explains how words do not in themselves refer to anything, it is people who use words to refer to things and people can unambiguously express their feeling even with wrong words.¹⁴

The crucial decision is not between subjectivity and objectivity, since subjectivity is simply irrelevant, but rather between detached-formal objectivity, on one hand and observer-contractual objectivity, on the other. The former might necessitate resort to the notion of exceptional subjectivity to explain outcome of cases where contracts are voided for mistake of terms but it is unnecessary on the more expansive observer-contractual objectivity¹⁵.

ii) The conception of objective test to cases of so-called mistake of terms.

According to *Smith v. Hughes*, the components of an operative mistake of terms are¹⁶ –

- a) There is an objectively determinable agreement (A1)
- b) The actor mistakenly believes the agreement is not for A1 but for an entirely different agreement (A2)
- c) The actor also mistakenly believes that the observer is agreeing to A2
- d) The observer knows of the mistakes in (b) and (c)

The argument is that once the objective agreement A1 is found via observer-contractual objectivity, the observer (the seller) cannot logically know of the actor's (buyer) intention to agree to A2. The observer cannot honestly and reasonably believe that the actor intends to A1 (implicit in finding an agreement for A1) and honestly and reasonably believe that he or she intends to agree to the inconsistent A2.

¹² 1998 1 WLR 896 HL

¹³ 1997 AC 749 HL

¹⁴ Ibid

¹⁵ Supra 4

¹⁶ Supra 2

The question that remains unanswered is - Was the contract for 'oats' as the seller alleged, or was the contract for 'old oats' as the buyer alleged?

The court's conclusion was entirely consistent with the observer-contractual objectivity. The agreement was for 'oats'. The buyer never specified the requirement of 'old oats, either expressly or implied and the buyer offered the price only after inspecting a sample of oats which corresponded with what was delivered later¹⁷. The seller had no reason to know of the buyer's intention to buy old oats, the buyer claimed that trainers used old oats as a rule and the seller was supposed to know of such intention which was rejected by the Court.

The buyer's unilateral mistaken assumption that the oats he was buying were old is legally irrelevant. Even the seller's knowledge of the buyer's mistake does not change this, absent a general obligation of disclosure. Even if it is found that the buyer mistook the seller's offer, it is impossible to find that the seller knew of it. No rational party would concede such knowledge when knowledge of the other's mistake as to subject matter can be admitted without cost. The seller's conduct is honestly and reasonably interpreted by the buyer as consenting to buy oats.

Mistake of term is not possible but there can be different approaches to the scenario using the objectivity principle¹⁸.

- 1) If the buyer's conduct is honestly and reasonably interpreted by the seller as consenting to buy oats and vice versa, then that is the objectively determined contract. The seller cannot, at the same time, honestly and reasonably believe that the buyer is consenting to old oats.
- 2) If the buyer's conduct is honestly and reasonably interpreted by the seller as promising old oats and vice versa, then that is the objectively determined contract. He can now not only refuse payment for new oats but also enforce the contract for old oats. This is theoretically possible but not the conclusion of *Smith v. Hughes*.
- 3) If seller's conduct merely induced the buyer's mistake of fact that the oats were old (it wasn't a term promising old oats), the contract is voidable for misrepresentation.
- 4) If the seller neither promised nor represented that the oats were old, but still had reason to know that the buyer did not intend to contract on his terms, but without knowing

¹⁷ Supra 6

¹⁸ Supra 5

what the buyer was intending to contract for, there would simply be no agreement between the parties on the ground of lack of consensus ad idem.

Smith v. Hughes recognizes the category of ‘known mistakes of term’ but it itself isn’t a positive instance of such a category¹⁹.

The final question that is to be pondered upon from Smith v. Hughes is – why is it that the buyer’s mistaken belief that the oats he purchased were old, attracts no relief, but the buyer’s mistake that the seller promised that the oats will be old will void the contract, if known to the seller? If a mistake as to some non-fundamental quality of the subject matter does not negate consent, why should a mistake as to whether the other party promised it, do so?

When contracts are set aside, even for mistake, it is done so because of the claimant’s defective consent to the contract. Like mistake, defective consent is not precise enough to be useful, but is loose enough to cause trouble.

The primary distinction between contract formation and vitiation of a contract is fundamental. It mirrors that key distinction between terms inside a contract and assumptions outside a contract. As Smith v. Hughes shows, the quality of the subject matter (that the oats are old) maybe either a term or an assumption attracting different reliefs. The same applies to existence and identity of the subject matter of the contract²⁰.

Mistake of terms and Mistake of facts raise different issues and principles. Mistake of terms deal with formation and contents of the contract, they raise issues of acceptance, implied as well as collateral terms. Mistake of facts are mistaken assumption of the context in which the contract is made²¹.

The contractual document will only be the objective reference point of determining mistake if, objectively determined, the parties have agreed that it embodies their agreement and their agreement has not been wrongly recorded²².

¹⁹ Supra 3

²⁰ *McRae v. Commonwealth Disposals Commission*, 1954 84 CLR 377 HCA

²¹ Supra 2

²² Supra 1

CONCLUSION

Smith v. Hughes is a landmark judgment in Contract Law as well as in the area of interpreting contracts. The judgment laid down important conclusions and principles –

- a) To take great care while defining objective or subjective tests of intention
- b) Once the contours of the objective test are properly understood, the cases are to be characterized as straightforward applications of objectivity. There is no incoherent need to resort to subjective approach of interpretation.
- c) The attempt to understand why mistakes of term only have to be known by the other party in order to void contracts. (Mistake of facts are important and fundamental but can only make the contract voidable and not void).

The objective meaning of an agreement is its only meaning, that particular words or combinations of words always have the same meaning. Although language must be shared, it is possible for there to be only two sharers. Words must always be understood in their context.

The actual intention of the parties is irrelevant to the formation of a contract. Logically, the actual or subjective intention should be equally irrelevant to determinations of what the parties actually agreed.²³ The author differs from this approach, since evidence of the actual mutual intention of the parties is relevant and admissible when the existence of a contract is in issue, evidence of their actual intention concerning the meaning of the contract should also be relevant and therefore admissible when it comes to the interpretation of an admitted contract.

²³ McLauchlan, 'A Contract Contradiction' (1999) 30 Victoria University of Wellington Law Review 175.