Nilai UNIVERSITY

OBM4405

ETHICS AND BUSINESS LAW

SELF INSTRUCTIONAL MATERIALS

FACULTY OF BUSINESS, HUMANITIES & HOSPITALITY

MASTER IN BUSINESS ADMINISTRATION
BANKING AND FINANCE

Contents

COURSE OVERVIEW

COURSE GUIDE DESCRIPTION

You must read this Course Guide carefully from the beginning to the end. It tells you briefly what the course is about and how you can work your way through the course material. It also suggests the amount of time you are likely to spend to complete the course successfully. Please refer to the course guide from time to time as you go through the course material as it will help you to clarify important study components or points that you might miss or overlook.

INTRODUCTION

Ethics and Business Law (OBM4405) is one of the courses offered at Nilai University. This course is worth 3 credit hours and should be covered over 10 to 17 weeks.

AIM OF THE COURSE

This module aims to provide you an opportunity to acquire a wide range of theoretical perspectives in order to evaluate organisational attempts at the management of change and innovation. You will be equipped with the conceptual skills for managing people in the organisation through periods of major change and for creating an environment that encourages creativity and innovatory behaviour. It gives you the imperative of constant surveyance of the external environment in order to attain stability for the long-term existence of the business.

STUDY SCHEDULE

It is a standard practice that learners accumulate 40 study hours for every credit hour. As such, for a three-credit hour course, you are expected to spend 120 study hours. Table 1 gives an estimation of how the 120 study hours could be accumulated.

Study Activities	Study Hours
Study the module	40
Attend to 3 to 5 tutorial sessions	34
Online participation	10
Revision	10
Assignment(s) and Examination(s)	26
TOTAL STUDY HOURS ACCUMULATED	120

TABLE 1: Estimation of Time Accumulation of Study Hours

COURSE LEARNING OUTCOME

After the successful completion of this module, students should be able to:

- Apply the values and attitudes that provide individuals with a commitment to act in the public interest and with social responsibilities.
- Analyze the need for a framework of laws, regulations and standard in business and their applications.
- Evaluate the defference between details rules-based and framework approches to ethics.

SUPPORT AND CONTACT DETAILS

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COURSE SYNOPSIS

Topic 1 introduces learners to the laws of contract. Learners will be exposed to the classification, elements, and enforceability of contracts. We will also cover the formation and termination of contracts. We will cover many cases that involves contract law to reinforce the concepts above.

Topic 2 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 3 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 4 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

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Topic 6 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 7 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 8 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 9 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

Topic 10 introduces learners to the concept of ethics in the business environment and ethical issues. Learners will be exposed to the cases which allow them to distinguish between ethics and law. The topic also discusses the importance of ethical values for managers in the organization.

PRIOR KNOWLEDGE

This is an introductory course. There is no prior knowledge needed.

ASSESSMENT

Assessment Methods and Types:

TASKS	PERCENTAGE
Mid-term Exam	20%
Group Assignment	40%
Final Examination	40%

TEXT

Main reference supporting the course:

Business law, Lee Mei Peng, Ivan Jeron Detta, Oxford University Press, 2018

Topic 1 ▸ INTRODUCTION TO THE LAW OF CONTRACT

LEARNING OUTCOMES

By the end of this topic, you will be able to:

1. Explain the classification, elements, and enforceability of contracts,
2. Explain the formation and termination of contracts.; and
3. Evaluate contract law cases.

1.1 DEFINITION

A contract may be defined as a legally binding agreement or, in the words of Sir Frederick Pollock: “A promise or set of promises which the law will enforce”.

The agreement will create rights and obligations that may be enforced in the courts. The normal method of enforcement is an action for damages for breach of contract, though in some cases the court may order performance by the party in default.

1.2 CLASSIFICATION

Contracts may be divided into two broad classes:

1. Contracts by deed

A deed is a formal legal document signed, witnessed and delivered to effect a conveyance or transfer of property or to create a legal obligation or contract.

2. Simple contracts

Contracts which are not deeds are known as simple contracts. They are informal contracts and may be made in any way – in writing, orally or they may be implied from conduct.

Another way of classifying contracts is according to whether they are "bilateral" or "unilateral".

3. Bilateral contracts

A bilateral contract is one where a promise by one party is exchanged for a promise by the other. The exchange of promises is enough to render them both enforceable. Thus in a contract for the sale of goods, the buyer promises to pay the price and the seller promises to deliver the goods.

4. Unilateral contracts

A unilateral contract is one where one party promises to do something in return for an act of the other party, as opposed to a promise, eg, where X promises a reward to anyone who will find his lost wallet. The essence of the unilateral contract is that only one party, X, is bound to do anything. No one is bound to search for the lost wallet, but if Y, having seen the offer, recovers the wallet and returns it, he/she is entitled to the reward.

SELF CHECK 1.1

1. Define contract.
2. Explain the 4 classifications of contracts

1.3 ELEMENTS

The essential elements of a contract are:

1. Agreement

An agreement is formed when one party accepts the offer of another and involves a "meeting of the minds".

2. Consideration

Both parties must have provided consideration, ie, each side must promise to give or do something for the other.

3. Intention to create legal relations

The parties must have intended their agreement to have legal consequences. The law will not concern itself with purely domestic or social agreements.

4. Form

In some cases, certain formalities (that is, writing) must be observed.

5. Capacity

The parties must be legally capable of entering into a contract.

6. Consent

The agreement must have been entered into freely. Consent may be vitiated by duress or undue influence.

7. Legality

The purpose of the agreement must not be illegal or contrary to public policy.

A contract which possesses all these requirements is said to be valid. The absence of an essential element will render the contract either void, voidable or unenforceable (as to which see below).

In addition, a contract consists of various terms, both express and implied. A term may be inserted into the contract to exclude or limit one party's liability (the so-called "small print"). A term may also be regarded as unfair. A contract may be invalidated by a mistake and where the contract has been induced by misrepresentation the innocent party may have the right to set it aside. As a general rule, third parties have no rights under a contract but there are exceptions to the doctrine of privity. There are different ways of discharging a contract and remedies are available for breach of contract at common law and in equity.

SELF CHECK 1.2

List the 7 essentials of a contract.

1.4 ENFORCEABILITY

1. Void contracts

A "void contract" is one where the whole transaction is regarded as a nullity. It means that at no time has there been a contract between the parties. Any goods or money obtained under the agreement must be returned. Where items have been resold to a third party, they may be recovered by the original owner.

2. Voidable contracts

A contract which is voidable operates in every respect as a valid contract unless and until one of the parties takes steps to avoid it. Anything obtained under the contract must be returned, insofar as this is possible. If goods have been resold before the contract was avoided, the original owner will not be able to reclaim them.

3. Unenforceable contracts

An unenforceable contract is a valid contract but it cannot be enforced in the courts if one of the parties refuses to carry out its terms. Items received under the contract cannot generally be reclaimed.

SELF CHECK 1.3

1. What is the difference between voidable contracts and unenforceable contracts?

1.5 FORMATION OF A CONTRACT

INTRODUCTION

A contract may be defined as an agreement between two or more parties that is intended to be legally binding.

The first requisite of any contract is an agreement (consisting of an offer and acceptance). At least two parties are required; one of them, the offeror, makes an offer which then, the offeree, accepts.

OFFER

An offer is an expression of willingness to contract made with the intention that it shall become binding on the offeror as soon as it is accepted by the offeree.

A genuine offer is different from what is known as an "invitation to treat", ie where a party is merely inviting offers, which he is then free to accept or reject. The following are examples of invitations to treat:

1. AUCTIONS

In an auction, the auctioneer's call for bids is an invitation to treat, a request for offers. The bids made by persons at the auction are offers, which the auctioneer can accept or reject as he chooses. Similarly, the bidder may retract his bid before it is accepted. See:

Payne v Cave (1789) 3 Term Rep 148

2. DISPLAY OF GOODS

The display of goods with a price ticket attached in a shop window or on a supermarket shelf is not an offer to sell but an invitation for customers to make an offer to buy. See:

FishervBell[1960]3AllER731
P.S.G.B. v Boots Chemists [1953] 1 All ER 482.

3. ADVERTISEMENTS

Advertisements of goods for sale are normally interpreted as invitations to treat. See:

Partridge v Crittenden [1968] 2 All ER 421.

However, advertisements may be construed as offers if they are unilateral, ie, open to all the world to accept (eg, offers for rewards). See:

Carlill v Carbolic Smoke Ball Co [1893] 1 QB 256.

4. MERE STATEMENTS OF PRICE

A statement of the minimum price at which a party may be willing to sell will not amount to an offer. See:

Harvey v Facey [1893] AC 552
Gibson v Manchester County Council [1979] 1 All ER 972.

5. TENDERS

Where goods are advertised for sale by tender, the statement is not an offer, but an invitation to treat; that is, it is a request by the owner of the goods for offers to purchase them. The process of competitive tendering came under scrutiny in the following cases:

Harvela Investments v Royal Trust Co. of Canada [1985] 2 All ER 966
Blackpool Aero Club v Blackpool Borough Council [1990] 3 All ER 2

1.6 ACCEPTANCE

An acceptance is a final and unqualified acceptance of the terms of an offer. To make a binding contract the acceptance must exactly match the offer. The offeree must accept all the terms of the offer.
However, in certain cases it is possible to have a binding contract without a matching offer and acceptance. See:

Brogden v Metropolitan Railway Co. (1877) 2 App Cas 666
Lord Denning in *Gibson v Manchester City Council* [1979] above
Percy Trentham Ltd v Archital Luxfer Ltd [1993] 1 Lloyd's Rep 25.

The following rules have been developed by the courts with regard to acceptance:

1. COUNTER OFFERS
If in his reply to an offer, the offeree introduces a new term or varies the terms of the offer, then that reply cannot amount to an acceptance. Instead, the reply is treated as a "counter offer", which the original offeror is free to accept or reject. A counter-offer also amounts to a rejection of the original offer which cannot then be subsequently accepted. See:

Hyde v Wrench (1840) 3 Beav 334.

A counter-offer should be distinguished from a mere request for information. See:

Stevenson v McLean (1880) 5 QBD 346.

If A makes an offer on his standard document and B accepts on a document containing his conflicting standard terms, a contract will be made on B's terms if A acts upon B's communication, eg by delivering goods. This situation is known as the "battle of the forms". See:

Butler Machine Tool v Excell-o-Corp [1979] 1 All ER 965.

2. CONDITIONAL ACCEPTANCE
If the offeree puts a condition in the acceptance, then it will not be binding.

3. TENDERS

A tender is an offer, the acceptance of which leads to the formation of a contract. However, difficulties arise where tenders are invited for the periodical supply of goods:
(a) Where X advertises for offers to supply a specified quantity of goods, to be supplied during a specified time, and Y offers to supply, acceptance of Y's tender creates a contract, under which Y is bound to supply the goods and the buyer X is bound to accept them and pay for them.
(b) Where X advertises for offers to supply goods up to a stated maximum, during a certain period, the goods to be supplied as and when demanded, acceptance by X of a tender received from Y does not create a contract. Instead, X's acceptance converts Y's tender into a standing offer to supply the goods up to the stated maximum at the stated price as and when requested to do so by X. The standing offer is accepted each time X places an order, so that there are a series of separate contracts for the supply of goods. See:

Great Northern Railway Co. v Witham (1873) LR 9 CP 16.

FACTS

Great Northern advertised for tenders for the supply of iron for a period of twelve months.

Witham tendered to supply the iron required for the period at certain fixed prices and "in such quantities as the company's store-keeper might order from time to time".

Great Northern accepted the tender but eventually Witham stopped supplying the iron.

Great Northern sued for breach of contract. Witham defended the claim and alleged that the agreement was not an enforceable contract as the was no consideration by Great Northern.

ISSUES

The court had to decide the obligation of a party who submits a tender guaranteeing their ability to provide goods and services at fixed prices when this tender is accepted by the party inviting tenders.

FINDING

There was a sufficient consideration for Witham's promise to supply the iron, despite Great Northern not being obliged to order any iron.

The Court did say that if Witham had given notice to Great Northern that the fixed prices would no longer apply then it was possible that the obligation to supply the iron at the fixed prices would end, even if the period of the supply arrangement had not ended.

QUOTE

Brett J said:

"So, if one says to another, 'If you will give me an order for iron, or other goods, I will supply it at a given price;' if the order is given, there is a complete contract which the seller is bound to perform. There is in such a case ample consideration for the promise. So, here, the company having given the defendant an order at his request, his acceptance of the order would bind them." – page 19 of [1873] LR 9 CP 16

"I think it would be wrong to countenance the notion that a man who tenders for the supply of goods in this way is not bound to deliver them when an order is given." – page 20 of [1873] LR 9 CP 16

IMPACT

A person who submits tenders which outline their ability to provide goods and services at set prices must be able to do so when called upon should their tender be accepted.

The Courts deem the contract to be created at the time the tender is accepted.

However, performance of the contract will not take place until the tender is called upon to perform and supply the goods or services. The tenderer however, may be allowed to give reasonable notice to withdraw their set prices, and thus withdraw their offer.

4. COMMUNICATION OF ACCEPTANCE

The general rule is that an acceptance must be communicated to the offeror. Until and unless the acceptance is so communicated, no contract comes into existence:

> Lord Denning in *Entores v Miles Far East Corp.* [1955] 2 All ER 493.

The acceptance must be communicated by the offeree or someone authorised by the offeree. If someone accepts on behalf of the offeree, without authorisation, this will not be a valid acceptance:

> *Powell v Lee* (1908) 99 LT 284.

The offeror cannot impose a contract on the offeree against his wishes by deeming that his silence should amount to an acceptance:

> *Felthouse v Bindley* (1862) 11 CBNS 869.

Where an instantaneous method of communication is used, eg telex, it will take effect when and where it is received. See:

> *Entores v Miles Far East Corp* [1955] 2 QB 327
> *The Brimnes* [1975] QB 929
> *Brinkibon v Stahag Stahl* [1983] 2 AC 34.

5. EXCEPTIONS TO THE COMMUNICATION RULE

a) In unilateral contracts the normal rule for communication of acceptance to the offeror does not apply. Carrying out the stipulated task is enough to constitute acceptance of the offer.
b) The offeror may expressly or impliedly waive the need for communication of acceptance by the offeree, eg, where goods are dispatched in response to an offer to buy.
c) The Postal Rule - Where acceptance by post has been requested or where it is an appropriate and reasonable means of communication between the parties, then acceptance is complete as soon as the letter of acceptance is posted, even if the letter is delayed, destroyed or lost in the post so that it never reaches the offeror. See:

Adams v Lindsell (1818) 1 B & Ald 681.
Household Fire Insurance Co. v Grant (1879) 4 Ex D 216.

The postal rule applies to communications of acceptance by cable, including telegram, but not to instantaneous modes such as telephone, telex and fax. The postal rule will not apply:

(i) Where the letter of acceptance has not been properly posted, as in *Re London and Northern Bank* (1900), where the letter of acceptance was handed to a postman only authorised to deliver mail and not to collect it.

(ii) Where the letter is not properly addressed. There is no authority on this point.

(iii) Where the express terms of the offer exclude the postal rule, ie if the offer specifies that the acceptance must reach the offeror. In *Holwell Securities v Hughes* (1974, below), the postal rule was held not to apply where the offer was to be accepted by "notice in writing". Actual communication was required.

(iv) It was said in *Holwell Securities* that the rule would not be applied where it would produce a "manifest inconvenience or absurdity".

Revocation of posted acceptance.
Can an offeree withdraw his acceptance, after it has been posted, by a later communication, which reaches the offeror before the acceptance? There is no clear authority in English law. The Scottish case of *Dunmore v Alexander* (1830) appears to permit such a revocation but it is an unclear decision. A strict application of the postal rule would not permit such withdrawal. This view is supported by decisions in: New Zealand in *Wenkheim v Arndt* (1873) and *South Africa in A-Z Bazaars v Ministry of Agriculture* (1974). However, such an approach is regarded as inflexible.

6. METHOD OF ACCEPTANCE
The offer may specify that acceptance must reach the offeror in which case actual communication will be required. See:

Holwell Securities v Hughes [1974] 1 All ER 161.

If a method is prescribed without it being made clear that no other method will suffice then it seems that an equally advantageous method would suffice. See:

Tinn v Hoffman (1873) 29 LT 271
Yates Building Co. v Pulleyn Ltd (1975) 119 SJ 370.

7. KNOWLEDGE OF THE OFFER

An offeree may perform the act that constitutes acceptance of an offer, with knowledge of that offer, but for a motive other than accepting the offer. The question that then arises is whether his act amounts to a valid acceptance. The position seems to be that: (a) An acceptance which is wholly motivated by factors other than the existence of the offer has no effect.

R v Clarke (1927) 40 CLR 227

(b) Where, however, the existence of the offer plays some part, however small, in inducing a person to do the required act, there is a valid acceptance of the offer. See:

Williams v Carwardine (1833) 5 Car & P 566.

8. CROSS-OFFERS

A writes to B offering to sell certain property at a stated price. B writes to A offering to buy the same property at the same price. The letters cross in the post. Is there (a) an offer and acceptance, (b) a contract? This problem was discussed, obiter, by the Court in *Tinn v Hoffman* (1873) 29 LT 271. Five judges said that cross-offers do not make a binding contract. One judge said they do.

1.7 TERMINATION OF THE OFFER

1. ACCEPTANCE

Once an offer has been accepted, a binding agreement is made and the offer ends.

2. REJECTION

If the offeree rejects the offer that is the end of it.

3. REVOCATION

The offer may be revoked by the offeror at any time until it is accepted. However, the revocation of the offer must be communicated to the offeree(s). Unless and until the revocation is so communicated, it is ineffective. See:

Byrne v Van Tienhoven (1880) 5 CPD 344.

The revocation need not be communicated by the offeror personally, it is sufficient if it is done through a reliable third party. See:

Dickinson v Dodds (1876) 2 ChD 463.

Where an offer is made to the whole world, it appears that it may be revoked by taking reasonable steps. See:

Shuey v United States [1875] 92 US 73.

Once the offeree has commenced performance of a unilateral offer, the offeror may not revoke the offer. See:

Errington v Errington [1952] 1 All ER 149
Daulia v Four Millbank Nominees [1978] 2 All ER 557.

4. COUNTER OFFER

See above for *Hyde v Wrench* (1840).

5. LAPSE OF TIME

Where an offer is stated to be open for a specific length of time, then the offer automatically terminates when that time limit expires. Where there is no express time limit, an offer is normally open only for a reasonable time. See:

Ramsgate Victoria Hotel v Montefiore (1866) LR 1 Ex 109.

6. FAILURE OF A CONDITION

An offer may be made subject to conditions. Such a condition may be stated expressly by the offeror or implied by the courts from the circumstances. If the condition is not satisfied the offer is not capable of being accepted. See:

Financings Ltd v Stimson [1962] 3 All ER 386.

7. DEATH

The offeree cannot accept an offer after notice of the offeror's death. However, if the offeree does not know of the offeror's death, and there is no personal element involved, then he may accept the offer. See:

Bradbury v Morgan (1862) 1 H&C 249.

1.8 CASES ON FORMATION OF A CONTRACT OFFER

Payne v Cave (1789)

The defendant made the highest bid for the plaintiff's goods at an auction sale, but he withdrew his bid before the fall of the auctioneer's hammer. It was held that the defendant was not bound to purchase the goods. His bid amounted to an offer which he was entitled to withdraw at any time before the auctioneer signified acceptance by knocking down the hammer. Note: The common law rule laid down in this case has now been codified in s57(2) Sale of Goods Act 1979.

Fisher v Bell (1960)

A shopkeeper displayed a flick knife with a price tag in the window. The Restriction of Offensive Weapons Act 1959 made it an offence to 'offer for sale' a 'flick knife'. The shopkeeper was prosecuted in the magistrates' court but the Justices declined to convict on the basis that the knife had not, in law, been 'offered for sale'.

This decision was upheld by the Queen's Bench Divisional Court. Lord Parker CJ stated: "It is perfectly clear that according to the ordinary law of contract the display of an article with a price on it in a shop window is merely an invitation to treat. It is in no sense an offer for sale the acceptance of which constitutes a contract."

PSGB v Boots (1953)

The defendants' shop was adapted to the "self-service" system. The question for the Court of Appeal was whether the sales of certain drugs were effected by or under the supervision of a registered pharmacist. The question was answered in the affirmative. Somervell LJ stated that "in the case of an ordinary shop, although goods are displayed and it is intended that customers should go and choose what they want, the contract is not completed until, the customer having indicated the articles which he needs, the shopkeeper, or someone on his behalf, accepts that offer. Then the contract is completed."

Partridge v Crittenden (1968)

It was an offence to offer for sale certain wild birds. The defendant had advertised in a periodical 'Quality Bramblefinch cocks, Bramblefinch hens, 25s each'. His conviction was quashed by the High Court. Lord Parker CJ stated that when one is dealing with advertisements and circulars, unless they indeed come from manufacturers, there is business sense in their being construed as invitations to treat and not offers for sale. In a very different context Lord Herschell in *Grainger v Gough (Surveyor of Taxes)* [1896] AC 325, said this in dealing with a price list:

"The transmission of such a price list does not amount to an offer to supply an unlimited quantity of the wine described at the price named, so that as soon as an order is given there is a binding contract to supply that quantity. If it were so, the merchant might find himself involved in any number of contractual obligations to supply wine of a particular description which he would be quite unable to carry out, his stock of wine of that description being necessarily limited."

Carlill v Carbolic Smoke Ball Co (1893)

An advert was placed for 'smoke balls' to prevent influenza. The advert offered to pay £100 if anyone contracted influenza after using the ball. The company deposited £1,000 with the Alliance Bank to show their sincerity in the matter. The plaintiff bought one of the balls but contracted influenza. It was held that she was entitled to recover the £100. The Court of Appeal held that:

(a) the deposit of money showed an intention to be bound, therefore the advert was an offer;
(b) it was possible to make an offer to the world at large, which is accepted by anyone who buys a smokeball;
(c) the offer of protection would cover the period of use; and
(d) the buying and using of the smokeball amounted to acceptance.

Harvey v Facey (1893)

The plaintiffs sent a telegram to the defendant, "Will you sell Bumper Hall Pen? Telegraph lowest cash price".
The defendants reply was "Lowest price £900".
The plaintiffs telegraphed "We agree to buy … for £900 asked by you".

It was held by the Privy Council that the defendants telegram was not an offer but simply an indication of the minimum price the defendants would want, if they decided to sell. The plaintiffs second telegram could not be an acceptance.

Gibson v MCC (1979)

The council sent to tenants details of a scheme for the sale of council houses. The plaintiff immediately replied, paying the £3 administration fee. The council replied: "The corporation may be prepared to sell the house to you at the purchase price of £2,725 less 20 per cent. £2,180 (freehold)." The letter gave details about a mortgage and went on "This letter should not be regarded as a firm offer of a mortgage. If you would like to make a formal application to buy your council house, please complete the enclosed application form and return it to me as soon as possible." G filled in and returned the form. Labour took control of the council from the Conservatives and instructed their officers not to sell council houses unless they were legally bound to do so. The council declined to sell to G.

In the House of Lords, Lord Diplock stated that words italicised seem to make it quite impossible to construe this letter as a contractual offer capable of being converted into a legally enforceable open contract for the sale of land by G's written acceptance of it. It was a letter setting out the financial terms on which it may be the council would be prepared to consider a sale and purchase in due course.

Harvela v Royal Trust (1985)

Royal Trust invited offers by sealed tender for shares in a company and undertook to accept the highest offer. Harvela bid $2,175,000 and Sir Leonard Outerbridge bid $2,100,000 or $100,000 in excess of any other offer. Royal Trust accepted Sir Leonard's offer. The trial judge gave judgment for Harvela.

In the House of Lords, Lord Templeman stated: "To constitute a fixed bidding sale all that was necessary was that the vendors should invite confidential offers and should undertake to accept the highest offer. Such was the form of the invitation. It follows that the invitation upon its true construction created a fixed bidding sale and that Sir Leonard was not entitled to submit and the vendors were not entitled to accept a referential bid."

Blackpool Aero Club v Blackpool Borough Council (1990)

BBC invited tenders to operate an airport, to be submitted by noon on a fixed date. The plaintiffs tender was delivered by hand and put in the Town Hall letter box at 11am. However, the tender was recorded as having been received late and was not considered. The club sued for breach of an alleged warranty that a tender received by the deadline would be considered. The judge awarded damages for breach of contract and negligence. The council's appeal was dismissed by the Court of Appeal.

1.9 CASES ON ACCEPTANCE OF A CONTRACT OFFER

Brogden v MRC (1877)

B supplied coal to MRC for many years without an agreement. MRC sent a draft agreement to B who filled in the name of an arbitrator, signed it and returned it to MRC's agent who put it in his desk. Coal was ordered and supplied in accordance with the agreement but after a dispute arose B said there was no binding agreement.

It was held that B's returning of the amended document was not an acceptance but a counter-offer which could be regarded as accepted either when MRC ordered coal or when B actually supplied. By their conduct the parties had indicated their approval of the agreement.

Gibson v MCC (1979)

Lord Denning said that one must look at the correspondence as a whole and the conduct of the parties to see if they have come to an agreement.

Trentham v Luxfer (1993)

T built industrial units and subcontracted the windows to L. The work was done and paid for. T then claimed damages from L because of defects in the windows. L argued that even though there had been letters, phone calls and meetings between the parties, there was no matching offer and acceptance and so no contract.

The Court of Appeal held that the fact that there was no written, formal contract was irrelevant, a contract could be concluded by conduct. Plainly the parties intended to enter into a contract, the exchanges between them and the carrying out of instructions in those exchanges, all supported T's argument that there was a course of dealing between the parties which amounted to a valid, working contract. Steyn LJ pointed out that:
(a) The courts take an objective approach to deciding if a contract has been made.
(b) In the vast majority of cases a matching offer and acceptance will create a contract, but this is not necessary for a contract based on performance.

Hyde v Wrench (1840)

6 June W offered to sell his estate to H for £1000; H offered £950
27 June W rejected H's offer
29 June H offered £1000. W refused to sell and H sued for breach of contract.

Lord Langdale MR held that if the defendant's offer to sell for £1,000 had been unconditionally accepted, there would have been a binding contract; instead the plaintiff made an offer of his own of £950, and thereby rejected the offer previously made by the defendant. It was not afterwards competent for the plaintiff to revive the proposal of the defendant, by tendering an acceptance of it; and that, therefore, there existed no obligation of any sort between the parties.

Stevenson v McLean (1880)

On Saturday, the defendant offered to sell iron to the plaintiff at 40 shillings a ton, open until Monday. On Monday at 10am, the plaintiff sent a telegram asking if he could have credit terms. At 1.34pm the plaintiff sent a telegram accepting the defendant's offer, but at 1.25pm the defendant had sent a telegram: 'Sold iron to third party' arriving at 1.46pm. The plaintiff sued the defendant for breach of contract and the defendant argued that the plaintiff's telegram was a counter-offer so the plaintiff's second telegram could not be an acceptance.

It was held that the plaintiff's first telegram was not a counter-offer but only an enquiry, so a binding contract was made by the plaintiff's second telegram.

Butler Machine Tool v Ex-Cell-O Corporation (1979)

The plaintiffs offered to sell a machine to the defendants. The terms of the offer included a condition that all orders were accepted only on the sellers' terms which were to prevail over any terms and conditions in the buyers' order. The defendants replied ordering the machine but on different terms and conditions. At the foot of the order was a tear-off slip reading, "We accept your order on the Terms and Conditions stated thereon." The plaintiffs signed and returned it, writing, "your official order … is being entered in accordance with our revised quotation …".

The Court of Appeal had to decide on which set of terms the contract was made. Lord Denning M.R. stated:

In many of these cases our traditional analysis of offer, counter-offer, rejection, acceptance and so forth is out-of-date. This was observed by Lord Wilberforce in *New Zealand Shipping Co Ltd v AM Satterthwaite*. The better way is to look at all the documents passing between the parties and glean from them, or from the conduct of the parties, whether they have reached agreement on all material points, even though there may be differences between the forms and conditions printed on the back of them. As Lord Cairns L.C. said in *Brogden v Metropolitan Railway Co* (1877):

… there may be a consensus between the parties far short of a complete mode of expressing it, and that consensus may be discovered from letters or from other documents of an imperfect and incomplete description.

Applying this guide, it will be found that in most cases when there is a "battle of forms" there is a contract as soon as the last of the forms is sent and received without objection being taken to it. Therefore, judgment was entered for the buyers.

GNR v Witham (1873)

GNR advertised for tenders for the supply of stores and W replied 'I undertake to supply the company for 12 months with such quantities as the company may order from time to time'. GNR accepted this tender and placed orders which W supplied. When W later refused to supply it was held that W's tender was a standing offer which GNR could accept by placing an order. W's refusal was a breach of contract but it also revoked W's standing offer for the future, so W did not have to meet any further orders.

Lord Denning in Entores v Miles Far East Corp (1955)

If a man shouts an offer to a man across a river but the reply is not heard because of a plane flying overhead, there is no contract. The offeree must wait and then shout back his acceptance so that the offeror can hear it.

Powell v Lee (1908)

The plaintiff applied for a job as headmaster and the school managers decided to appoint him. One of them, acting without authority, told the plaintiff he had been accepted. Later the managers decided to appoint someone else. The plaintiff brought an action alleging that by breach of a contract to employ him he had suffered damages in loss of salary. The county court judge held that there was no contract as there had been no authorised communication of intention to contract on the part of the body, that is, the managers, alleged to be a party to the contract. This decision was upheld by the King's Bench Division.

Felthouse v Bindley (1862)

The plaintiff discussed buying a horse from his nephew and wrote to him "If I hear no more about him, I consider the horse mine …" The nephew did not reply but wanted to sell the horse to the plaintiff, and when he was having a sale told the defendant auctioneer not to sell the horse. By mistake the defendant sold the horse. The plaintiff sued the defendant in the tort of conversion but could only succeed if he could show that the horse was his.

It was held that the uncle had no right to impose upon the nephew a sale of his horse unless he chose to comply with the condition of writing to repudiate the offer. It was clear that the nephew intended his uncle to have the horse but he had not communicated his intention to his uncle, or done anything to bind himself. Nothing, therefore, had been done to vest the property in the horse in the plaintiff. There had been no bargain to pass the property in the horse to the plaintiff, and therefore he had no right to complain of the sale.

Entores v Miles Far East Corp (1955)

The plaintiffs in London made an offer by Telex to the defendants in Holland. The defendant's acceptance was received on the plaintiffs' Telex machine in London. The plaintiffs sought leave to serve notice of a writ on the defendants claiming damages for breach of contract. Service out of the jurisdiction is allowed to enforce a contract made within the the jurisdiction. The Court of Appeal had to decide where the contract was made.

Denning L.J. stated that the rule about instantaneous communications between the parties is different from the rule about the post. The contract is only complete when the acceptance is received by the offeror: and the contract is made at the place where the acceptance is received. The contract was made in London where the acceptance was received. Therefore service could be made outside the jurisdiction.

The Brimnes (1975)

The defendants hired a ship from the plaintiff shipowners. The shipowners complained of a breach of the contract. The shipowners sent a message by Telex, withdrawing the ship from service, between 17.30 and 18.00 on 2 April. It was not until the following morning that the defendants saw the message of withdrawal on the machine.

Edmund-Davies L.J. agreed with the conclusion of the trial judge. The trial judge held that the notice of withdrawal was sent during ordinary business hours, and that he was driven to the conclusion either that the charterers' staff had left the office on April 2 'well before the end of ordinary business hours' or that if they were indeed there, they 'neglected to pay attention to the Telex machine in the way they claimed it was their ordinary practice to do.' He therefore concluded that the withdrawal Telex must be regarded as having been 'received' at 17.45 hours and that the withdrawal was effected at that time.

Note: Although this is a case concerning the termination of a contract, the same rule could apply to the withdrawal and acceptance of an offer.

Brinkibon v Stahag Stahl (1983)

The buyers, an English company, by a telex, sent from London to Vienna, accepted the terms of sale offered by the sellers, an Austrian company. The buyers issued a writ claiming damages for breach of the contract.

The House of Lords held that the service of the writ should be set aside because the contract had not been made within the court's jurisdiction. Lord Wilberforce stated that the present case is, as Entores itself, the simple case of instantaneous communication between principals, and, in accordance with the general rule, involves that the contract (if any) was made when and where the acceptance was received. This was in Vienna.

Adams v Lindsell (1818)

2 Sept. The defendant wrote to the plaintiff offering to sell goods asking for a reply "in the course of post"
5 Sept. The plaintiff received the letter and sent a letter of acceptance.
9 Sept. The defendant received the plaintiff's acceptance but on 8 Sept had sold the goods to a third party.

It was held that a binding contract was made when the plaintiff posted the letter of acceptance on 5 Sept, so the defendant was in breach of contract.

Household v Grant (1879)

G applied for shares in the plaintiff company. A letter of allotment of shares was posted but G never received it. When the company went into liquidation G was asked, as a shareholder, to contribute the amount still outstanding on the shares he held. The trial judge found for the plaintiff.

The Court of Appeal affirmed the judgment. Thesiger LJ stated that "Upon balance of conveniences and inconveniences it seems to me … it was more consistent with the acts and declarations of the parties in this case to consider the contract complete and absolutely binding on the transmission of the notice of allotment through the post, as the medium of

communication that the parties themselves contemplated, instead of postponing its completion until the notice had been received by the defendant."

Holwell Securities v Hughes (1974)

The defendant gave the plaintiff an option to buy property which could be exercised "by notice in writing". The plaintiffs posted a letter exercising this option but the letter was lost in the post and the plaintiffs claimed specific performance. The Court of Appeal held that the option had not been validly exercised. Lawton LJ stated that the plaintiffs were unable to do what the agreement said they were to do, namely, fix the defendant with knowledge that they had decided to buy his property. There was no room for the application of the postal rule since the option agreement stipulated what had to be done to exercise the option.

Tinn v Hoffman (1873)

Acceptance was requested by return of post. Honeyman J said: "That does not mean exclusively a reply by letter or return of post, but you may reply by telegram or by verbal message or by any other means not later than a letter written by return of post."

Yates v Pulleyn (1975)

The defendant granted the plaintiff an option to buy land, exercisable by notice in writing to be sent by "registered or recorded delivery post". The plaintiff sent a letter accepting this offer by ordinary post, which was received by the defendant who refused to accept it as valid.

It was held that this method of acceptance was valid and was no disadvantage to the offeror, as the method stipulated was only to ensure delivery and that had happened.

R v Clarke (1927) (Australia)

The Government offered a reward for information leading to the arrest of certain murderers and a pardon to an accomplice who gave the information. Clarke saw the proclamation. He gave information which led to the conviction of the murderers. He admitted that his only object in doing so was to clear himself of a charge of murder and that he had no intention of claiming the reward at that time. He sued the Crown for the reward. The High Court of Australia dismissed his claim. Higgins J stated that: "Clarke had seen the offer, indeed; but it was not present to his mind - he had forgotten it, and gave no consideration to it, in his intense excitement as to his own danger. There cannot be assent without knowledge of the offer; and ignorance of the offer is the same thing whether it is due to never hearing of it or forgetting it after hearing."

Williams v Carwardine (1833)

The defendant offered a reward for information leading to the conviction of a murderer. The plaintiff knew of this offer and gave information that it was her husband after he had beaten her, believing she had not long to live and to ease her conscience. It was held that the plaintiff was entitled to the reward as she knew about it and her motive in giving the information was irrelevant.

1.10 CASES ON TERMINATION OF A CONTRACT OFFER

Byrne v Van Tienhoven (1880)

1 Oct. D posted a letter offering goods for sale.
8 Oct. D revoked the offer; which arrived on 20 Oct.
11 Oct. P accepted by telegram
15 Oct. P posted a letter confirming acceptance.

It was held that the defendant's revocation was not effective until it was received on 20 Oct. This was too late as the contract was made on the 11th when the plaintiff sent a telegram. Judgment was given for the plaintiffs.

Dickinson v Dodds (1876)

Dodds offered to sell his house to Dickinson, the offer being open until 9am Friday. On Thursday, Dodds sold the house to Allan. Dickinson was told of the sale by Berry, the estate agent, and he delivered an acceptance before 9am Friday. The trial judge awarded Dickinson a decree of specific performance. The Court of Appeal reversed the decision of the judge.

James LJ stated that the plaintiff knew that Dodds was no longer minded to sell the property to him as plainly and clearly as if Dodds had told him in so many words, "I withdraw the offer." This was evident from the plaintiff's own statements. It was clear that before there was any attempt at acceptance by the plaintiff, he was perfectly well aware that Dodds had changed his mind, and that he had in fact agreed to sell the property to Allan. It was impossible, therefore, to say there was ever that existence of the same mind between the two parties which is essential in point of law to the making of an agreement.

Shuey v U.S. (1875)

On 20 April 1865, the Secretary of War published in the public newspapers and issued a proclamation, announcing that liberal rewards will be paid for any information that leads to the arrest of certain named criminals. The proclamation was not limited in terms to any specific period. On 24 November 1865, the President issued an order revoking the offer of the reward. In 1866 the claimant discovered and identified one of the named persons, and informed the authorities. He was, at all times, unaware that the offer of the reward had been revoked.

The claimant's petition was dismissed. It was held that the offer of a reward was revoked on 24 November and notice of the revocation was published. It was withdrawn through the same channel in which it was made. It was immaterial that the claimant was ignorant of the withdrawal. The offer of the reward not having been made to him directly, but by means of a published proclamation, he should have known that it could be revoked in the manner in which it was made.

Errington v Errington and Woods (1952)

A father bought a house on mortgage for his son and daughter-in-law and promised them that if they paid off the mortgage, they could have the house. They began to do this but before they had finished paying, the father died. His widow claimed the house. The daughter-in-law was granted possession of the house by the trial judge and the Court of Appeal.

Denning LJ stated: "The father's promise was a unilateral contract - a promise of the house in return for their act of paying the instalments. It could not be revoked by him once the couple entered on performance of the act, but it would cease to bind him if they left it incomplete and unperformed, which they have not done. If that was the position during the father's lifetime, so it must be after his death. If the daughter-in-law continues to pay all the building society instalments, the couple will be entitled to have the property transferred to them as soon as the mortgage is paid off; but if she does not do so, then the building society will claim the instalments from the father's estate and the estate will have to pay them. I cannot think that in those circumstances the estate would be bound to transfer the house to them, any more than the father himself would have been."

Daulia v Four Millbank Nominees (1978)

The defendant offered to sell property to the plaintiff. The parties agreed terms and agreed to exchange contracts. The defendant asked the plaintiff to attend at the defendant's office to exchange. The plaintiff attended but the defendant sold to a third party for a higher price. It was held that the contract fell foul of s40(1) Law of property Act 1925 and the plaintiff's claim was struck out. However, Goff L.J. stated obiter:

In unilateral contracts the offeror is entitled to require full performance of the condition imposed otherwise he is not bound. That must be subject to one important qualification - there must be an implied obligation on the part of the offeror not to prevent the condition being satisfied, an obligation which arises as soon as the offeree starts to perform. Until then the offeror can revoke the whole thing, but once the offeree has embarked on performance, it is too late for the offeror to revoke his offer.

Ramsgate v Montefiore (1866)

On 8 June, the defendant offered to buy shares in the plaintiff company. On 23 Nov, the plaintiff accepted but the defendant no longer wanted them and refused to pay. It was held that the six-month delay between the offer in June and the acceptance in November was unreasonable and so the offer had 'lapsed', ie it could no longer be accepted and the defendant was not liable for the price of the shares.

Financings Ltd v Stimson (1962)

The defendant at the premises of a dealer signed a form by which he offered to take a car on HP terms from the plaintiffs. He paid a deposit and was allowed to take the car away. He was dissatisfied with it and returned it to the dealer, saying he did not want it. The car was stolen from the dealer's premises and damaged. The plaintiffs, not having been told that the defendant had returned the car, signed the HP agreement.

It was held by the Court of Appeal (a) that the defendant had revoked his offer by returning the car to the dealer. (b) In view of an express provision in the form of the contract that the defendant had examined the car and satisfied himself that it was in good order and condition, the offer was conditional on the car remaining in substantially the same condition until the moment of acceptance. That condition not being fulfilled, the acceptance was invalid.

Bradbury v Morgan (1862)

JM Leigh requested Bradbury & Co to give credit to HJ Leigh, his brother. JM Leigh guaranteed his brother's account to the extent of £100. Bradbury thereafter credited HJ Leigh in the usual way of their business. JM Leigh died but Bradbury, having no notice or knowledge of his death, continued to supply HJ Leigh with goods on credit. JM Leigh's executors (Morgan) refused to pay, arguing that they were not liable as the debts were contracted and incurred after the death of JM Leigh and not in his lifetime. Judgment was given for the plaintiffs, Bradbury.

1.11 CONSIDERATION

INTRODUCTION

The mere fact of agreement alone does not make a contract. Both parties to the contract must provide consideration if they wish to sue on the contract. This means that each side must promise to give or do something for the other. (*Note*: if a contract is made by deed, then consideration is not needed.)

For example, if one party, A (the promisor) promises to mow the lawn of another, B (the promisee), A's promise will only be enforceable by B as a contract if B has provided consideration. The consideration from B might normally take the form of a payment of money but could consist of some other service to which A might agree. Further, the promise of a money payment or service in the future is just as sufficient a consideration as payment

itself or the actual rendering of the service. Thus the promisee has to give something in return for the promise of the promisor in order to convert a bare promise made in his favour into a binding contract.

DEFINITION

Lush J. in *Currie v Misa* (1875) LR 10 Exch 153 refered to consideration as consisting of a detriment to the promisee or a benefit to the promisor:

"… some right, interest, profit or benefit accruing to one party, or some forebearance, detriment, loss or responsibility given, suffered or undertaken by the other."

The definition given by Sir Frederick Pollock, approved by Lord Dunedin in *Dunlop v Selfridge Ltd* [1915] AC 847, is as follows:

"An act or forebearance of one party, or the promise thereof, is the price for which the promise of the other is bought, and the promise thus given for value is enforceable."

TYPES OF CONSIDERATION

1. EXECUTORY CONSIDERATION

Consideration is called "executory" where there is an exchange of promises to perform acts in the future, eg a bilateral contract for the supply of goods whereby A promises to deliver goods to B at a future date and B promises to pay on delivery. If A does not deliver them, this is a breach of contract and B can sue. If A delivers the goods his consideration then becomes executed.

2. EXECUTED CONSIDERATION

If one party makes a promise in exchange for an act by the other party, when that act is completed, it is executed consideration, eg in a unilateral contract where A offers £50 reward for the return of her lost handbag, if B finds the bag and returns it, B's consideration is executed.

RULES GOVERNING CONSIDERATION

1. CONSIDERATION MUST NOT BE PAST

If one party voluntarily performs an act, and the other party then makes a promise, the consideration for the promise is said to be in the past. The rule is that past consideration is no consideration, so it is not valid and cannot be used to sue on a contract. For example, A gives B a lift home in his car. On arrival B promises to give A £5 towards the petrol. A cannot enforce this promise as his consideration, giving B a lift, is past. See:

Re McArdle [1951] 1 All ER 905.

EXCEPTIONS TO THIS RULE:

(A) PREVIOUS REQUEST
If the promisor has previously asked the other party to provide goods or services, then a promise made after they are provided will be treated as binding. See:

Lampleigh v Braithwait (1615) Hob 105.

(B) BUSINESS SITUATIONS
If something is done in a business context and it is clearly understood by both sides that it will be paid for, then past consideration will be valid. See:

Re Casey's Patents [1892] 1 Ch 104.

Note: The principles in *Lampleigh v Braithwait* as interpreted in Re Casey's Patents were applied by the Privy Council in:

Pao On v Lau Yiu Long [1980] AC 614

(C) THE BILLS OF EXCHANGE ACT 1882
Under s27(1) it is provided that any antecedent debt or liability is valid consideration for a bill of exchange. For example, A mows B's lawn and a week later B gives A a cheque for £10. A's work is valid consideration in exchange for the cheque.

2. CONSIDERATION MUST BE SUFFICIENT
BUT NEED NOT BE ADEQUATE

Providing consideration has some value, the courts will not investigate its adequacy. Where consideration is recognised by the law as having some value, it is described as "real" or "sufficient" consideration. The courts will not investigate contracts to see if the parties have got equal value. See:

Chappell & Co Ltd v Nestle Co Ltd [1959] 2 All ER 701.

3. CONSIDERATION MUST MOVE FROM THE PROMISEE

The person who wishes to enforce the contract must show that they provided consideration; it is not enough to show that someone else provided consideration. The promisee must show that consideration "moved from" (ie, was provided by) him. The consideration does not have to move to the promisor. If there are three parties involved, problems may arise. See:

Price v Easton (1833) 4 B & Ad 433

4. FOREBEARANCE TO SUE

If one person has a valid claim against another (in contract or tort) but promises to forbear from enforcing it, that will constitute valid consideration if made in return for a promise by the other to settle the claim. See:

Alliance Bank v Broom (1864) 2 Dr & Sm 289.

5. EXISTING PUBLIC DUTY

If someone is under a public duty to do a particular task, then agreeing to do that task is not sufficient consideration for a contract. See:

Collins v Godefroy (1831) 1 B & Ad 950.

If someone exceeds their public duty, then this may be valid consideration. See:

Glassbrooke Bros v Glamorgan County Council [1925] AC 270.

6. EXISTING CONTRACTUAL DUTY

If someone promises to do something they are already bound to do under a contract, that is not valid consideration. Contrast:

Stilk v Myrick (1809) 2 Camp 317.
Hartley v Ponsonby (1857) 7 E & B 872.

The principle set out in *Stilk v Myrick* was amended by the following case. Now, if the performance of an existing contractual duty confers a practical benefit on the other party this can constitute valid consideration. See:

Williams v Roffey Bros Ltd [1990] 1 All ER 512.

7. EXISTING CONTRACTUAL DUTY OWED TO A THIRD PARTY

If a party promises to do something for a second party, but is already bound by a contract to do this for a third party, this is good consideration. See:

Scotson v Pegg (1861) 6 H & N 295.

8. PART PAYMENT OF A DEBT

1.12 CASES ON CONSIDERATION

Re McArdle (1951)

A wife and her three grown-up children lived together in a house. The wife of one of the children did some decorating and later the children promised to pay her £488 and they signed a document to this effect.

It was held that the promise was unenforceable as all the work had been done before the promise was made and was therefore past consideration.

Lampleigh v Braithwait (1615)

Braithwait killed someone and then asked Lampleigh to get him a pardon. Lampleigh got the pardon and gave it to Braithwait who promised to pay Lampleigh £100 for his trouble.

It was held that although Lampleigh's consideration was past (he had got the pardon) Braithwaite's promise to pay could be linked to Braithwaite's earlier request and treated as one agreement, so it could be implied at the time of the request that Lampleigh would be paid.

Re Casey's Patent (1892)

A and B owned a patent and C was the manager who had worked on it for two years. A and B then promised C a one-third share in the invention for his help in developing it. The patents were transferred to C but A and B then claimed their return.

It was held that C could rely on the agreement. Even though C's consideration was in the past, it had been done in a business situation, at the request of A and B and it was understood by both sides that C would be paid and the subsequent promise to pay merely fixed the amount.

Pao On v Lau Yiu Long (1980)

Lord Scarman said:

"An act done before the giving of a promise to make a payment or to confer some other benefit can sometimes be consideration for the promise. The act must have been done at the promisors' request: the parties must have understood that the act was to be remunerated either by a payment or the conferment of some other benefit: and payment, or the conferment of a benefit, must have been legally enforceable had it been promised in advance."

Chapple v Nestle (1959)

Nestle were running a special offer whereby members of the public could obtain a music record by sending off three wrappers from Nestle's chocolate bars plus some money. The copyright to the records was owned by Chapple, who claimed that there had been breaches of their copyright. The case turned round whether the three wrappers were part of the consideration. It was held that they were, even though they were then thrown away when received.

Price v Easton (1833)

Easton made a contract with X that in return for X doing work for him, Easton would pay Price £19. X did the work but Easton did not pay, so Price sued. It was held that Price's claim must fail, as he had not provided consideration.

Alliance Bank v Broom (1864)

The defendant owed an unsecured debt to the plaintiffs. When the plaintiffs asked for some security, the defendant promised to provide some goods but never produced them. When the plaintiffs tried to enforce the agreement for the security, the defendant argued that the plaintiffs had not provided any consideration.

It was held that normally in such a case, the bank would promise not to enforce the debt, but this was not done here. By not suing, however, the bank had shown forbearance and this was valid consideration, so the agreement to provide security was binding.

Collins v Godefroy (1831)

Godefroy promised to pay Collins if Collins would attend court and give evidence for Godefroy. Collins had been served with a subpoena (ie, a court order telling someone they must attend). Collins sued for payment. It was held that as Collins was under a legal duty to attend court he had not provided consideration. His action therefore failed.

Glassbrooke v GCC (1925)

The police were under a duty to protect a coal mine during a strike, and proposed mobile units. The mine owner promised to pay for police to be stationed on the premises. The police complied with this request but when they claimed the money, the mine owner refused to pay saying that the police had simply carried out their public duty.

It was held that although the police were bound to provide protection, they had a discretion as to the form it should take. As they believed mobile police were sufficient, they had acted over their normal duties. The extra protection was good consideration for the promise by the mine owner to pay for it and so the police were entitled to payment.

Stilk v Myrick (1809)

Two out of eleven sailors deserted a ship. The captain promised to pay the remaining crew extra money if they sailed the ship back, but later refused to pay.

It was held that as the sailors were already bound by their contract to sail back and to meet such emergencies of the voyage, promising to sail back was not valid consideration. Thus the captain did not have to pay the extra money.

Hartley v Ponsonby (1857)

When nineteen out of thirty-six crew of a ship deserted, the captain promised to pay the remaining crew extra money to sail back, but later refused to pay saying that they were only doing their normal jobs. In this case, however, the ship was so seriously undermanned that the rest of the journey had become extremely hazardous.

It was held that sailing the ship back in such dangerous conditions was over and above their normal duties. It discharged the sailors from their existing contract and left them free to enter into a new contract for the rest of the voyage. They were therefore entitled to the money.

Williams v Roffey (1990)

Roffey had a contract to refurbish a block of flats and had sub-contracted the carpentry work to Williams. After the work had begun, it became apparent that Williams had underestimated the cost of the work and was in financial difficulties. Roffey, concerned that the work would not be completed on time and that as a result they would fall foul of a

penalty clause in their main contract with the owner, agreed to pay Williams an extra payment per flat. Williams completed the work on more flats but did not receive full payment. He stopped work and brought an action for damages. In the Court of Appeal, Roffey argued that Williams was only doing what he was contractually bound to do and so had not provided consideration.

It was held that where a party to an existing contract later agrees to pay an extra "bonus" in order to ensure that the other party performs his obligations under the contract, then that agreement is binding if the party agreeing to pay the bonus has thereby obtained some new practical advantage or avoided a disadvantage. In the present case there were benefits to Roffey including (a) making sure Williams continued his work, (b) avoiding payment under a damages clause of the main contract if Williams was late, and (c) avoiding the expense and trouble of getting someone else. Therefore, Williams was entitled to payment.

Scotson v Pegg (1861)

Scotson contracted to deliver coal to X, or to X's order. X sold the coal to Pegg and ordered Scotson to deliver the coal to Pegg. Then Pegg promised Scotson that he would unload it at a fixed rate. In an action by Scotson to enforce Pegg's promise, Pegg argued that the promise was not binding because Scotson had not provided consideration as Scotson was bound by his contract with X (a third party) to deliver the coal.

It was held that Scotson's delivery of coal (the performance of an existing contractual duty to a third party, X) was a benefit to Pegg and was valid consideration. It could also been seen as a detriment to Scotson, as they could have broken their contract with X and paid damages.

1.13 PART-PAYMENT OF DEBTS

THE GENERAL RULE

If one person owes a sum of money to another and agrees to pay part of this in full settlement, the rule at common law (the rule in *Pinnel's Case* (1602) 5 CoRep 117a) is that part-payment of a debt is not good consideration for a promise to forgo the balance. Thus, if A owes B £50 and B accepts £25 in full satisfaction on the due date, there is nothing to prevent B from claiming the balance at a later date, since there is no consideration proceeding from A to enforce the promise of B to accept part-payment. This is because he is already bound to pay the full amount, an agreement based on the same principle as *Stilk v Myrick* (1809). It also protects a creditor from the economic duress of his debtor.

In *Pinnel's Case* (1602), Cole owed Pinnel £8-10s-0d (£8.50) which was due on 11 November. At Pinnel's request, Cole payed £5-2s-2d (£5.11) on 1 October, which Pinnel accepted in full

settlement of the debt. Pinnel sued Cole for the amount owed. It was held that part-payment in itself was not consideration. However, it was held that the agreement to accept part-payment would be binding if the debtor, at the creditor's request, provided some fresh consideration. Consideration might be provided if the creditor agrees to accept:

* part-payment on an earlier date than the due date (ie, as in Pinnel's Case itself); or
* chattel instead of money (a "horse, hawk or robe" may be more beneficial than money); or
* part-payment in a different place to that originally specified.

Despite its harshness the rule in *Pinnel's Case* was affirmed by the House of Lords and still represents the law:

In *Foakes v Beer* (1884) 9 App Cas 605, Mrs Beer had obtained judgment for a debt against Dr Foakes, who subsequently asked for time to pay. She agreed that she would take no further action in the matter provided that Foakes paid £500 immediately and the rest by half-yearly instalments of £150. Foakes duly kept to his side of the agreement. Judgment debts, however, carry interest. The House of Lords held that Mrs Beer was entitled to the £360 interest which had accrued. Foakes had not "bought" her promise to take no further action on the judgment. He had not provided any consideration.

The rule was recently applied by the Court of Appeal:

In *Re Selectmove* [1995] 2 All ER 531, Selectmove owed arrears of tax to the Inland Revenue. The IR was in a position to put Selectmove into liquidation because it was unable to meet its liabilities. There was a meeting at which Selectmove proposed to pay all future tax as and when it fell due and that it would pay off the arrears at the rate of £1,000 a month commencing the following February. The Collector of Taxes informed Selectmove that this proposal would need approval of his superiors; and that he would get back to them if it was not acceptable. Sometime later the IR commenced liquidation proceedings which Selectmove resisted, relying upon the agreement made at the meeting in July.
The Court of Appeal held, dismissing the defence (1) that a promise to pay a sum which the debtor was already bound to pay was not good consideration; (2) any promise made by the Collector of Taxes was made without actual or ostensible authority. Selectmove's attempt to use the notion in *Williams v Roffey Bros* (1990) failed as it was held that it was applicable only where the existing obligation which is pre-promised is one to supply goods or services, not where it is an obligation to pay money.

More recent cases include:

Ferguson v Davies (1996) The Independent December 12th 1996
Re C (a Debtor) [1996] BPLR 535

EXCEPTIONS TO THE RULE

Apart from the exceptions to the rule mentioned in *Pinnel's Case* itself, there are two others at common law and one exception in equity.

A) PART-PAYMENT OF THE DEBT BY A THIRD PARTY

A promise to accept a smaller sum in full satisfaction will be binding on a creditor where the part-payment is made by a third party on condition that the debtor is released from the obligation to pay the full amount. See:

Hirachand Punamchand v Temple [1911] 2 KB 330 - A father paid a smaller sum to a money lender to pay his son's debts, which the money lender accepted in full settlement. Later the money lender sued for the balance. It was held that the part-payment was valid consideration, and that to allow the moneylender's claim would be a fraud on the father.

B) COMPOSITION AGREEMENTS

The rule does not apply to composition agreements. This is an agreement between a debtor and a group of creditors, under which the creditors agree to accept a percentage of their debts (eg, 50p in the pound) in full settlement. Despite the absence of consideration, the courts will not allow an individual creditor to sue the debtor for the balance: *Wood v Robarts* (1818). The reason usually advanced for this rule is that to allow an individual creditor to claim the balance would amount to a fraud on the other creditors who had all agreed to the percentage.

C) PROMISSORY ESTOPPEL

This is the name that has been given to the equitable doctrine which has as its principal source the obiter dicta of Denning J in *High Trees House Ltd* [1947] (see below)

PROMISSORY ESTOPPEL

A further exception to the rule in *Pinnel's Case* is to be found in the equitable doctrine of promissory estoppel. The doctrine provides a means of making a promise binding, in certain circumstances, in the absence of consideration. The principle is that if someone (the promisor) makes a promise, which another person acts on, the promisor is stopped (or estopped) from going back on the promise, even though the other person did not provide consideration (in so far as is it is inequitable to do so).

DEVELOPMENT

The modern doctrine is largely based on dicta of Denning J in *Central London Property Trust Ltd v High Trees House Ltd* [1947] 1 KB 130 and on the decision of the House of Lords in *Tool Metal Manufacturing Co Ltd v Tungsten Electric Co Ltd* [1955] 1 WLR 761 and can be traced to *Hughes v Metropolitan Railway* (1877) 2 App Cas 439.

(a) *Hughes Case* (1877) - In October a landlord gave his tenant six months notice to repair and in the event of a failure to repair, the lease would be forfeited. In November the landlord opened negotiations for the sale of the premises, but these ended in December without agreement. Meanwhile the tenant had not done the repairs and when the six months period was up, the landlord sought possession.
The House of Lords held that the landlord could not do so. The landlord had, by his conduct, led the tenant to suppose that as long as negotiations went on, the landlord would not enforce the notice. He could not subsequently take advantage of the tenant relying on this. Therefore, the notice did not run during the period of negotiations. However, the six month period would begin to run again from the date of the breakdown of negotiations.

(b) *High Trees* (1947) - In 1937 the Ps granted a 99 year lease on a block of flats in London to the Ds at an annual rent of £2500. Because of the outbreak of war in 1939, the Ds could not get enough tenants and in 1940 the Ps agreed in writing to reduce the rent to £1250. After the war in 1945 all the flats were occupied and the Ps sued to recover the arrears of rent as fixed by the 1937 agreement for the last two quarters of 1945.
Denning J held that they were entitled to recover this money as their promise to accept only half was intended to apply during war conditions. This is the ratio decidendi of the case. He stated obiter, that if the Ps sued for the arrears from 1940-45, the 1940 agreement would have defeated their claim. Even though the Ds did not provide consideration for the Ps'

promise to accept half rent, this promise was intended to be binding and was acted on by the Ds. Therefore the Ps were estopped from going back on their promise and could not claim the full rent for 1940-45.

(c) *Tool Metal Case* (1955) - see below.

Thus it seems that if a person promises that he will not insist on his strict legal rights, and the promise is acted upon, then the law will require the promise to be honoured even though it is not supported by consideration.

REQUIREMENTS

The exact scope of the doctrine of promissory estoppel is a matter of debate but it is clear that certain requirements must be satisfied before the doctrine can come into play:

(A) CONTRACTUAL/LEGAL RELATIONSHIP

All the cases relied on by Denning J in *High Trees House* were cases of contract. However, in *Durham Fancy Goods v Michael Jackson (Fancy Goods)* [1968] 2 QB 839, Donaldson J said that an existing contractual relationship was not necessary providing there was "a pre-existing legal relationship which could, in certain circumstances, give rise to liabilities and penalties".

(B) PROMISE

There must be a clear and unambiguous statement by the promisor that his strict legal rights will not be enforced, ie one party must make a promise which is intended to be binding: *The Scaptrade* [1983] QB 529. However, it can be implied or made by conduct as in the *Hughes Case* (1877).

(C) RELIANCE

The promisee must have acted in reliance on the promise. There is some uncertainty as to whether the promisee (i) should have relied on the promise by changing his position to their detriment (ie, so that he is put in a worse position if the promise is revoked): *Ajayi v Briscoe* [1964] 1 WLR 1326, or (ii) whether they should have merely altered their position in some way, not necessarily for the worse.

In *Alan Co Ltd v El Nasr Export & Import Co* [1972] 2 QB 189, Lord Denning disclaimed detriment as an element of promissory estoppel, saying it was sufficient if the debtor acted on the promise by paying the lower sum. He said that "he must have been led to act differently from what he otherwise would have done".

(D) INEQUITABLE TO REVERT

It must be inequitable for the promisor to go back on his promise and revert to his strict legal rights. If the promisor's promise has been extracted by improper pressure it will not be inequitable for the promisor to go back on his promise. See:

D & C Builders v Rees [1965] 2 QB 617 - The Ps, a small building company, had completed some work for Mr Rees for which he owed the company £482. For months the company, which was in severe financial difficulties, pressed for payment. Eventually, Mrs Rees, who had become aware of the company's problems, contacted the company and offered £300 in full settlement. She added that if the company refused this offer they would get nothing. The company reluctantly accepted a cheque for £300 "in completion of the account" and later sued for the balance. The Court of Appeal held that the company was entitled to succeed. Lord Denning was of the view that it was not inequitable for the creditors to go back on their word and claim the balance as the debtor had acted inequitably by exerting improper pressure.

(E) A SHIELD OR A SWORD?

At one point it was said in *Coombe v Coombe* [1951] 2 KB 215 that the doctrine may only be raised as a defence: "as a shield and not a sword". It was held that the doctrine cannot be raised as a cause of action. This means that the doctrine only operates as a defence to a claim and cannot be used as the basis for a case. However, this was doubted in *Re Wyven Developments* [1974] 1 WLR 1097 by Templeman J, who appeared to think that this was no longer the case and that it could create rights. Lord Denning in *Evenden v Guildford City AFC* [1975] QB 917 also adopted this approach.

(F) EXTINCTIVE OR SUSPENSIVE OF RIGHTS?

Another question raised by this doctrine is whether it extinguishes rights or merely suspends them. The prevalent authorities are in favour of it merely suspending rights, which can be revived by giving reasonable notice or by conditions changing.

(a) Where the debtor's contractual obligation is to make periodic payments, the creditor's right to receive payments during the period of suspension may be permanently extinguished, but the creditor may revert to their strict contractual rights either upon giving reasonable notice, or where the circumstances which gave rise to the promise have changed as in *High Trees*. See:

Tool Metal Case (1955) - Patent owners promised to suspend periodic payments of compensation due to them from manufacturers from the outbreak of war. It was held by the House of Lords that the promise was binding during the period of suspension, but the owners could, on giving reasonable notice to the other party, revert to their legal entitlement to receive the compensation payments.

(b) It is not settled law that there can be no such resumption of payments in relation to a promise to forgo a single sum. In *D & C Builders*, which concerned liability for a single lump sum, Lord Denning expressed obiter that the court would not permit the promisor to revert to his strict legal right and that the estoppel would be final and permanent if the promise was intended and understood to be permanent in effect.

The preferred approach is to look at the nature of the promise: if as in *High Trees* and *Tool Metal*, it is intended to be temporary in application and to reserve to the promisor the right subsequently to reassert his strict legal rights, the effect will be suspensive only; and if on the other hand, it is intended to be permanent (as envisaged in *D & C Builders*), then there is no reason why in principle or authority the promise should not be given its full effect so as to extinguish the promisor's right.

1.14 INTENTION TO CREATE LEGAL RELATIONS

INTRODUCTION

The parties must intend the agreement to be legally binding. But how can the court find out what is in the parties' minds? The nearest the courts can get to discover this intention is to apply an objective test and judge the situation by what was said and done. The law divides agreements into two groups, social & domestic agreements and business agreements.

SOCIAL & DOMESTIC AGREEMENTS

This group covers agreements between family members, friends and workmates. The law presumes that social agreements are not intended to be legally binding. See, for example:

Lens v Devonshire Club (1914) The Times, December 4.

However, if it can be shown that the transaction had the opposite intention, the court may be prepared to rebut the presumption and to find the necessary intention for a contract. The cases show it is a difficult task to rebut such a presumption.

Agreements between a husband and wife living together as one household are presumed not to be intended to be legally binding, unless the agreement states to the contrary. See:

Balfour v Balfour [1919] 2 KB 571.

The presumption against a contractual intention will not apply where the spouses are not living together in amity at the time of the agreement. See:

Merritt v Merritt [1970] 2 All ER 760.

If a social agreement will have serious consequences for the parties, this may rebut the presumption. See:

Parker v Clarke [1960] 1 All ER 93.
Tanner v Tanner [1975] 1 WLR 1346.

It seems that agreements of a domestic nature between parent and child are likewise presumed not to be intended to be binding. See:

Jones v Padavatton [1969] 2 All ER 616.

Where the parties to the agreement share a household but are not related, the court will examine all the circumstances. See:

Simpkins v Pays [1955] 3 All ER 10.

BUSINESS/COMMERCIAL AGREEMENTS

In business agreements the presumption is that the parties intend to create legal relations and make a contract. This presumption can be rebutted by the inclusion of an express statement to that effect in the agreement. See:

Rose and Frank Co v Crompton Bros Ltd [1925] AC 445.

Similarly, football pools stated to be "binding in honour only" are not legal contracts so that a participant may not recover his winnings. See:

Jones v Vernons Pools [1938] 2 All ER 626.

Contractual intention may be negatived by evidence that "the agreement was a goodwill agreement … made without any intention of creating legal relations": *Orion Insurance v Sphere Drake Insurance* [1990] 1 Lloyd's Rep 465.

If a clause is put in an agreement and the clause is ambiguous then the courts will intervene and interpret it. See:

Edwards v Skyways [1964] 1 All ER 494.

Contractual intention may be negatived by the vagueness of a statement or promise. See:

JH Milner v Percy Bilton [1966] 1 WLR 1582.

There are situations where it would appear at first sight that the parties had entered into a commercial agreement, but, nevertheless, a contract is not created:

1. MERE PUFFS

For the purposes of attracting custom, tradesmen may make vague exaggerated claims in adverts. Such statements are essentially statements of opinion or "mere puff" and are not intended to form the basis of a binding contract. By contrast, more specific pledges such as, "If you can find the same holiday at a lower price in a different brochure, we will refund you the difference", are likely to be binding (See *Carlill's Case* [1893]).

A statement will not be binding if the court considers that it was not seriously meant. See:

Weeks v Tybald (1605) Noy 11.
Heilbut, Symons & Co v Buckleton (1913)

2. LETTERS OF COMFORT

This is a document supplied by a third party to a creditor, indicating a concern to ensure that a debtor meets his obligations to the creditor. Depending on the terms, such letters may be either binding contracts or informal and uncertain assurances resting entirely upon business goodwill. See

Kleinwort Benson v Malaysia Mining Corp [1989] 1 All ER 785.

3. LETTERS OF INTENT

This is a device by which one person indicates to another that he is likely to place a contract with him, but is not yet ready to be bound. A typical example of a situation where a letter of intent might be provided is where a main contractor is preparing a tender and he plans to sub-contract some of the work. He would need to know the cost of the sub-contracted work in order to calculate his own tender, but would not want to be committed to that sub-contractor until he knows whether his tender has been successful. In these circumstances, the main contractor writes to tell the sub-contractor that he has been chosen.

Where the language of such a letter does not negative contractual intention, the courts can hold the parties to be bound by the document. They will be inclined to do so where the parties have acted on the document for a long period of time or have expended considerable sums of money in reliance on it (*Turriff Constructuion v Regalia Knitting Mills* (1971) 22 EG 169 - letter of intent held to be a collateral contract for preliminary work).

4. COLLECTIVE AGREEMENTS

This is an agreement between a trade union and an employer regulating rates of pay and conditions of work. Section 179 of the Trade Union and Labour Relations (Consolidation) Act 1992 states that such agreements are not intended to be legally enforceable unless they are written and expressly affirm that they are to be binding.

"FREE" GIFTS

This section is for 'A' Level students as this issue has appeared on 'A' Level Law exam papers, but may also be of interest to ILEx students. Consider the following extract from John N. Adams & Roger Brownsword, *Understanding Contract Law*, Third Edition, p36-7:

"… in *Esso Petroleum Co. Ltd v Customs and Excise Commissioners* (1976), the question was whether Esso were liable to pay purchase tax on some promotional World Cup coins (advertised as "free" at Esso garages at the rate of one coin to every four gallons of petrol

purchased). For reasons which need not detain us, this question hinged on whether the coins were sold to the motorist. To this apparently simple question three different answers were offered.

One view (taken by the trial judge, Pennycuick V.-C., and by Lord Fraser who dissented in the House of Lords) was that the motorist had a straightforward contract for the coins as part of the undisputed contract for the purchase of petrol.

A second view (supported by the three members of the Court of Appeal, and by Viscount Dilhorne and Lord Russell in the House of Lords) was that the motorist had no contract for the coins, the coins being a gift. According to this interpretation, the promise to deliver the coins was not binding on Esso.

The third view (relied upon by Lords Wilberforce and Simon in the House of Lords, and given as an alternative interpretation by Lord Denning M.R. in the Court of Appeal and by Viscount Dilhorne and Lord Russell in the House of Lords) was that there were two contracts involved in the transaction: one a straightforward contract for the purchase of the petrol, and the other a so-called "collateral contract" concerning the coins. The terms of the suggested "collateral contract" concerning the coins were to the effect that the garage promised to give the motorist a coin in return for the motorist entering into a contract to buy four gallons of petrol, not, it should be noted, in return for the motorist promising to pay money for the coins as such. Although this collateral contract analysis treated the coins as the subject matter of a contract, it was agreed that under the definition of a "contract of sale goods" in the (then applicable) Sale of Goods Act 1893, this was not a contract of sale since the consideration for the coins under the contract was not money.

The upshot of this confusing saga was that the coins could be seen as the subject matter of a contract of sale (the first view above), or as a gift (the second view above), or as the subject matter of a contract which was not a contract of sale (the third view above). On the first view, Esso lost, but on either of the other two views, which were the views which prevailed, Esso won."

1.15 CASES ON INTENTION

1.15.1 SOCIAL & DOMESTIC AGREEMENTS

Lens v Devonshire Club (1914)

It was held that the winner of a competition held by a golf club could not sue for his prize where "no one concerned with that competition ever intended that there should be any

legal results flowing from the conditions posted and the acceptance by the competitor of those conditions".

Balfour v Balfour (1919)

The defendant who worked in Ceylon, came to England with his wife on holiday. He later returned to Ceylon alone, the wife remaining in England for health reasons. The defendant promised to pay the plaintiff £30 per month as maintenance, but failed to keep up the payments when the marriage broke up. The wife sued. It was held that the wife could not succeed because: (1) she had provided no consideration for the promise to pay £30; and (2) agreements between husbands and wives are not contracts because the parties do not intend them to be legally binding.

Merrit v Merrit (1970)

The husband left his wife. They met to make arrangements for the future. The husband agreed to pay £40 per month maintenance, out of which the wife would pay the mortgage. When the mortgage was paid off he would transfer the house from joint names to the wife's name. He wrote this down and signed the paper, but later refused to transfer the house.

It was held that when the agreement was made, the husband and wife were no longer living together, therefore they must have intended the agreement to be binding, as they would base their future actions on it. This intention was evidenced by the writing. The husband had to transfer the house to the wife.

Parker v Clarke (1960)

Mrs Parker was the niece of Mrs Clarke. An agreement was made that the Parkers would sell their house and live with the Clarkes. They would share the bills and the Clarkes would then leave the house to the Parkers. Mrs Clarke wrote to the Parkers giving them the details of expenses and confirming the agreement. The Parkers sold their house and moved in. Mr Clarke changed his will leaving the house to the Parkers. Later the couples fell out and the Parkers were asked to leave. They claimed damages for breach of contract.

It was held that the exchange of letters showed the two couples were serious and the agreement was intended to be legally binding because (1) the Parkers had sold their own home, and (2) Mr Clarke changed his will. Therefore the Parkers were entitled to damages.

Tanner v Tanner (1975)

A man promised a woman that the house in which they had lived together (without being married) should be available for her and the couple's children. It was held that the promise had contractual force because, in reliance on it, the woman had moved out of her rent-controlled flat.

Jones v Padavatton (1969)

In 1962, Mrs Jones offered a monthly allowance to her daughter if she would give up her job in America and come to England and study to become a barrister. Because of accommodation problems Mrs Jones bought a house in London where the daughter lived and received rents from other tenants. In 1967 they fell out and Mrs Jones claimed the house even though the daughter had not even passed half of her exams.

It was held that the first agreement to study was a family arrangement and not intended to be binding. Even if it was, it could only be deemed to be for a reasonable time, in this case five years. The second agreement was only a family agreement and there was no intention to create legal relations. Therefore, the mother was not liable on the maintenance agreement and could also claim the house.

Simpkins v Pays (1955)

The defendant, her granddaughter, and the plaintiff, a paying lodger shared a house. They all contributed one-third of the stake in entering a competition in the defendant's name. One week a prize of £750 was won but on the defendant's refusal to share the prize, the plaintiff sued for a third.

It was held that the presence of the outsider rebutted the presumption that it was a family agreement and not intended to be binding. The mutual arrangement was a joint enterprise to which cash was contributed in the expectation of sharing any prize.

1.15.2 BUSINESS/COMMERCIAL AGREEMENTS

Rose v Crompton Bros (1925)

The defendants were paper manufacturers and entered into an agreement with the plaintiffs whereby the plaintiffs were to act as sole agents for the sale of the defendant's paper in the US. The written agreement contained a clause that it was not entered into as a formal or legal agreement and would not be subject to legal jurisdiction in the courts but was a record of the purpose and intention of the parties to which they honourably pledged themselves, that it would be carried through with mutual loyalty and friendly co-operation. The plaintiffs placed orders for paper which were accepted by the defendants. Before the orders were sent, the defendants terminated the agency agreement and refused to send the paper.

It was held that the sole agency agreement was not binding owing to the inclusion of the "honourable pledge clause". Regarding the orders which had been placed and accepted, however, contracts had been created and the defendants, in failing to execute them, were in breach of contract.

Jones v Vernon Pools (1938)

The plaintiff claimed to have won the football pools. The coupon stated that the transaction was "binding in honour only". It was held that the plaintiff was not entitled to recover because the agreement was based on the honour of the parties (and thus not legally binding).

Edwards v Skyways (1964)

The plaintiff pilot was made redundant by the defendant. He had been informed by his pilots association that he would be given an ex gratia payment (ie, a gift). The defendant failed to pay and the pilot sued. The defendant argued that the use of the words "ex gratia" showed that there was no intention to create legal relations.

It was held that this agreement related to business matters and was presumed to be binding. The defendants had failed to rebut this presumption. The court also stated that the words "ex gratia" or "without admission of liability" are used simply to indicate that the party agreeing to pay does not admit any pre-existing liability on his part; but he is certainly not seeking to preclude the legal enforceability of the settlement itself by describing the payment as "ex gratia".

JH Milner v Percy Bilton (1966)

A property developer reached an "understanding" with a firm of solicitors to employ them in connection with a proposed development, but neither side entered into a definite commitment. The use of deliberately vague language was held to negative contractual intention.

Weeks v Tybald (1605)

The defendant "affirmed and published that he would give £100 to him that should marry his daughter with his consent." The court held that "It is not reasonable that the defendant should be bound by such general words spoken to excite suitors."

Heilbut, Symons & Co v Buckleton (1913)

The plaintiff said to the defendants' manager that he understood the defendants to be "bringing out a rubber company." The manager replied that they were, on the strength of which statement the plaintiff applied for, and was allotted, shares in the company. It turned out not to be a rubber company and the plaintiff claimed damages, alleging that the defendants had warranted that it was a rubber company. The claim failed as nothing said by the defendants' manager was intended to have contractual effect.

Kleinwort Benson v Malaysia Mining Corp (1989)

The plaintiff bank agreed with the defendants to lend money to a subsidiary of the defendants. As part of the arrangement, the defendants gave the plaintiffs a letter of comfort which stated that it was the company's policy to ensure that the business of its subsidiary is at all times in a position to meet its liabilities. The subsidiary went into liquidation and the plaintiffs claimed payment from the defendants.

It was held that the letters of comfort were statements of the company's present policy, and not contractual promises as to future conduct. They were not intended to create legal relations, and gave rise to no more than a moral responsibility on the part of the defendants to meet the subsidiary's debt.

Esso Petroleum Ltd v Commissioners of Customs and Excise [1976] 1 All ER 117

In 1970 the taxpayers ('Esso') devised a petrol sales promotion scheme. The scheme involved the distribution of millions of coins to petrol stations which sold Esso petrol. Each of the coins bore the likeness of one of the members of the English soccer team which went to Mexico in 1970 to play in the World Cup competition. The object of the scheme was that petrol station proprietors should encourage motorists to buy Esso petrol by offering to give away a coin for every four gallons of Esso petrol which the motorist bought. The coins were of little intrinsic value but it was hoped that motorists would persist in buying Esso petrol in order to collect the full set of 30 coins. The scheme was extensively advertised by Esso in the press and on television with phrases such as: 'Going free, at your Esso Action Station now', and: 'We are giving you a coin with every four gallons of Esso petrol you buy.' Folders were also circulated by Esso to petrol stations which stated, inter alia: 'One coin should be given to every motorist who buys four gallons of petrol - two coins for eight gallons and so on.' 4,900 petrol stations joined the scheme. Large posters were delivered by Esso to those stations, the most prominent lettering on the posters stating: 'The World Cup coins', 'One coin given with every four gallons of petrol'. The Customs and Excise Commissioners claimed that the coins were chargeable to purchase tax under s2(1) of the Purchase Tax Act 1963 on the ground that they had been 'produced in quantity for general sale' and therefore fell within Group 25 of Sch 1 to the 1963 Act.

Held (Lord Fraser of Tullybelton dissenting) - The coins had not been 'produced … for … sale', within Group 25 of Sch 1, and were not therefore chargeable for the following reasons -

(i) On the basis that the posters and other advertising material constituted an offer by the garage proprietors to enter into a contract with each customer to supply a coin with every four gallons of petrol sold, the contract envisaged was not a contract of 'sale', since the consideration for the transfer of the coins was not a money payment but the undertaking by the customer to enter into a collateral contract to purchase the appropriate quantity of Esso petrol.

(ii) (per Viscount Dilhorne and Lord Russell of Killowen, Lord Wilberforce and Lord Simon of Glaisdale dissenting) Furthermore, in the circumstances, and in particular in view of the fact that the coins were of little intrinsic value to customers, it could not be inferred that either Esso or the petrol station proprietors on the one hand, or the customers on the other, intended that there should be a legally binding contract to supply the coins to customers who bought the appropriate quantity of petrol. It followed that the coins had been produced for distribution by way of gift and not by way of sale.

1.16 PRIVITY OF CONTRACT

1. THE DOCTRINE OF PRIVITY

"The doctrine of privity means that a contract cannot, as a general rule, confer rights or impose obligations arising under it on any person except the parties to it." (GH Treitel, *The Law of Contract*)

The common law reasoned that:

1. Only a promisee may enforce the promise meaning that if the third party is not a promisee he is not privy to the contract. See:

> *Dunlop Tyre Co v Selfridge* [1915] AC 847 - The plaintiffs sold tyres to Dew & Co, wholesale distributors, on terms that Dew would obtain an undertaking from retailers that they should not sell below the plaintiffs' list price. Dew sold some of the tyres to the defendants, who retailed them below list price. The plaintiffs sought an injunction and damages. The action failed because although there was a contract between the defendants and Dew, the plaintiffs were not a party to it and "only a person who is a party to a contract can sue on it," (per Lord Haldane).

2. There is the principle that consideration must move from the promisee. See:

> *Tweddle v Atkinson* (1861) 1 B&S 393 - The fathers of a husband and wife agreed in writing that both should pay money to the husband, adding that the husband should have the power to sue them for the respective sums. The husband's claim against his wife's fathers' estate was dismissed, the court justifying the decision largely because no consideration moved from the husband.

The two principles of privity and consideration have become entwined but are still distinct.

2. EXCEPTIONS

If the doctrine of privity was inflexibly applied it would cause considerable injustice and inconvenience. Many exceptions to it have therefore been developed.

A) COLLATERAL CONTRACTS

A contract between two parties may be accompanied by a collateral contract between one of them and a third person relating to the same subject-matter. For example:

> *Shanklin Pier v Detel Products* [1951] 2 KB 854. The plaintiffs had employed contractors to paint a pier. They told them to buy paint made by the defendants. The defendants had told them that the paint would last for seven years. It only lasted for three months. The court decided that the plaintiffs could sue the defendants on a collateral contract. They had provided consideration for the defendants' promise by entering into an agreement with the contractors, which entailed the purchase of the defendants' paint.

There must, however, be an intention to create a collateral contract before that contract can be formed

B) AGENCY

The concept of agency is an exception to the doctrine of privity in that an agent may contract on behalf of his principal with a third party and form a binding contract between the principal and third party.

For example, a third party may be able to take the benefit of an exclusion clause by proving that the party imposing the clause was acting as the agent of the third party, thereby bringing the third party into a direct contractual relationship with the plaintiff:

> In *Scruttons Ltd v Midland Silicones Ltd* [1962] AC 446, a bill of lading limited the liability of a shipping company to $500 per package. The defendant stevedores had contracted with the shipping company to unload the plaintiff's goods on the basis that they were to be covered by the exclusion clause in the bill of lading. The plaintiffs were ignorant of the contract between the shipping company and the stevedores. Owing to the stevedores negligence, the cargo was damaged and, when sued, they pleaded the limitation clause in the bill of lading. The House of Lords held that the stevedores could not rely on the clause as there was no privity of contract between the plaintiffs and defendants.
>
> Lord Reid suggested that the stevedores could be brought into a contractual relationship with the owner of the goods through the agency of the carrier provided certain conditions were met: (1) that the bill of lading makes it clear that the stevedore is intended to be protected by the exclusion clauses therein. (2) that the bill of lading makes

> it clear that the carrier is contracting as agent for the stevedore. (3) the carrier must have authority from the stevedore to act as agent, or perhaps, later ratification by the stevedore would suffice. (4) consideration must move from the stevedore.

All of the above conditions were satisfied in *New Zealand Shipping v Satterthwaite (The Eurymedon)* [1975] AC 154.

C) TRUSTS

Equity developed a general exception to the doctrine of privity by use of the concept of trust. A trust is an equitable obligation to hold property on behalf of another.

> The device was approved by the House of Lords in *Les Affreteurs Reunis v Leopold Walford* [1919] AC 801, where a broker (C) negotiated a charterparty by which the shipowner (A) promised the charterer (B) to pay the broker a commission. It was held that B was trustee of this promise for C, who could thus enforce it against A.

However, the trust device has fallen into disuse because of the strict requirements of constituting a trust and most particularly that there should be a specific intention on the part of the person declaring the trust that it should be a trust.

D) RESTRICTIVE COVENANTS

Restrictive covenants may, if certain conditions are satisfied, run with the land and bind purchasers of it to observe the covenants for the benefit of adjoining owners.

> For example, in *Tulk v Moxhay* (1848) 2 Ph 774, the plaintiff who owned several houses in Leicester Square sold the garden in the centre to Elms, who covenanted that he would keep the gardens and railings in their present condition and continue to allow individuals to use the gardens. The land was sold to the defendants who knew of the restriction contained in the contract between the plaintiff and Elms. The defendant announced that he was going to build on the land, and the plaintiff, who still owned several adjacent houses, sought an injunction to restrain him from doing so. It was held that the covenant would be enforced in equity against all subsequent purchasers with notice.

This device was carried over into the law of contract by the Privy Council in *Lord Strathcona SS Co v Dominion Coal Co* [1926] AC 108, but Diplock J refused to follow the decision in *Port Line Ltd v Ben Line Steamers* [1958] 2 QB 146. Most recently, in *Law Debenture Trust Corp v Ural Caspian Oil Corp* [1993] 2 All ER 355, it was emphasised that the principle permitted no more than the grant of a negative injunction to restrain the person acquiring the property from doing acts which would be inconsistent with the performance of the contract by his predecesser and had

never been used to impose upon a purchaser a positive duty to perform the covenants of his predecessor.

E) STATUTES

Certain exceptions to the doctrine of privity have been created by statute, including price maintenance agreements; and certain contracts of insurance enforceable in favour of third parties. For example, under s148(4) of the Road Traffic Act 1972, an injured party may recover compensation from an insurance company once he has obtained judgment against the insured person.

F) REMEDIES OF THE CONTRACTING PARTY

The question of the extent to which a contracting party may recover for loss sustained by a third party who is intended to benefit from the contract was raised in:

> *Jackson v Horizon Holidays* [1975] 1 WLR 1468. The plaintiff entered into a contract for himself and his family. The holiday provided failed to comply with the description given by the defendants in a number of respects. The plaintiff recovered damages and the defendants appealed against the amount. Lord Denning MR thought the amount awarded was excessive compensation for the plaintiff himself, but he upheld the award on the ground that the plaintiff had made a contract for the benefit of himself and his family, and that he could recover for their loss as well as for his own.

However, in *Woodar Investment Development v Wimpey Construction* [1980] 1 WLR 277, the House of Lords rejected the basis on which Lord Denning had arrived at his decision, and reaffirmed the view that a contracting party cannot recover damages for the loss sustained by the third party. Their Lordships did not dissent from the actual decision in Jackson, which they felt could be supported either because the damages were awarded for the plaintiff's own loss; or because booking family holidays or ordering meals in restaurants calls for special treatment.

3. ACADEMIC DEBATE ON THE DOCTRINE

GH Treitel, *The Law of Contract*, 9th ed, 1995, p588, states:
"The rule that no one except a party to a contract can be made liable under it is generally regarded as just and sensible. But the rule that no one except a party to a contract can enforce it may cause inconvenience where it prevents the person most interested in enforcing the contract from doing so. The many exceptions to the doctrine make it tolerable in practice, but they have provoked the question whether it would not be better further to modify the doctrine or to abolish it altogether."

4. REFORM

Proposals for legislative reform were made by the Law Revision Committee as long ago as 1937 (Cmnd. 5449) and further proposals were put forward for discussion by the Law Commission in 1991 (Paper No 121, 1991). In July 1996, the Law Commission published proposals in "Privity of Contract; Contracts for the Benefit of Third Parties" (Cmnd. 3329; Law Com No 242), which recommended that the law

expressly provide for third parties to be able to enforce contracts (including taking advantage of exclusion/limitation clauses) in certain circumstances. These proposals for reform were acted upon.
The Contracts (Rights of Third Parties) Act 1999 received Royal Assent on 11 November 1999. It reforms the common law rule of privity of contract. Section 1 provides that a third party may in his own right enforce a term of a contract if:

> (a) the contract expressly provides that he may, or
> (b) the term purports to confer a benefit on him (except where on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party).

There shall be available to the third party any remedy that would have been available to him in an action for breach of contract if he had been a party to the contract: s1(5).

1.17 MISREPRESENTATION

INTRODUCTION

A misrepresentation is a false statement of fact made by one party to another, which, whilst not being a term of the contract, induces the other party to enter the contract.

The effect of an actionable misrepresentation is to make the contract voidable, giving the innocent party the right to rescind the contract and/or claim damages.

1. FALSE STATEMENT OF FACT

An actionable misrepresentation must be a false statement of fact, not opinion or future intention or law.

(A) STATEMENTS OF OPINION

A false statement of opinion is not a misrepresentation of fact. See:

> *Bisset v Wilkinson* [1927] AC 177.

However, where the person giving the statement was in a position to know the true facts and it can be proved that he could not reasonably have held such a view as a result, then his opinion will be treated as a statement of fact. See:

Smith v Land & House Property Corp. (1884) 28 Ch D 7.

Some expressions of opinion are mere puffs. Thus, in *Dimmock v Hallet* (1866) 2 Ch App 21, the description of land as 'fertile and improvable' was held not to constitute a representation.

(B) STATEMENTS AS TO THE FUTURE

A false statement by a person as to what he will do in the future is not a misrepresentation and will not be binding on a person unless the statement is incorporated into a contract.

However, if a person knows that his promise, which has induced another to enter into a contract, will not in fact be carried out then he will be liable. See:

Edgington v Fitzmaurice (1885) 29 Ch D 459
Esso Petroleum v Mardon [1976] QB 801.

(C) STATEMENTS OF THE LAW

A false statement as to the law is not actionable misrepresentation because everyone is presumed to know the law. However, the distinction between fact and law is not simple. See:

Solle v Butcher [1950] 1 KB 671.

(D) SILENCE

Generally, silence is not a misrepresentation. The effect of the maxim caveat emptor is that the other party has no duty to disclose problems voluntarily. Thus if one party is labouring under a misapprehension there is no duty on the other party to correct it. See:

Smith v Hughes (1871) LR 6 QB 597.

However, there are three fundamental exceptions to this rule:

(i) HALF TRUTHS

The representor must not misleadingly tell only part of the truth. Thus, a statement that does not present the whole truth may be regarded as a misrepresentation. See:

Nottingham Brick & Tile Co. v Butler (1889) 16 QBD 778.

(ii) STATEMENTS WHICH BECOME FALSE

Where a statement was true when made out but due to a change of circumstances has become false by the time it is acted upon, there is a duty to disclose the truth. See:

With v O'Flanagan [1936] Ch 575.

(iii) CONTRACTS UBERRIMAE FIDEI

Contracts uberrimae fidei (contracts of the utmost good faith) impose a duty of disclosure of all material facts because one party is in a strong position to know the truth. Examples would include contracts of insurance and family settlements.

A material fact is something which would influence a reasonable person in making the contract. If one party fails to do this, the contract may be avoided. See:

Lambert v Co-Operative Insurance Society [1975] 2 Lloyd's Rep 485.

Where there is a fiduciary relationship between the parties to a contract a duty of disclosure will arise, eg, solicitor and client, bank manager and client, trustee and beneficiary, and inter-family agreements.

(E) OTHER REPRESENTATIONS

The term 'statement' is not to be interpreted too literally:
* In *Gordon v Selico Ltd* (1986) 278 EG 53, it was held that painting over dry rot, immediately prior to sale of the property, was a fraudulent misrepresentation.
* In *St Marylebone Property v Payne* (1994) 45 EG 156, the use of a photograph taken from the air, printed with arrows (misleadingly) indicating the extent of land boundaries, was held to convey a statement of fact (which amounted to actionable misrepresentation).

2. THE MISREPRESENTATION MUST HAVE INDUCED THE CONTRACT

The false statement must have induced the representee to enter into the contract. The requirements here are that (a) the misrepresentation must be material and (b) it must have been relied on.

(A) MATERIALITY

The misrepresentation must be material, in the sense that it would have induced a reasonable person to enter into the contract. However, the rule is not strictly objective:
In *Museprime Properties v Adhill Properties* [1990] 36 EG 114, the judge referred, with approval, to the view of *Goff and Jones: Law of Restitution* that, any misrepresentation which induces a person to enter into a contract should be a ground for rescission of that contract. If the misrepresentation would have induced a reasonable person to enter into the contract, then the court will presume that the representee was so induced, and the onus will be on the representor to show that the representee did not rely on the misrepresentation either wholly or in part. If, however, the misrepresentation would not have induced a reasonable person to contract, the onus will be on the misrepresentee to show that the misrepresentation induced him to act as he did. See:

Museprime Properties v Adhill Properties [1990] 36 EG 114.

(B) RELIANCE

The representee must have relied on the misrepresentation.
There will be no reliance if the misrepresentee was unaware of the misrepresentation. See:

Horsfall v Thomas [1862] 1 H&C 90.

There will be no reliance if the representee does not rely on the misrepresentation but on his own judgment or investigations. See:

Attwood v Small (1838) 6 Cl & F 232.

(*Note*: this rule does not apply where the misrepresentation was fraudulent and the representee was asked to check the accuracy of the statement: *Pearson v Dublin Corp* [1907] AC 351.)
There will be reliance even if the misrepresentee is given an opportunity to discover the truth but does not take the offer up. The misrepresentation will still be considered as an inducement. See:

Redgrave v Hurd (1881) 20 Ch D 1.

There will be reliance even if the misrepresentation was not the only inducement for the representee to enter into the contract. See:

Edgington v Fitzmaurice (above)

3. TYPES OF MISREPRESENTATION

Once misrepresentation has been established it is necessary to consider what type of misrepresentation has been made. There are three types of misrepresentation: fraudulent, negligent and wholly innocent. The importance of the distinction lies in the remedies available for each type.

(A) FRAUDULENT MISREPRESENTATION

Fraudulent misrepresentation was defined by Lord Herschell in *Derry v Peek* (1889) as a false statement that is "made (i) knowingly, or (ii) without belief in its truth, or (iii) recklessly, careless as to whether it be true or false." Therefore, if someone makes a statement which they honestly believe is true, then it cannot be fraudulent. See:

Derry v Peek (1889) 14 App Cas 337.

The burden of proof is on the plaintiff - he who asserts fraud must prove it. Tactically, it may be difficult to prove fraud, in the light of Lord Herschell's requirements.
The remedy is rescission (subject to exceptions discussed later) and damages in the tort of deceit (see later).

(B) NEGLIGENT MISREPRESENTATION

This is a false statement made by a person who had no reasonable grounds for believing it to be true. There are two possible ways to claim: either under common law or statute.

(i) NEGLIGENT MISSTATEMENT AT COMMON LAW
The House of Lords have held that in certain circumstances damages may be recoverable in tort for negligent misstatement causing financial loss:

> *Hedley Byrne v Heller* [1964] AC 465.

Success depends upon proof of a special relationship existing between the parties. Such a duty can arise in a purely commercial relationship where the representor has (or purports to have) some special skill or knowledge and knows (or it is reasonable for him to assume) that the representee will rely on the representation. See:

> *Esso Petroleum v Mardon* [1976] (above)
> *Williams v Natural Life Health Foods* (1998) TheTimes, May 1.

The remedies are rescission (subject to exceptions discussed later) and damages in the tort of negligence (see later).

(ii) NEGLIGENT MISREPRESENTATION
UNDER s2(1) MISREPRESENTATION ACT 1967
Section 2(1) of the Misrepresentation Act 1967 provides:

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

This provision does not require the representee to establish a duty of care and reverses the burden of proof. Once a party has proved that there has been a misrepresentation which induced him to enter into the contract, the person making the misrepresentation will be liable in damages unless he proves he had reasonable grounds to believe and did believe that the facts represented were true. This burden may be difficult to discharge as shown in:

> *Howard Marine & Dredging Co v Ogden & Sons* [1978] QB 574.

Remedies: recent case-law has shown that the remedies available are as those available in fraud unless the representor discharges the burden of proof. In particular,

damages will be based in the tort of deceit rather than the tort of negligence (see later).

(C) WHOLLY INNOCENT MISREPRESENTATION
This is a false statement which the person makes honestly believing it to be true. The remedy is either (i) rescission with an indemnity, or (ii) damages in lieu of rescission under the courts discretion in s2(2) Misrepresentation Act 1967 (see below).

4. REMEDIES FOR MISREPRESENTATION

Once an actionable misrepresentation has been established, it is then necessary to consider the remedies available to the misrepresentee.

(A) RESCISSION
Rescission, ie setting aside the contract, is possible in all cases of misrepresentation. The aim of rescission is to put the parties back in their original position, as though the contract had not been made.
The injured party may rescind the contract by giving notice to the representor. However, this is not always necessary as any act indicating repudiation, eg notifying the authorities, may suffice. See:

Car & Universal Finance v Caldwell [1965] 1 QB 525.

BARS TO RESCISSION:
Rescission is an equitable remedy and is awarded at the discretion of the court. The injured party may lose the right to rescind in the following four circumstances:

(i) AFFIRMATION OF THE CONTRACT

The injured party will affirm the contract if, with full knowledge of the misrepresentation and of their right to rescind, they expressly state that they intend to continue with the contract, or if they do an act from which the intention may be implied. See:

Long v Lloyd [1958] 1 WLR 753.

Note that in *Peyman v Lanjani* [1985] Ch 457, the Court of Appeal held that the plaintiff had not lost his right to rescind because, knowing of the facts which afforded this right, he proceeded with the contract, unless he also knew of the right to rescind. The plaintiff here did not know he had such right. As he did not know he had such right, he could not be said to have elected to affirm the contract.

(ii) LAPSE OF TIME

If the injured party does not take action to rescind within a reasonable time, the right will be lost.

Where the misrepresentation is fraudulent, time runs from the time when the fraud was, or with reasonable diligence could have been discovered. In the case of non-fraudulent misrepresentation, time runs from the date of the contract, not the date of discovery of the misrepresentation. See:

Leaf v International Galleries [1950] 2 KB 86.

(iii) RESTITUTION IN INTEGRUM IMPOSSIBLE

The injured party will lose the right to rescind if substantial restoration is impossible, ie if the parties cannot be restored to their original position. See:

Vigers v Pike (1842) 8 CI&F 562.

Precise restoration is not required and the remedy is still available if substantial restoration is possible. Thus, deterioration in the value or condition of property is not a bar to rescission:

Armstrong v Jackson [1917] 2 KB 822.

(iv) THIRD PARTY ACQUIRES RIGHTS

If a third party acquires rights in property, in good faith and for value, the misrepresentee will lose their right to rescind. See: Phillips v Brooks [1919] 2 KB 243 under Mistake.

Thus, if A obtains goods from B by misrepresentation and sells them to C, who takes in good faith, B cannot later rescind when he discovers the misrepresentation in order to recover the goods from C.

(v) NOTE:

The right to rescind the contract will also be lost if the court exercises its discretion to award damages in lieu of rescission under s2(2) of the Misrepresentation Act 1967.

For innocent misrepresentation two previous bars to rescission were removed by s1 of the Misrepresentation Act 1967: the misrepresentee can rescind despite the misrepresentation becoming a term of the contract (s1(a)), and the misrepresentee can rescind even if the contract

has been executed (s1(b)). Generally, this will be relevant to contracts for the sale of land and to tenancies.

(B) INDEMNITY

An order of rescission may be accompanied by the court ordering an indemnity. This is a money payment by the misrepresentor in respect of expenses necessarily created in complying with the terms of the contract and is different from damages. See:

Whittington v Seale-Hayne (1900) 82 LT 49.

(C) DAMAGES

(i) FRAUDULENT MISREPRESENTATION

The injured party may claim damages for fraudulent misrepresentation in the tort of deceit. The purpose of damages is to restore the victim to the position he occupied before the representation had been made.

The test of remoteness in deceit is that the injured party may recover for all the direct loss incurred as a result of the fraudulent misrepresentation, regardless of foreseeability:

Doyle v Olby (Ironmongers) Ltd [1969] 2 QB 158
Smith New Court Securities v Scrimgeour Vickers [1996] 4 All ER 769.

Moreover, damages may include lost opportunity costs, eg loss of profits. See:

East v Maurer [1991] 2 All ER 733.

In *Archer v Brown* [1984] 2 All ER 267, the court held that the plaintiff was entitled to aggravated damages in deceit for the distress he had suffered.

The claimant will not be entitled to recover damages after the date he discovered the misrepresentation and had an opportunity to avoid further loss:

Downs v Chappell [1996] 3 All ER 344.

(ii) NEGLIGENT MISREPRESENTATION

The injured party may elect to claim damages for negligent misrepresentation at common law. The test of remoteness in the tort of negligence is that the injured party may recover for only reasonably foreseeable loss (*Esso Petroleum v Mardon* [1976] QB 801).

Alternatively, the injured party may claim damages for negligent misrepresentation under s2(1) of the Misrepresentation Act 1967. This will be the normal course to pursue as s2(1) reverses the burden of proof. Damages will be assessed on the same basis as fraudulent misrepresentation rather than the tort of negligence, ie 'direct consequence' rather than 'reasonable foreseeability'. See:

Royscott Trust Ltd v Rogerson [1991] 3 WLR 57

(iii) WHOLLY INNOCENT MISREPRESENTATION

In cases of non-fraudulent misrepresentation, s2(2) of the Misrepresentation Act 1967 gives the court a discretion, where the injured party would be entitled to rescind, to award damages in lieu of rescission. Damages under s2(2) cannot be claimed as such; they can only be awarded by the court. Section 2(2) states:
"Where a person has entered into a contract after a misrepresentation has been made to him otherwise than fraudulently, and he would be entitled, by reason of the misrepresentation, to rescind the contract, then, if it is claimed, in any proceedings arising out of the contract, that the contract ought to be or has been rescinded the court or arbitrator may declare the contract subsisting and award damages in lieu of rescission, if of opinion that it would be equitable to do so, having regard to the nature of the misrepresentation and the loss that would be caused by it if the contract were upheld, as well as to the loss that rescission would cause to the other party."
It is not clear from the above words if the right to damages will be lost if the representee has lost the right to rescind (See Cheshire & Fifoot, p301-2; Treitel, p333). According to *Thomas Witter v TBP Industries* (1996) (below), this will not be a bar provided the plaintiff had such a right in the past.
It is not yet clear what the measure of damages is under s2(2):

· According to Treitel (p337) and to Chitty, damages under s2(2) may be lower than the damages awarded under s2(1). Chitty suggests the possibility of a special measure to compensate the injured party for the loss of the right to rescind.
· According to Cheshire & Fifoot, compensation should be limited to an indemnity (p305). This was in substance the view taken by the High Court in:

Thomas Witter v TBP Industries [1996] 2 All ER 573.

5. EXCLUDING LIABILITY FOR MISREPRESENTATION

Any term of a contract which excludes liability for misrepresentation or restricts the remedy available is subject to the test of reasonableness. Section 3 of the Misrepresentation Act 1967, as amended by s8 of UCTA 1977, provides that:

"If a contract contains a term which would exclude or restrict:
a) any liability to which a party to a contract may be subject by reason of any misrepresentation made by him before the contract was made; or
b) any remedy available to another party to the contract by reason of such a misrepresentation,
that term shall be of no effect except insofar as it satisfies the requirement of reasonableness as stated in s11(1) of the Unfair Contract Terms Act 1977; and it is for those claiming that the term satisfies that requirement to show that it does."

(Section 11(1) UCTA 1977 provides that "… the term shall have been a fair and reasonable one to be included having regard to the circumstances which were, or

ought reasonably to have been, known to or in the contemplation of the parties when the contract was made.")

1.18 CASES ON MISREPRESENTATION

1. FALSE STATEMENT OF FACT

Bisset v Wilkinson [1927] AC 177

The plaintiff purchased from the defendant two blocks of land for the purpose of sheep farming. During negotiations the defendant said that if the place was worked properly, it would carry 2,000 sheep. The plaintiff bought the place believing that it would carry 2,000 sheep. Both parties were aware that the defendant had not carried on sheep-farming on the land. In an action for misrepresentation, the trial judge said:

"In ordinary circumstances, any statement made by an owner who has been occupying his own farm as to its carrying capacity would be regarded as a statement of fact. … This, however, is not such a case. … In these circumstances … the defendants were not justified in regarding anything said by the plaintiff as to the carrying capacity as being anything more than an expression of his opinion on the subject."

The Privy Council concurred in this view of the matter, and therefore held that, in the absence of fraud, the purchaser had no right to rescind the contract.

Smith v Land & House Property Corp (1884) 28 Ch D 7

The plaintiff put up his hotel for sale stating that it was let to a 'most desirable tenant'. The defendants agreed to buy the hotel. The tenant was bankrupt. As a result, the defendants refused to complete the contract and were sued by the plaintiff for specific performance. The Court of Appeal held that the plaintiff's statement was not mere opinion, but was one of fact.

Edgington v Fitzmaurice (1885) 29 Ch D 459

The plaintiff shareholder received a circular issued by the directors requesting loans to the amount of £25,000 with interest. The circular stated that the company had bought a lease of a valuable property. Money was needed for alterations of and additions to the property and to transport fish from the coast for sale in London. The circular was challenged as being misleading in certain respects. It was alleged, inter alia, that it was framed in such a way as to lead to the belief that the debentures would be a charge on the property of the company, and that the whole object of the issue was to pay off pressing liabilities of the company, not to complete the alterations, etc. The plaintiff who had taken debentures, claimed repayment

of his money on the ground that it had been obtained from him by fraudulent mis-statements.

The Court of Appeal held that the statement of intention was a statement of fact and amounted to a misrepresentation and that the plaintiff was entitled to rescind the contract. Although the statement was a promise of intent the court held that the defendants had no intention of keeping to such intent at the time they made the statement.

Esso Petroleum v Mardon [1976] QB 801

Esso's experienced representative told Mardon that Esso estimated that the throughput of petrol on a certain site would reach 200,000 gallons in the third year of operation and so persuaded Mardon to enter into a tenancy agreement in April 1963 for three years. Mardon did all that could be expected of him as tenant but the site was not good enough to achieve a throughput of more than 60,000-70,000 gallons. Mardon lost money and was unable to pay for petrol supplied. Esso claimed possession of the site and money due. Mardon claimed damages in respect of the representation alleging that it amounted to (i) a warranty; and (ii) a negligent misrepresentation.

The Court of Appeal affirmed the finding of negligence under the principle of Hedley Byrne v Heller (1964). On the issue of warranty, Lord Denning MR stated:

"… it was a forecast made by a party, Esso, who had special knowledge and skill. It was the yardstick (the "e a c") by which they measured the worth of a filling station. They knew the facts. They knew the traffic in the town. They knew the throughput of comparable stations. They had much experience and expertise at their disposal. They were in a much better position than Mr Mardon to make a forecast. It seems to me that if such a person makes a forecast -intending that the other should act on it and he does act on it- it can well be interpreted as a warranty that the forecast is sound and reliable in this sense that they made it with reasonable care and skill. … If the forecast turned out to be an unsound forecast, such as no person of skill or experience should have made, there is a breach of warranty."

Solle v Butcher [1950] 1 KB 671

In 1931 a dwelling house had been converted into five flats. In 1938 Flat No. 1 was let for three years at an annual rent of £140. In 1947 the defendant took a long lease of the building, intending to repair bomb damage and do substantial alterations. The plaintiff and defendant discussed the rents to be charged after the work had been completed. The plaintiff told the defendant that he could charge £250 for Flat 1. The plaintiff paid rent at £250 per year for some time and then took proceedings for a declaration that the standard rent was £140. The defendant contended that the flat had become a new and separate dwelling by reason of change of identity, and therefore not subject to the Rent Restriction Acts. This was held to be a statement of fact. (Note: this is a case on Mistake.)

Smith v Hughes (1871) LR 6 QB 597

The plaintiff farmer asked the manager of the defendant, who was a trainer of racehorses, if he would like to buy some oats, and showed him a sample. The manager wrote to say that he would take the whole quantity. The plaintiff delivered a portion of them. The defendant complained that the oats were new oats, whereas he thought he was buying old oats, new oats being useless to him. The plaintiff, who knew that the oats were new, refused to take them back and sued for the price. There was a conflict of evidence as to what took place between the plaintiff and the manager. The court ordered a new trial. Blackburn J stated:

"… on the sale of a specific article, unless there be a warranty making it part of the bargain that it possesses some particular quality, the purchaser must take the article he has bought, though it does not possess that quality. And I agree that, even if the vendor was aware that the purchaser thought that the article possessed that quality, and would not have entered into the contract unless he had so thought, still the purchaser is bound, unless the vendor was guilty of some fraud or deceit upon him. A mere abstinence from disabusing the purchaser of that impression is not fraud or deceit, for, whatever may be the case in a court of morals, there is no legal obligation on the vendor to inform the purchaser that he is under a mistake which has not been induced by the act of the vendor."

Nottingham Brick & Tile Co v Butler (1889) 16 QBD 778

The buyer of land asked the seller's solicitor if there were any restrictive covenants on the land and the solicitor said he did not know of any. He did not say that he had not bothered to read the documents. The court held that even though the statement was literally true it was a misrepresentation. There were restrictive covenants and the contract could be rescinded.

With v O'Flanagan [1936] Ch 575

During the course of negotiations for the sale of a medical practice, the vendor made representations to the purchaser that it was worth £2000 a year. By the time when the contract was signed, they were untrue. The value of the practice had declined in the meantime (to £250) because of the vendor's inability to attend to it through illness. Lord Wright MR quoted:

"So again, if a statement has been made which is true at the time, but which during the course of negotiations becomes untrue, then the person who knows that it has become untrue is under an obligation to disclose to the other the change of circumstances."

Therefore, the failure of the vendor to disclose the state of affairs to the purchaser amounted to a misrepresentation.

Lambert v Co-Operative Insurance [1975] 2 Lloyd's Rep 485

In 1963 Mrs Lambert signed a proposal form for an insurance policy to cover her own and her husband's jewellery. No questions were asked about previous convictions and Mrs L gave no information about them. She knew that her husband had been convicted some years earlier of stealing cigarettes and fined £25. The company issued a policy providing that it should be void if there was an omission to state any fact material to the risk. The policy was renewed from year to year. In 1971 the husband was convicted of conspiracy to steal and theft and sentenced to 15 months imprisonment. Mrs L knew of the conviction but did not disclose it and the policy was renewed. In 1972, seven items of the insured jewellery, valued at £311, were lost or stolen.

Mrs L's claim was repudiated on the grounds that she had failed to disclose her husband's first and second convictions. The judge dismissed the wife's claim on the ground that the 1971 conviction was a material fact and that a prudent insurer, knowing of it, would not have continued the risk. This decision was upheld by the Court of Appeal.

2. THE MISREPRESENTATION MUST HAVE INDUCED THE CONTRACT

Museprime Properties v Adhill Properties [1990] 36 EG 114

In a sale by auction of three properties the particulars wrongly represented the rents from the properties as being open to negotiation. The statements in the auction particulars and made later by the auctioneer misrepresented the position with regard to rent reviews. In fact, on two of the three properties rent reviews had been triggered and new rents agreed. The plaintiff company successfully bid for the three properties and discovered the true situation. They commenced an action for rescission. The defendant company countered with the defence that the misrepresentations were not such as to induce any reasonable person to enter into the contract.

It was held that the plaintiff's had established, and indeed that the defendants conceded, that misrepresentation had occurred and any misrepresentation is a ground for rescission. The judge referred, with approval, to the view of Goff and Jones: Law of Restitution (see Lecture p2-3), that the question whether representations would have induced a reasonable person to enter into a contract was relevant only to the onus of proof. Here the plaintiffs had established their claim to rescission of the contract on the ground of material misrepresentation because the inaccurate statements had induced them to buy the properties. They would therefore be awarded the return of their deposit, damages in respect of lost conveyancing expenses and interest.

Horsfall v Thomas [1862] 1 H&C 90

The buyer of a gun did not examine it prior to purchase. It was held that the concealment of a defect in the gun did not affect his decision to purchase as, since he was unaware of the

misrepresentation, he could not have been induced into the contract by it. His action thus failed.

Attwood v Small (1838) 6 CI&F 232

The purchasers of a mine were told exaggerated statements as to its earning capacity by the vendors. The purchasers had these statements checked by their own expert agents, who in error reported them as correct. Six months after the sale was complete the plaintiffs found the defendant's statement had been inaccurate and they sought to rescind on the ground of misrepresentation. It was held in the House of Lords that there was no misrepresentation, and that the purchaser did not rely on the representations.

Redgrave v Hurd (1881) 20 Ch D 1

The plaintiff solicitor advertised for a partner who would also purchase his residence. The Defendant replied and during two interviews, the plaintiff represented that his business was bringing in either about £300 a year, or from £300-£400 a year. At a third interview the plaintiff produced summaries of business done, which showed gross receipts below £200 a year. The defendant asked how the difference was made up and the plaintiff produced a quantity of letters and papers which, he stated, related to other business which he had done. The defendant did not examine the books and papers thus produced, but only looked cursorily at them, and ultimately agreed to purchase the house and take a share in the business for £1,600. The trial judge came to the conclusion that the letters and papers, if examined, would have shown business of only £5 or £6 a year. Finding that the practice was utterly worthless, the defendant refused to complete the contract, and the plaintiff brought an action for specific performance. The Court of Appeal gave judgment for the defendant. Lord Jessel MR stated:

"If a man is induced to enter into a contract by a false representation it is not a sufficient answer to him to say, "If you had used due diligence you would have found out that the statement was untrue. You had a means afforded to you of discovering its falsity, and did not choose to avail yourself of them." I take it to be a settled doctrine of equity, not only as regards specific performance but also as regards rescission, that this is not an answer unless there is such delay as constitutes a defence under the Statute of Limitations. That, of course, is quite a different thing."

Edgington v Fitzmaurice (1885) 29 Ch D 459

For full facts, see above. The plaintiff was induced to lend money to a company by (a) the statement of intent, and (b) his mistaken belief that he would have a charge on the assets of the company. He was able to claim damages for deceit even though he admitted that he would not have lent the money, had he not held this mistaken belief.

3. TYPES OF MISREPRESENTATION

Derry v Peek (1889) 14 App Cas 337

A special Act incorporating a tramway company provided that the carriages might be moved by animal power and, with the consent of the Board of Trade, by steam power. The directors issued a prospectus containing a statement that by this special Act the company had the right to use steam instead of horses. The plaintiff bought shares on the strength of this statement. The Board of Trade refused to consent to the use of steam and the company was wound up. The plaintiff brought an action for deceit.

It was held by the House of Lords that in an action for deceit, it is not enough to establish misrepresentation alone; something more must be proved to cast liability on the defendant. There is an essential difference between the case where the defendant honestly believes in the truth of a statement although he is careless, and where he is careless with no such honest belief. Fraud is established where it is proved that a false statement is made: (a) knowingly; or (b) without belief in its truth; or (c) recklessly, careless as to whether it be true or false. If fraud is proved, the motive of the person making the statement is irrelevant. It matters not that there was no intention to cheat or injure the person to whom the statement was made. The defendants were not fraudulent in this case. They made a careless statement but they honestly believed in its truth.

Hedley Byrne v Heller [1964] AC 465

Hedley Byrne were a firm of advertising agents. They intended to advertise on behalf of Easypower Ltd. They wanted to know if Easypower were creditworthy, and asked their bank, the national Provincial, to find out. The National Provincial got in touch with Easypower's bankers, Heller & Partners. Heller told the National Provincial, "in confidence and without responsibility on our part," that Easypower were good for £100,000 per annum on advertising contracts. Hedley Byrne relied on this statement in placing orders on behalf of Easypower and, as a result, lost more than £17,000 when Easypower went into liquidation. They sought to recover this loss as damages.

In the House of Lords, Lord Pearce stated that a man may come under a special duty to exercise care in giving information or advice. Whether such a duty has been assumed must depend on the relationship of the parties. Was there such a special relationship in the present case as to impose on Heller a duty of care to Hedley Byrne as the undisclosed principals for whom National Provincial was making the inquiry? The answer to that question depends on the circumstances of the transaction. A most important circumstance is the form of the inquiry and of the answer. Both were plainly stated to be without liability. The words clearly prevented a special relationship from arising.

Williams v Natural Life Health Foods Ltd (1998) The Times, May 1.

See Law Report.

Howard Marine v Ogden [1978] QB 574

The defendants wished to hire two barges from the plaintiffs. The plaintiffs quoted a price for the hire in a letter. At a meeting, the defendants asked about the carrying capacity of the barges. The plaintiffs' representative replied it was about 1,600 tonnes. The answer was given honestly but was wrong. It was based on the representative's recollection of the deadweight figure given in Lloyd's Register of 1,800 tonnes. The correct figure, 1,195 tonnes, appeared in shipping documents which the representative had seen, but had forgotten. Because of their limited carrying capacity, the defendant's work was held up. They refused to pay the hire charges. The plaintiffs sued for the hire charges and the defendants counter-claimed damages.

By a majority, the Court of Appeal found the plaintiffs liable under s2(1) as the evidence adduced by the plaintiffs was not sufficient to show that their representative had an objectively reasonable ground for disregarding the carrying capacity figure given in the shipping document and preferring the figure in Lloyd's Register.

4. REMEDIES FOR MISREPRESENTATION

(A) RESCISSION

Car & Universal Finance v Caldwell [1965] 1 QB 525

Caldwell sold his car to Norris. The cheque was dishonoured when it was presented the next day. He immediately informed the police and the Automoblie Association of the fraudulent transaction. Subsequently Norris sold the car to X who sold it to Y who sold it to Z who sold it to the plaintiffs. In interpleader proceedings one of the issues to be tried was whether the defendant's conduct and representations amounted to a rescission of the contract of sale. It was held that the contract was voidable because of the fraudulent misrepresentation and the owner had done everything he could in the circumstances to avoid the contract. As it had been avoided before the sale to the third party, no title was passed to them and the owner could reclaim the car.

Long v Lloyd [1958] 1 WLR 753

The defendant advertised for sale a lorry as being in 'exceptional condition' and he told the plaintiff purchaser that it did 11 miles to the gallon and, after a trial run, all that was wrong with the vehicle. The plaintiff purchase the lorry and, two days later, on a short run, further faults developed and the plaintiff noticed that it did only about 5 miles to the gallon. That evening he reported these things to the defendant and the plaintiff accepted the defendant's offer to pay for some of the repairs. The next day the lorry set out on a longer

journey and broke down. The plaintiff wrote to the defendant asking for the return of his money. The lorry had not been in a roadworthy condition, but the defendant's representations concerning it had been honestly made. The Court of Appeal held that the plaintiff was not entitled to rescission of the contract as he had finally accepted the lorry before he had purported to rescind. The second journey amounted to affirmation of the contract.

Leaf v International Galleries [1950] 2 KB 86

The plaintiff bought a painting after an innocent misrepresentation was made to him that it was by 'J. Constable'. He did not discover this until five years later and claimed rescission immediately. The Court of Appeal held that the plaintiff had lost his right to rescind after such a period of time. His only remedy after that length of time was for damages only, a claim which he had not brought before the court.

Vigers v Pike (1842) 8 CI&F 562

A lease of a mine which had been entered into as a result of a misrepresentation could not be rescinded as there had been considerable extraction of minerals since the date of the contract.

Armstrong v Jackson [1917] 2 KB 822

A broker purported to buy shares for a client, but in fact sold his own shares to the client. Five years later, when the shares had fallen in value from nearly £3 to 5s, it was held that the client could rescind on account of the broker's breach of duty. He still had the identical shares and was able to return them, together with the dividends he had received. McCardie J. said:

"It is only … where the plaintiff has sustained loss by the inferiority of the subject-matter or a substantial fall in its value that he will desire to exert his power of rescission … If mere deterioration of the subject-matter negatived the right to rescind, the doctrine of rescission would become a vain thing."

(B) INDEMNITY

Whittington v Seale-Hayne (1900) 82 LT 49

The plaintiffs bred poultry and were induced to enter into a lease of property belonging to the defendants by an oral representation that the premises were in a sanitary condition. In fact the water supply was poisoned and the manager fell ill and the stock died. The terms of the lease required the plaintiffs to pay rent to the defendants and rates to the local authority and they were also obliged to make certain repairs ordered by the local council.

Farwell J rescinded the lease, and, following the judgment of Bowen LJ in *Newbigging v Adam* (1886) 34 Ch D 582, held that the plaintiffs could recover the rents, rates and repairs

under the covenants in the lease but nothing more. They could not recover removal expenses and consequential loss (ie, loss of profits, value of lost stock and medical expenses) as these did not arise from obligations imposed by the lease (the contract did not require the farm to be used as a poultry farm). Had they been awarded, they would have amounted to an award of damages (ie, expenses resulting from the running of the poultry farm).

(C) DAMAGES

Doyle v Olby (Ironmongers) Ltd [1969] 2 QB 158

After buying an ironmonger's business, things turned out to be very different from what the vendors had led the plaintiff to believe. He was awarded damages for fraudulent misrepresentations and the appeal concerned, among other things, the measure of damages. Lord Denning MR said that: "The defendant is bound to make reparation for all the actual damage directly flowing from the fraudulent inducement … It does not lie in the mouth of the fraudulent person to say that they could not have been reasonably foreseen."

Smith v New Court Securities [1996] 4 All ER 769

See Law Report.

East v Maurer [1991] 2 All ER 733

The defendant who owned two hair salons agreed to sell one to the plaintiffs. They were induced to buy, in part by a representation from the defendant that he hoped in future to work abroad and that he did not intend to work in the second salon. In fact, the defendant continued to work at the second salon and many of his clients followed him. The result of this was that the plaintiffs saw a steady fall-off in business and never made a profit. They were finally forced to sell for considerably less than they paid. The court at first instance found that the defendant's representations were false. The defendant appealed on the assessment of the award of damages.

The Court of Appeal held that the proper approach was to assess the profit the plaintiff might have made had the defendant not made the representation(s). 'Reparation for all actual damage' as indicated by Lord Denning in Doyle v Olby would include loss of profits. The assessment of profits was however, to be on a tortious basis, that is, placing the plaintiff in the same position he would have been in, had the wrong not been committed.

The plaintiff could recover damages in respect of another such business in which he would have invested his money if the representation had been made, but not the profits which he would have made out of the defendant's business, if the representation relating to it had been true. (*Note*: the damages were reduced by one-third, from £15,000 to £10,000).

Archer v Brown [1984] 2 All ER 267

See Law Report.

Downs v Chappell [1996] 3 All ER 344

See Law Report.

Royscott Trust Ltd v Rogerson [1991] 3 WLR 57

A car dealer induced a finance company to enter into a hire-purchase agreement by mistakenly misrepresenting the amount of the deposit paid by the customer, who later defaulted and sold the car to a third party. The finance company sued the car dealer for innocent misrepresentation and claimed damages under s2(1).

The Court of Appeal held that the dealer was liable to the finance company under s2(1) for the balance due under the agreement plus interest on the ground that the plain words of the subsection required the court to apply the deceit rule. Under this rule the dealer was liable for all the losses suffered by the finance company even if those losses were unforeseeable, provided that they were not otherwise too remote. It was in any event a foreseeable event that a customer buying a car on HP might dishonestly sell the car.

Thomas Witter v TBP Industries [1996] 2 All ER 573.

MISREPRESENTATION ACT 1967

1. Removal of certain bars to rescission for innocent misrepresentation.

Where a person has entered into a contract after a misrepresentation has been made to him, and-
(a) the misrepresentation has become a term of the contract; or
(b) the contract has been performed;
or both, then, if otherwise he would be entitled to rescind the contract without alleging fraud, he shall be so entitled, subject to the provisions of this Act, notwithstanding the matters mentioned in paragraphs (a) and (b) of this section.

2. Damages for misrepresentation.

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

(2) Where a person has entered into a contract after a misrepresentation has been made to him otherwise than fraudulently, and he would be entitled, by reason of the misrepresentation, to rescind the contract, then, if it is claimed, in any proceedings arising out of the contract, that the contract ought to be or has been rescinded, the court or arbitrator may declare the contract subsisting and award damages in lieu of rescission, if of opinion that it would be equitable to do so, having regard to the nature of the misrepresentation and the loss that would be caused by it if the contract were upheld, as well as to the loss that rescission would cause to the other party.

(3) Damages may be awarded against a person under subsection (2) of this section whether or not he is liable to damages under subsection (1) thereof, but where he is so liable any award under the said subsection (2) shall be taken into account in assessing his liability under the said subsection (1).

3. Avoidance of provision excluding liability for misrepresentation.

[If a contract contains a term which would exclude or restrict-
(a) any liability to which a party to a contract may be subject by reason of any misrepresentation made by him before the contract was made; or
(b) any remedy available to another party to the contract by reason of such a misrepresentation,
that term shall be of no effect except in so far as it satisfies the requirement of reasonableness as stated in section 11(1) of the Unfair Contract Terms Act 1977; and it is for those claiming that the term satisfies that requirement to show that it does.]

4. Amendments of Sale of Goods Act 1893

…

5. Saving for past transactions.

Nothing in this Act shall apply in relation to any misrepresentation or contract of sale which is made before the commencement of this Act.

1.19 MISTAKE

INTRODUCTION

For a mistake to affect the validity of a contract it must be an "operative mistake", ie, a mistake which operates to make the contract void. The effect of a mistake is:

· At common law, when the mistake is operative the contract is usually void ab initio, ie, from the beginning. Therefore, no property will pass under it and no obligations can arise under it.

· Even if the contract is valid at common law, in equity the contract may be voidable on the ground of mistake. Property will pass and obligations will arise unless or until the contract is avoided. However, the right to rescission may be lost.

Unfortunately, there is no general doctrine of mistake - the rules are contained in a disparate group of cases. This is also an area of confusing terminology. No two authorities seem to agree on a common classification, and often the same terminology is used to cover different forms of mistake.

COMMON MISTAKE

A common mistake is one when both parties make the same error relating to a fundamental fact. The cases may be categorised as follows:

(A) RES EXTINCTA

A contract will be void at common law if the subject matter of the agreement is, in fact, non-existent. See for example:

Couturier v Hastie (1856) 5 HL Cas 673

In addition, s6 of the Sale of Goods Act 1979 provides that:

Where there is a contract for the sale of specific goods, and the goods without the knowledge of the sellers have perished at the time when the contract was made, the contract is void.

Other relevant cases include:

Griffith v Brymer (1903) 19 TLR 434
Galloway v Galloway (1914) 30 TLR 531

Couturier v Hastie was interpreted differently by the High Court of Australia in:

McRae v The Commonwealth Disposals Commission (1950) 84 CLR 377

(B) RES SUA

Where a person makes a contract to purchase that which, in fact, belongs to him, the contract is void. For example see:

Cooper v Phibbs (1867) LR 2 HL 149

(C) MISTAKE AS TO QUALITY

A mistake as to the quality of the subject matter of a contract has been confined to very narrow limits. According to Lord Atkin: "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." See:

Bell v Lever Bros Ltd [1931] All ER 1.

In cases since *Bell v Lever Bros* the courts have not been over-ready to find a mistake as to quality to be operative. See:

Solle v Butcher [1949] 2 All ER 1107
Leaf v International Galleries [1950] 1 All ER 693
Harrison & Jones Ltd v Bunten & Lancaster Ltd [1953] 1 All ER 903
Associated Japanese Bank Ltd v Credit du Nord [1988] 3 All ER 902
BCCI v Ali and others [1999] 2 All ER 1005

REMEDIES

Where a contract is void for identical mistake, the court exercising its equitable jurisdiction, can:

· Refuse specific performance
· Rescind any contractual document between the parties
· Impose terms between the parties, in order to do justice.

Relevant cases include:

Cooper v Phibbs (1867) LR 2 HL 149
Solle v Butcher [1949] 2 All ER 1107
Grist v Bailey [1966] 2 All ER 875
Magee v Pennine Insurance [1969] 2 All ER 891

Rescission for mistake is subject to the same bars as rescission for misrepresentation.

UNILATERAL MISTAKE

The case of unilateral mistake is where only one party is mistaken. The cases may be categorised as follows:

(A) MISTAKE AS TO THE TERMS OF THE CONTRACT

Where one party is mistaken as to the nature of the contract and the other party is aware of the mistake, or the circumstances are such that he may be taken to be aware of it, the contract is void.

For the mistake to be operative, the mistake by one party must be as to the terms of the contract itself. See:

Hartog v Colin & Shields [1939] 3 All ER 566

A mere error of judgement as to the quality of the subject matter will not suffice to render the contract void for unilateral mistake. See:

Smith v Hughes (1871) LR 6 QB 597

REMEDY

Equity follows the law and will rescind a contract affected by unilateral mistake or refuse specific performance as in:

Webster v Cecil (1861) 30 Beav 62

(B) MISTAKE AS TO IDENTITY

Here one party makes a contract with a second party, believing him to be a third party (ie, someone else). The law makes a distinction between contracts where the parties are inter absentes and where the parties are inter praesentes.

Contract made inter absentes

Where the parties are not physically in each others presence, eg, they are dealing by correspondence, and one party is mistaken as to the identity, not the attributes, of the other and intends instead to deal with some identifiable third party, and the other knows this, then the contract will be void for mistake. See:

Cundy v Lindsay (1878) 3 App Cas 459

If the innocent party believes that he is dealing with a reputable firm, not a rogue, see:

King's Norton Metal Co Ltd v Edridge Merrett Co Ltd (1897) TLR 98

Two conclusions are commonly drawn from these two cases: (1) that to succeed in the case of a mistake as to identity there must be an identifiable third party with whom one intended to contract; and (2) the mistake must be as to identity and not attributes.

Contract made inter praesentes

Where the parties are inter praesentes (face to face) there is a presumption that the mistaken party intends to deal with the other person who is physically present and identifiable by sight and sound, irrespective of the identity which one or other may assume. For such a mistake to be an operative mistake and to make the agreement void the mistaken party must show that:

(i) they intended to deal with someone else;
(ii) the party they dealt with knew of this intention;
(iii) they regarded identity as of crucial importance; and

(iv) they took reasonable steps to check the identity of the other person
(see Cheshire & Fifoot, *Law of Contract*, p257-263).

Even where the contract is not void, it may be voidable for fraudulent misrepresentation but if the goods which are the subject-matter have passed to an innocent third party before the contract is avoided, that third party may acquire a good title. The main cases are as follows:

Phillips v Brooks [1919] 2 KB 243
Ingram v Little [1960] 3 All ER 332 (a controversial case)
Lewis v Avery [1971] 3 All ER 907

The exception to the above rule is that if a party intended to contract only with the person so identified, such a mistake will render the contract void:

Lake v Simmons [1927] AC 487

A more recent case is:

Citibank v Brown Shipley [1991] 2 All ER 690

MUTUAL MISTAKE

A mutual mistake is one where both parties fail to understand each other.

WHERE THE PARTIES ARE AT CROSS PURPOSES

In cases where the parties misunderstand each other's intentions and are at cross purposes, the court will apply an objective test and consider whether a 'reasonable man' would take the agreement to mean what one party understood it to mean or what the other party understood it to mean:

* If the test leads to the conclusion that the contract could be understood in one sense only, both parties will be bound by the contract in this sense.

* If the transaction is totally ambiguous under this objective test then there will be no consensus ad idem (agreement as to the same thing) and the contract will be void:

Wood v Scarth (1858) 1 F&F 293
Raffles v Wichelhaus (1864) 2 H&C 906
Scriven Bros v Hindley & Co [1913] 3 KB 564

REMEDY

If the contract is void at law on the ground of mistake, equity "follows the law" and specific performance will be refused and, in appropriate circumstances, the contract will be

rescinded. However, even where the contract is valid at law, specific performance will be refused if to grant it would cause hardship. Thus the remedy of specific performance was refused in *Wood v Scarth* (above).

A recent case is:

Nutt v Read (1999) The Times, December 3.

MISTAKE RELATING TO DOCUMENTS

NON EST FACTUM

As a general rule, a person is bound by their signature to a document, whether or not they have read or understood the document: *L'Estrange v Graucob* [1934] 2 KB 394. However, where a person has been induced to sign a contractual document by fraud or misrepresentation, the transaction will be voidable.

Sometimes, the plea of non est factum, namely that 'it is not my deed' may be available. A successful plea makes a document void. The plea was originally used to protect illiterate persons who were tricked into putting their mark on documents. It eventually became available to literate persons who had signed a document believing it to be something totally different from what it actually was. See, for example:

Foster v Mackinnon (1869) LR 4 CP 704

The use of the rule in modern times has been restricted. For a successful plea of non est factum two factors have to be established:

(i) the signer was not careless in signing; and
(ii) there is a radical difference between the document which was signed and what the signer thought he was signing.

The following decision of the House of Lords is the leading case on this topic:

Saunders v Anglia Building Society (Gallie v Lee) [1970] 3 All ER 961

Note: Because of the strict requirements, it may be better for the innocent party to bring a claim based on undue influence.

1.20 CASES ON MISTAKE

COMMON MISTAKE

Couterier v Hastie (1856) 5 HL Cas 673

The plaintiff merchants shipped a cargo of Indian corn and sent the bill of lading to their London agent, who employed the defendant to sell the cargo. On 15 May 1848, the defendant sold the cargo to Challender on credit. The vessel had sailed on 23 February but the cargo became so heated and fermented that it was unfit to be carried further and sold. On May 23 Challender gave the plaintiff notice that he repudiated the contract on the ground that at the time of the sale to him the cargo did not exist. The plaintiffs brought an action against the defendant (who was a del credere agent, ie, guaranteed the performance of the contract) to recover the purchase price.

Martin B ruled that the contract imported that, at the time of sale, the corn was in existence as such and capable of delivery, and that, as it had been sold, the plaintiffs could not recover. This judgment was affirmed by the House of Lords.

Griffith v Brymer (1903) 19 TLR 434

At 11am on 24 June 1902 the plaintiff had entered into an oral agreement for the hire of a room to view the coronation procession on 26 June. A decision to operate on the King, which rendered the procession impossible, was taken at 10am on 24 June. Wright J held the contract void. The agreement was made on a missupposition of facts which went to the whole root of the matter, and the plaintiff was entitled to recover his £100.

Galloway v Galloway (1914) 30 TLR 531

See Cheshire & Fifoot, p239.

McRae v Commonwealth Disposals Commission (1950) 84 CLR 377

The defendants sold an oil tanker described as lying on Jourmand Reef off Papua. The plaintiffs incurred considerable expenditure in sending a salvage expedition to look for the tanker. There was in fact no oil tanker, nor any place known as Jourmand Reef. The plaintiffs brought an action for (1) breach of contract, (2) deceit, and (3) negligence. The trial judge gave judgment for the plaintiffs in the action for deceit. He held that *Couturier v Hastie* obliged him to hold that the contract of sale was void and the claim for breach of contract failed. Both parties appealed.

The High Court of Australia stated that it was not decided in *Couturier v Hastie* that the contract in that case was void. The question whether it was void or not did not arise. If it had arisen, as in an action by the purchaser for damages, it would have turned on the ulterior question whether the contract was subject to an implied condition precedent. In the present case, there was a contract, and the Commission contracted that a tanker existed in the position specified. Since there was no such tanker, there had been a breach of contract, and the plaintiffs were entitled to damages for that breach.

Cooper v Phibbs (1867) LR 2 HL 149

An uncle told his nephew, not intending to misrepresent anything, but being in fact in error, that he (the uncle) was entitled to a fishery. The nephew, after the uncle's death, acting in the belief of the truth of what the uncle had told him, entered into an agreement to rent the fishery from the uncle's daughters. However, the fishery actually belonged to the nephew himself. The House of Lords held that the mistake was only such as to make the contract voidable. Lord Westbury said "If parties contract under a mutual mistake and misapprehension as to their relative and respective rights, the result is that that agreement is liable to be set aside as having proceeded upon a common mistake" on such terms as the court thought fit to impose; and it was so set aside.

N.B. According to Smith & Thomas, *A Casebook on Contract*, Tenth edition, p506, "At common law such a contract (or simulacrum of a contract) is more correctly described as void, there being in truth no intention to a contract". However, Denning LJ applied *Cooper v Phibbs* in *Solle v Butcher* (1949) (below).

Bell v Lever Bros Ltd [1931] All ER 1

The plaintiff company contracted with the defendants who were to act as chairman and vice-chairman of a subsidiary company. It was later agreed between the parties that the defendants should resign their positions in consideration of payments by way of compensation. It later transpired that the defendants, without the knowledge of the plaintiffs, had engaged in private transactions resulting in a secret profit to themselves. These transactions constituted breaches of the defendants' contracts, which would have entitled the plaintiffs to terminate those contracts forthwith if they had known of the transactions.

It was held by the House of Lords (3-2) that the erroneous belief on the part of both parties to the agreements, that the service contracts were determinable except by agreement did not involve the actual subject-matter of the agreements, but merely related to the quality of the subject-matter and so was not of such a fundamental character as to constitute an underlying assumption without which the parties would not have entered into the agreements, and, therefore, the plaintiffs were not entitled to succeed in their action.

See extract from the speech of Lord Atkin.

Solle v Butcher [1949] 2 All ER 1107

For facts, see below. Denning LJ stated:

"Let me first consider mistakes which render a contract a nullity. All previous decisions on this subject must now be read in the light of Bell v Lever Bros. Ltd. 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 he was under a mistake".

Leaf v International Galleries [1950] 1 All ER 693

In 1944, the plaintiff bought from the sellers an oil painting of Salisbury Cathedral which was represented to him as a painting by Constable, a representation which was held to be one of the terms of the contract. In 1949 he found that the picture was not a Constable. The buyer brought an action for the rescission of the contract on the ground that there had been an innocent misrepresentation. The Court of Appeal held that the buyer had lost the right to rescind when he accepted delivery of the picture, or at least, when a reasonable time had elapsed after his acceptance, and five years was more than a reasonable time. Denning LJ stated obiter:

"There was a mistake about the quality of the subject-matter, because both parties believed the picture to be a Constable; and that mistake was in one sense essential or fundamental. But such a mistake does not avoid the contract: there was no mistake at all about the subject-matter of the sale. It was a specific picture, "Salisbury Cathedral." The parties were agreed in the same terms on the same subject-matter, and that is sufficient to make a contract: see *Solle v Butcher*."

Harrison v Bunten [1953] 1 All ER 903

By two contracts in writing, the sellers agreed to sell, and the buyers agreed to buy, a quantity of Calcutta Kapok "Sree" brand. After the goods had been delivered, the buyers found that, instead of being pure kapok, they contained an admixture of cotton, which was unsuitable for their machinery. Both parties thought that Calcutta Kapok "Sree" brand was pure kapok.

Pilcher J held that when goods are sold under a known trade description, without misrepresentation or breach of warranty, the fact that both parties are unaware that goods of that known trade description lack any particular quality is irrelevant. If goods answering to the particular description are supplied, the parties are bound by their contract and there is no room for the doctrine that the contract can be treated as a nullity on the ground of mutual mistake, even though the mistake, from the purchaser's point of view, may turn out to be of a fundamental character. Therefore the contracts were not nullities and the buyers were bound by them.

Associated Japanese Bank v Credit du Nord [1988] 3 All ER 902

B made a sale and leaseback transaction of specified precision engineering machines with AJB. B's obligations under the leaseback agreement were guaranteed by CDN. At all times both banks believed that the four machines existed and were in B's possession. After B failed to keep up the payments it was discovered that the transaction was a fraud perpetrated by B. AJB sued CDN on the guarantee. It was held by Steyn J that on its true construction the guarantee was subject to an express or implied condition precedent that there was a lease in respect of four existing machines. It followed, therefore, that since the machines did not exist AJB's claim failed and would be dismissed.

Steyn J stated obiter that a contract will be void ab initio for common mistake if a mistake by both parties to the contract renders the subject matter of the contract essentially and radically different from that which both parties believed to exist at the time the contract was executed. However, the party seeking to rely on the mistake must have had reasonable grounds for entertaining the belief on which the mistake was based.

BCCI v Ali and others [1999] 2 All ER 1005

See Law Report.

Cooper v Phibbs (1867)

For facts, see above. The House of Lords set the agreement aside on the terms that the defendant should have a lien on the fishery for such money as the defendant had expended on its improvements

Solle v Butcher [1949] 2 All ER 1107

In 1931 a dwelling house had been converted into five flats. In 1938 Flat No. 1 was let for three years at an annual rent of £140. In 1947 the defendant took a long lease of the building, intending to repair bomb damage and do substantial alterations. The plaintiff and defendant discussed the rents to be charged after the work had been completed. The plaintiff told the defendant that he could charge £250 for Flat 1. The plaintiff paid rent at £250 per year for some time and then took proceedings for a declaration that the standard rent was £140. The defendant contended that the flat had become a new and separate dwelling by reason of change of identity, and therefore not subject to the Rent Restriction Acts.

The Court of Appeal held that (i) the structural alterations and improvements were not such as to destroy the identity of the flat as let in 1939, and (ii) on the evidence, the parties had addressed their minds to the material issue of identity of the new flat, and their mistake or common misapprehension as to whether the flat had been so altered as to destroy its identity was a mistake of fact, and the landlord was entitled to have the lease set asid in equity on such terms as the court thought fit.

Grist v Bailey [1966] 2 All ER 875

The defendant agreed to sell a house, subject to an existing tenant, for £850. The defendant refused to perform and alleged that the agreement had been entered into by her under mistake of fact. The defendant believed that the property was occupied by a statutory tenant who had actually died. Its value with vacant possession would have been £2,250. The tenant's son occupied the flat, paying the rent at the office of solicitors, but left without having claimed to have a statutory tenancy under the Increase of Rent … Act 1920. The plaintiff buyer brought an action for specific performance of the agreement. The defendant counterclaimed for rescission of the sale agreement.

It was held that there was equitable jurisdiction to set aside the sale agreement for common mistake of fact and the sale agreement would be set aside because the mistake was fundamental, even on the footing that it had been open to the son to maintain a claim to protection as a statutory tenant, and any fault of the defendant vendor in not knowing who her tenant was was not sufficient to disentitle her to relief, the defendant offering to submit to a condition that she would enter into a fresh contract to sell the property to the plaintiff at a proper vacant possession price.

Magee v Penine Insurance [1969] 2 All ER 891

The plaintiff signed a proposal form, filled in by his son, for the insurance of a motor car. There were a number of mis-statements in the proposal, in particular it was mis-stated that the plaintiff held a driving licence. The proposal was accepted by the defendant insurance company. The car was accidentally damaged and the plaintiff made a claim in respect of it. The insurance company offered £385 in settlement of the claim which the plaintiff accepted. The insurance company then discovered the mis-statements in the proposal form and refused to pay.

It was held by the Court of Appeal, that on its true construction, the insurance company's letter was an offer of compromise and not merely an offer to quantify the claim, but judgment would be given for the defendant insurance company on the following grounds:
(a) (per Lord Denning MR) although the acceptance by the plaintiff of the insurance company's offer constituted a contract of compromise binding at law, the parties were acting under a common and fundamental mistake in that they thought that the original policy was good and binding. The contract was therefore voidable in equity, and it would be set aside because in the circumstances it was not equitable to hold the insurance company to it;
(b) (per Fenton Atkinson LJ) the agreement to compromise was made on the basis of an essential contractual assumption, namely, that there was in existence a valid and enforceable policy of insurance. Since that assumption was false the insurance company was entitled to avoid the agreement on the ground of mutual mistake in a fundamental and vital matter.

UNILATERAL MISTAKE

Hartog v Shields [1939] 3 All ER 566

The defendants contracted to sell to the plaintiff 30,000 hare skins, but by an alleged mistake they offered the goods at certain prices per pound instead of at those prices per piece. The value of a piece was approximately one-third that of a pound. In verbal and written negotiations which took place prior to the sale, reference had always been made to the price per piece and never to the price per pound, and expert evidence was given that hare skins were generally sold at prices per piece.

It was held that the plaintiff could not reasonably have supposed that the offer expressed the real intention of the persons making it, and must have known it to have been made by mistake. The plaintiff did not, by his acceptance of the offer, make a binding contract with the defendants.

Smith v Hughes [1861-73] All ER 632

The plaintiff farmer, having new oats, asked the manager of the defendant racehorse trainer, if he wanted to buy oats. On being answered by the manager that he was always ready to buy good oats, the farmer gave him a sample and told him the price. The manager took away the sample and the next day bought the bulk, but afterwards refused to accept the oats because they were new, whereas he said, he had thought to buy old oats. In the county court, there was a conflict of testimony over the type of oats mentioned at the bargaining. It was held that the passive acquiescence of the seller in the self-deception of the buyer did not, in the absence of fraud or deceit on the part of the seller, entitle the buyer to avoid the contract, and there must be a new trial.

Webster v Cecil (1861) 30 Beav 62

The defendant, having refused to sell some property to the plaintiff for £2,000, wrote a letter in which, as the result of a mistaken calculation, he offered to sell it for £1,250. The plaintiff accepted but the defendant refused to complete. Romilly MR refused a decree of specific performance.

Cundy v Lindsay [1874-80] All ER 1149

A rogue named Blenkarn ordered goods in writing from Lindsay & Co. He gave his address as "Blenkarn & Co, 37 Wood Street, Cheapside" and signed the letter in such a way that the name appeared to be "Blenkiron & Co". A very respectable firm known as Blenkiron & Sons which carried on business at 123 Wood Street was well known to Lindsay who did not ascertain their correct address but dispatched the goods to "Blenkiron & Co, 37 Wood Street, Cheapside." Blenkarn was convicted of obtaining goods by false pretences, but

before his conviction he had sold some of the goods to Cundy in the ordinary course of business and Cundy re-sold them all to different persons before the fraud was discovered.

It was held that as Lindsay & Co knew nothing of Blenkarn and intended to deal only with Blenkiron & Sons, a fact which was known to Blenkarn, there was no common intention which could lead to any contract between the parties, and therefore, the property in the goods remained in Lindsay and Cundy had no title to them.

King's Norton Metal v Edridge Merret (1897) TLR 98

A rogue named Wallis ordered some goods, on notepaper headed "Hallam & Co", from King's Norton. The goods were paid for by a cheque drawn by "Hallam & Co". King's Norton received another letter purporting to come from Hallam & Co, containing a request for a quotation of prices for goods. In reply King's Norton quoted prices, and Hallam then by letter ordered some goods, which were sent off to them. These goods were never paid for. Wallis had fraudulently obtained these goods and sold them to Edridge Merret, who bought them bona fide. King's Norton brought an action to recover damages for the conversion of the goods.

It was held by the Court of Appeal held that if a person, induced by false pretences, contracted with a rogue to sell goods to him and the goods were delivered the rogue could until the contract was disaffirmed give a good title to a bona fide purchaser for value. The plaintiffs intended to contract with the writer of the letters. If it could have been shown that there was a separate entity called Hallam & Co and another entity called Wallis then the case might have come within the decision in Cundy v Lindsay. In the opinion of AL Smith LJ, there was a contract by the plaintiffs with the person who wrote the letters, by which the property passed to him. There was only one entity, trading it might be under an alias, and there was a contract by which the property passed to him.

Philips v Brooks [1918-19] All ER 246

North visited the plaintiff jeweller, and chose some pearls and a ring. While writing a cheque in payment, he represented to the plaintiff that he was Sir George Bullough, with an address in St James Sq, London. The plaintiff had heard of Sir George as a man of means, and on referring to the directory found that he lived at the address given by North. He therefore allowed North to take away the ring. In fact, the cheque was worthless and North was convicted of obtaining the ring from the plaintiff by false pretences. North had pawned the ring with the defendant pawnbrokers, who took it bona fide and without notice in the course of business, giving value for it. The plaintiff brought an action for the return of the ring.

It was held that the plaintiff intended to contract with North although he would not have made the contract, but for the defendant's fraudulent misrepresentation, and therefore, the

property in the ring passed to North who could give a good title to any third party acquiring it bona fide, without notice and for value, and the action failed.

Ingram and others v Little [1960] 3 All ER 332

The joint owners of a car, two sisters and a third person, advertised it for sale. A swindler called on them and agreed to buy the car. When they refused to accept a cheque, he tried to convince them that he was a reputable person and said that he was a Mr Hutchinson of Stanstead House, Caterham. One sister went to the local post office and returned to say that she had checked the name and address in the telephone directory. They decided to accept the cheque. The cheque was dishonoured and the man, who was not Mr Hutchinson, disappeared having sold the car to Little, who had bought it in good faith. The owners brought an action to recover the car or its value from Little.

It was held by the Court of Appeal (Devlin LJ dissenting) that the offer to sell on payment by cheque was made only to the person whom the swindler had represented himself to be, and as the swindler knew this, the offer was not one which was capable of being accepted by him. Therefore, there had been no contract for the sale of the car by the plaintiffs and they were entitled to recover the car or damages from the defendant.

Lewis v Avery [1971] 3 All ER 907

Lewis advertised his car for sale. A man, who turned out to be a rogue, called on Lewis, tested the car and said that he liked it. He called himself "Richard Green" and made Lewis believe that he was a well-known film actor of that name. They agreed a price and the rogue wrote out a cheque. He said he wanted to take the car at once. Lewis asked for proof of identity and he was shown a studio pass which bore the name "Richard Green" and a photograph of the rogue. On seeing this Lewis was satisfied and let the rogue have the car and log book. The cheque was dishonoured. Meanwhile the rogue had sold the car to Avery, who bought in good faith and without knowledge of the fraud. Lewis brought an action for the conversion of the car. It was held by the Court of Appeal, distinguishing and doubting *Ingram v Little*, that:

(1) the fraud perpetrated by the rogue rendered the contract between Lewis and the rogue voidable and not void because-
(a) where a transaction had taken place between a seller and a person physically present before him there was a presumption that the seller was dealing with that person even though, because of the latter's fraud, the seller thought that he was dealing with another individual whom he believed to be the person physically present. In the present case there was nothing to rebut the presumption that Lewis was dealing with the person present before him, ie the rogue; and
(b) Lewis failed to show that, at the time of offering to sell his car to the rogue, he regarded his identity as a matter of vital importance. It was merely a mistake as to the attributes of the rogue, ie his creditworthiness.

(2) Accordingly, since Lewis had failed to avoid the contract before the rogue parted with the property in the car to Avery, the latter, having bought the car bona fide and without notice of the fraud, had acquired a good title thereto and the action failed.

Lake v Simmonds [1927] All ER 49

A woman, Esme Ellison, who had bought certain goods from the plaintiff jeweller on previous occasions, told him that her husband, Van der Borgh, wished to give her a pearl necklace. Believing that she was the person she represented herself to be and that her statements were true, the jeweller allowed her to take two necklaces to show her husband. In fact Esme was not Van der Borgh's wife. Having obtained the necklaces Esme sold them and retained the proceeds. The plaintiff brought an action against his insurance company, who refused to pay as the goods had been entrusted by him to the thief.

It was held by the House of Lords, that in obtaining the necklaces in the way that she did, Esme was guilty of larceny by a trick, and therefore, when the plaintiff permitted her to take the necklaces there was no consensus ad idem (agreement as to the same thing) between them and the necklaces were not "entrusted" to her within the exceptions clause in the policy, which was to be constructed contra proferentem. Accordingly, the plaintiff was entitled to succeed.

Citibank v Brown Shipley [1991] 2 All ER 690

See Law Report.

MUTUAL MISTAKE

Wood v Scarth (1858) 1 F&F 293

The defendant offered in writing to let a pub to the plaintiff at £63 pa. After a conversation with the defendant's clerk, the plaintiff accepted by letter, believing that the £63 rental was the only payment under the contract. In fact, the defendant had intended that a £500 premium would also be payable and he believed that his clerk had explained this to the plaintiff. The defendant refused to complete and the plaintiff brought an action for specific performance. The court refused the order of specific performance but the defendant was liable in damages.

Raffles v Wichelhaus (1864) 2 H&C 906

The plaintiff agreed to sell cotton to the defendant which was "to arrive ex Peerless from Bombay". When the cotton arrived the plaintiff offered to deliver but the defendants refused to accept the cotton. The defendants pleaded that the ship mentioned was intended

by them to be the ship called the Peerless, which sailed from Bombay in October and that the plaintiff had not offered to deliver cotton which arrived by that ship, but instead offered to deliver cotton which arrived by another ship, also called Peerless, which had sailed from Bombay in December.

Judgment was given for the defendants. It was held that there was nothing on the face of the contract to show which Peerless was meant; so that this was a plain case of latent ambiguity, as soon as it was shown that there were two Peerlesses from Bombay; and parol evidence could be given when it was found that the plaintiff meant one and the defendants the other. If this was the case, there was no consensus ad idem, and therefore no binding contract.

Scriven Bros v Hindley [1913] 3 KB 564

The defendants bid at an auction for two lots, believing both to be hemp. In fact Lot A was hemp but Lot B was tow, a different commodity in commerce and of very little value. The defendants declined to pay for Lot B and the sellers sued for the price. The defendants' mistake arose from the fact that both lots contained the same shipping mark, "SL", and witnesses stated that in their experience hemp and tow were never landed from the same ship under the same shipping mark. The defendants' manager had been shown bales of hemp as "samples of the 'SL' goods". The auctioneer believed that the bid was made under a mistake as to the value of the tow.

Lawrence J said that as the parties were not ad idem the plaintiffs could recover only if the defendants were estopped from relying upon what was now admittedly the truth. He held that the defendants were not estopped since their mistake had been caused by or contributed to by the negligence of the plaintiffs.

Foster v Mackinnon (1869) LR 4 CP 704

The defendant, an elderly gentleman, signed a bill of exchange on being told that it was a guarantee similar to one which he had previously signed. He had only been shown the back of it. It was held that there should be a new trial. Byles J stated:

"It seems plain, on principle and on authority, that if a blind man, or a man who cannot read, or who, for some reason (not implying negligence) forbears to read, has a written contract falsely read over to him, the reader misreading it to such a degree that the written contract is of a nature altogether different from the contract pretended to be read from the paper which the blind or illiterate man afterwards signs; then at least if there be no negligence, the signature obtained is of no force. And it is invalid not merely on the ground of fraud, where fraud exists, but on the ground that the mind of the signer did not accompany the signature; in other words, he never intended to sign and therefore, in contemplation of law, never did sign the contract to which his name is appended. In the present case, … he was deceived, not merely as to the legal effect, but as to the actual contents of the instrument."

Saunders v Anglia Building Society [1970] 3 All ER 961

Mrs Gallie, a widow aged 78, had made a will leaving her house to her nephew, Parkin. Parkin's friend, Lee, was heavily in debt and discussed with Parkin how to raise money on the house. In Parkin's presence, Lee put before Mrs Gallie a document which he told her was a deed of gift of the house to Parkin. She did not read it because she had broken her spectacles. The deed was in fact a deed of sale of the house to Lee. Using this deed, Lee mortgaged the house to the Anglia Building Society, and borrowed £2,000. Lee defaulted on the payments and the building society brought an action for possession of the house. Mrs Gallie sued for a declaration that the deed was void--non est factum--and for the recovery of the title deeds. When she died, the action was taken over by her executrix, Saunders. The Court of Appeal and the House of Lords gave judgment for the building society.

It was held by the House of Lords that the plea of non est factum can only rarely be established by a person of full capacity and although it is not confined to the blind and illiterate any extension of the scope of the plea would be kept within narrow limits. In particular, it is unlikely that the plea would be available to a person who signed a document without informing himself of its meaning.

The burden of establishing a plea of non est factum falls on the party seeking to disown the document and that:
(1) the party must show that in signing the document he acted with reasonable care. Carelessness (or negligence devoid of any special, technical meaning) on the part of the person signing the document would preclude him from later pleading non est factum on the principle that no man may take advantage of his own wrong.
(2) In relation to the extent and nature of the difference between the document as it is and the document as it was believed to be, the distinction formerly drawn between the character and the contents of the document is unsatisfactory and it is essential, if the plea is to be successful, to show that there is a radical or fundamental distinction.

1.21 DURESS

In order for there to be a valid contract the parties must act freely. If one of the parties is forced to make the contract by violence or the threat of violence, that is duress, and renders the contract voidable.

DURESS TO THE PERSON

The original common law of duress confined the doctrine within very narrow limits. Only duress to the person was recognised during the nineteenth century, and this required actual or threatened violence to the victim. For example, see:

Barton v Armstrong [1976] AC 104.

DURESS TO GOODS

The nineteenth century limitation on duress meant that it could not be applied to 'duress of goods'. If a person, unlawfully detained, or threatened to detain, another's goods, this was not considered to be sufficient duress to enable a contract to be avoided. See:

Skeate v Beale (1840) 11 Ad&El 983.

Although this case lays down the rule that a contract entered into in pursuance of a threat to retain goods cannot be thereby set aside, there is a restitutionary rule to the effect that money paid to obtain the release of goods wrongfully retained, or to avoid their seizure, may be recovered. See:

Maskell v Horner [1915] 3 KB 106

The decision in *Skeate v Beale* was strongly criticised (though obiter) by Kerr J in:

Occidental Worldwide Investment Corp v Skibs A/S Avanti (The Sibeon and The Sibotre) [1976] 1 Lloyd's Rep 293.

This view was endorsed by Mocatta J in *The Atlantic Baron* [1979] QB 705, and by Lord Scarman in *Pao On v Lau Yiu Long* (below). In the light of the modern developments of duress, it would seem that *Skeate v Beale* is no longer good law.

ECONOMIC DURESS

In recent times, the courts have extended the concept of duress from its earlier limits so as to recognise that certain forms of commercial pressure could amount to economic duress. The first modern case to make this clear was:

The Sibeon and The Sibotre [1976] 1 Lloyd's Rep 293.

A subsequent case confirmed that duress could take the form of economic duress:

North Ocean Shipping v Hyundai Construction (The Atlantic Baron) [1979] QB 705.

The Privy Council had an opportunity to consider economic duress, and agreed with the observations in *The Sibeon and The Sibotre*, in:

Pao On v Lau Yiu Long [1980] AC 614.

A further important development was the decision of the House of Lords, which modified the approach previously taken, in:

Universe Tankships v ITWF (The Universe Sentinel) [1982] 2 All ER 67.

A significant feature of this judgment is its departure from the previously stringent requirement of *The Sibeon* and *Pao On* that the victim's will and consent should have been 'overborne' by the pressure. This approach of Lord Scarman was cited and approved by the Court of Appeal in:

B&S Contractors v Victor Green Publications [1984] ICR 419.

The concept of economic duress was considered in two High Court cases:

Atlas Express Ltd v Kafco (Importers and Distributors) Ltd [1989] 1 All ER 641
Vantage Navigation Corp v Bahwan Building Materials (The Alev) [1989] 1 Lloyd's Rep 138.

It can be seen that from the cases since *Pao On* (1980) there has been a considerable relaxation of the criteria needed to prove economic duress. All that is now required is a suppression of the victim's will and voluntary consent.

The following case, considered by the House of Lords, is a useful reminder of the fact that the pressure applied must be improper in the legal sense:

Dimskal Shipping Co v ITWF (The Evia Luck) [1991] 4 All ER 871.

See also:

CTN Cash & Carry Ltd v Gallagher Ltd [1994] 4 All ER 714.

REMEDIES FOR DURESS

(A) The effect of duress is to make the contract voidable (not void). The injured party will, therefore, be entitled to have the contract set aside for operative duress, unless he has expressly or impliedly affirmed it. The victim of duress must seek rescission as soon as possible after the original pressure has ceased to operate (*The Atlantic Baron* (above)).

(B) As duress has been equated with the tort of intimidation (see the judgments of Lord Denning MR in *D&C Builders v Rees* (1966) and Lord Scarman in *Universe Tankships* (1982)), it would follow that a remedy for damages would lie in tort. See:

Morgan v Fry [1968] 2 QB 710 (for the definition of the tort of intimidation)
D&C Builders v Rees [1966] 2 QB 617
Universe Tankships v ITWF [1982] 2 All ER 67.

(For the measure of damages for the tort of intimidation, see *Rookes v Barnard* [1964] AC 1129.)

(C) There is, as yet, no authority on the question of whether or not an injured party who has affirmed the contract may nevertheless recover damages in tort. Chitty (para 501) has the

view that damages should be recoverable, since otherwise a party who has lost the right to avoid the contract is left without a remedy for a clearly unlawful act.

1.22 CASES ON DURESS

DURESS TO THE PERSON

Barton v Armstrong [1976] AC 104

A (the former chairman of a company) threatened B (the managing director) with death if he did not agree to purchase A's shares in the company. There was some evidence that B thought the proposed agreement was a satisfactory business arrangement both from his own point of view and that of the company. B executed a deed on behalf of the company carrying out the agreement. He sought a declaration that the deed was executed under duress and was void.

The Privy Council held that if A's threats were "a" reason for B's executing the deed he was entitled to relief even though he might well have entered into the contract if A had uttered no threats to induce him to do so. The onus was on A to prove that the threats he made contributed nothing to B's decision to sign.

DURESS TO GOODS

Skeate v Beale (1840) 11 Ad&El 983

A tenant who was threatened with the levying of distress by his landlord in respect of rent owed, promised to pay part immediately and the balance within one month. When the tenant failed to pay the balance, as agreed, the landlord brought an action for the balance. The tenant pleaded that the distress was wrongful in that a smaller sum only was owed. He had consented to the agreement because the landlord threatened to sell the goods immediately unless the agreement was made. This plea of duress was rejected.

Maskell v Horner [1915] 3 KB 106

Toll money was taken from the plaintiff under a threat to close down his market stall and to seize his goods if he did not pay. These tolls were, in fact, demanded from him with no right in law. The Court of Appeal allowed the plaintiff to recover all the toll money paid, even though the payments had been made over a considerable period of time. Lord Reading CJ stated that if a person pays money, which he is not bound to pay, under a compulsion of urgent and pressing necessity or of seizure, he can recover it as money had and received under the law of restitution.

It was held that there was a wider restitutionary rule that money paid to avoid goods being seized or to obtain their release could be recovered. Further, it was held that in the present case there was a compulsory agreement to enter into, whereas in *Skeate* the agreement was entered into voluntarily.

NOTE: The distinction between the *Skeate v Beale* line of cases and the decision in *Maskell v Horner* is hard to follow, and it has been pointed out that the peculiar result would follow that although an agreement to pay money under duress of goods is enforceable, sums paid in pursuance of such an agreement by the coerced can be recovered in an action for money had and received under the law of restitution.

The Sibeon and The Sibotre [1976] 1 Lloyd's Rep 293

Kerr J stated: "if I should be compelled to sign a lease or some other contract for a nominal but legally sufficient consideration under an imminent threat of having my house burnt down or a valuable picture slashed through without any threat of physical violence to anyone, I do not think that the law would uphold the agreement … The true question is ultimately whether or not the agreement in question is to be regarded as having been concluded voluntarily."

ECONOMIC DURESS

The Sibeon and The Sibotre [1976] (above)

The charterers of two ships renegotiated the rates of hire after a threat by them that they would go bankrupt and cease to trade if payments under the contract of hire were not lowered. Since they also represented that they had no substantial assets, this would have left the owners with no effective legal remedy. The owners would have had to lay up the vessels and would then have been unable to meet mortgages and charges - a fact known by the charterers. The threats themselves were false in that there was no question of the charterers being bankrupted by high rates of hire.

Kerr J rejected the earlier confines of duress. But, he said, in a contractual situation commercial pressure is not enough to prove economic duress. The court must, he said, be satisfied that the consent of the other party was overborne by compulsion so as to deprive him of his free consent and agreement. This would depend on the facts in each case. He considered that two questions had to be asked before the test could be satisfied: (1) did the victim protest at the time of the demand and (2) did the victim regard the transaction as closed or did he intend to repudiate the new agreement? Kerr J considered that the owners would have been entitled to set aside the renegotiated rates on the ground of economic duress, but that on the present facts their will and consent had not been 'overborne' by what was ordinary commercial pressures.

The Atlantic Baron [1979] QB 705

The builders of a ship demanded a 10% increase on the contract price from the owners largely because the value of the US dollar fell by 10%, or threatened not to complete the ship. The owners paid the increased rate demanded from them, although they protested that there was no legal basis on which the demand could be made. The owners were commercially compelled to pay since, at the time of the threat, they were negotiating a very lucrative contract for the charter of the ship being built.

Mocatta J decided that this constituted economic duress. The illegitimate pressure exerted by the building company was their threat to break the construction contract. Where a threat to break a contract had led to a further contract, that contract, even though it was made for good consideration, was voidable by reason of economic duress. However, the right to have the contract set aside could be lost by affirmation. The plaintiffs had delayed in reclaiming the extra 10% until eight months later, after the delivery of a second ship. This delay deafeated the plaintiff's claim for the rescission of the contract to pay the extra 10%.

Pao On v Lau Yiu Long [1980] AC 614

The plaintiff had threatened not to proceed with a contract for the sale of shares, unless the other side agreed to a renegotiation of certain subsidiary arrangements. Anxious to complete the main agreement, but knowing that they could claim specific performance of it, the defendant, wishing to avoid litigation, agreed. When the plaintiff later tried to enforce these arrangements the defendant claimed that they had been extracted by duress, and were therefore voidable. The Privy Council held that the plaintiff was entitled to succeed. On the facts, the defendant considered the matter thoroughly, chose to avoid litigation and formed the opinion that there was no risk in the subsidiary arrangements. In short, there was commercial pressure, but no coercion.

Lord Scarman agreed with the observations of Kerr J in *The Sibeon and The Sibotre* that in a contractual situation, commercial pressure is not enough. There must be present some factor 'which could be regarded as a coercion of his will so as to vitiate his consent'. In determining whether there was a coercion of will such that there was no true consent, it is material to enquire: whether the person alleged to have been coerced did or did not protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have an alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it. All these matters are relevant in determining whether he acted voluntarily or not.

The Universe Sentinel [1982] 2 All ER 67

A trade union had 'blacked' the plaintiff's ship, ie threatened to induce the crew of a ship to break their contracts of employment and so to prevent the ship from leaving port, unless the owner paid a large sum of money, partly to the union welfare fund. In view of the

catastrophic financial consequences which the shipowners would suffer if these threats were carried out, it was conceded that they constituted economic duress, vitiating the shipowners' consent to the agreement. It was held by the House of Lords that these payments could be recovered.

Lord Diplock stated that economic duress could be relied upon by a victim where his apparent consent was induced by pressure exercised on him by the other party which the law does not regard as legitimate, with the consequence that the consent is treated in law as revocable unless expressly or impliedly approbated after the illegitimate pressure has ceased to operate on his mind.

Lord Scarman dealt with the two elements of economic duress, ie consent induced by coercion of the will of the victim, and the fact that the pressure was illegitimate. In his discussion of 'compulsion', Lord Scarman modified the approach previously taken. His Lordship stated: "Compulsion is variously described in the authorities as coercion or the vitiation of consent. The classic case of duress is, however, not the lack of will to submit but the victim's intentional submission arising from the realisation that there is no other practical choice open to him … The absence of choice can be proved in various ways, eg by protest, by the absence of independent advice, or by a declaration of intention to go to law to recover the money paid or the property transferred … But non of these evidential matters goes to the essence of duress. The victim's silence will not assist the bully, if the lack of any practicable choice but to submit is proved." In the present case there was no protest at the time, but only a determination to do whatever was needed as rapidly as possible to release the ship.

B&S Contractors v Victor Green Publications [1984] ICR 419

A contractor who had undertaken to erect stands for an exhibition at Olympia told his client, less than a week before the exhibition was due to open, that the contract would be cancelled unless the client paid an additional sum to meet claims which were being made against the contractor by his workforce. The consequence of not having the stands erected in time would have been disastrous for the client in that it would have gravely damaged his reputation and might have exposed him to heavy claims for damages from exhibitors to whom space on the stands had been let. In these circumstances it was held that the payment had been made under duress and that the client was entitled to recover it back.

Atlas Express v Kafco [1989] 1 All ER 641

Kafco, a small company dealing in basketware, had secured a large contract from Woolworths and had obtained a large quantity of goods to fulfil it. They entered into a contract with Atlas, a national road carrier, to distribute the goods to Woolworths' shops. Before entering into the contract Atlas's manager inspected the cartons used by Kafco and, estimating a minimum load of 400 cartons, quoted a price £1.10 per carton (total, £440). In fact, the first load contained only 200 cartons which the manager said was not viable unless

Kafco agreed to pay a minimum of £440 per load. It was essential to Kafco's commercial survival that they should be able to meet delivery dates. It would have been difficult, if not impossible, to find alternative carriers to do so. Kafco agreed to the new terms but later refused to pay at the new rate.

It was held that Kafco were not bound by the new terms: economic duress had vitiated the new agreement and, in any case, there was no consideration for it. Tucker J found that the defendants' apparent consent to the agreement was induced by pressure which was illegitimate and he found that it was not approbated.

The Alev [1989] 1 Lloyd's Rep 138

The plaintiffs chartered a vessel to hirers who were carrying the defendants cargo of steel. The hirers defaulted on the payments and the plaintiffs were obliged by the terms of the bills of lading to carry the cargo. This would involve extra costs. They therefore negotiated with the defendants who agreed to pay extra costs and not to detain or arrest the vessel while in port. This agreement was secured through threats, including a statement that unless the defendants paid the extra costs they would not get their cargo. When the ship was in port and had commenced unloading the defendants ignored the agreement and arrested the ship. They pleaded duress to any breach of contract and claimed damages.

It was held that the agreement clearly fell within the principles of economic duress. During their negotiations the plaintiffs did make an illegal threat to withhold cargo and they were fully aware that, since they were legally obliged to carry the cargo, even if at a loss of profit to themselves, such a threat would be unlawful. The defendant's right to rely on duress was therefore established and the contract was voidable on the ground of duress.

The Evia Luck [1991] 4 All ER 871

Whilst the the plaintiff's ship was in harbour in Sweden, it was boarded by agents of the International Transport Workers' Federation, who informed them that the ship would be blacked and loading would not be continued until the company entered into certain agreements with ITWF, including back pay to the crew, new contracts of employment at higher wages and guarantees for future payments. At first the plaintiffs would not agree and the ship was in fact blacked. Yielding to the pressure, the company agreed to sign the various agreements, which were expressly declared to be governed by English law. The plaintiffs then sought to avoid the agreement on the grounds of duress and claimed restitution of all sums paid.

The House of Lords in discussing what constituted economic duress, said the fact that ITWF's conduct was quite legal in Sweden was irrelevant. In stipulating that the agreements were to be governed by English law, the defendants had to accept English law as the proper law of conduct. Under English law a contract obtained by duress was voidable, and improper

economic pressure (blacking the ship) constituted one form of duress. The owners were thus entitled to avoid the agreements they entered into because of pressure from ITWF.

CTN Cash & Carry v Gallagher [1994] 4 All ER 714

The plaintiffs purchased cigarettes from the defendants. One consignment was delivered by the defendants to the wrong warehouse (although it did belong to the plaintiffs). The parties agreed that the defendants would collect the consignment and transport it to the proper warehouse, but before this could be done the entire consignment was stolen. Each purchase of cigarettes was a separate sale and a separate contract made by credit. Credit facilities had been arranged with the defendants and they reserved an absolute right to withdraw credit at any time and for any reason. When the consignment was stolen the plaintiffs initially refused to pay, but were coerced into doing so by the defendants' threat to withdraw all credit facilities. Later, the plaintiffs reclaimed the payment arguing that they had paid under duress.

The Court of Appeal, while recognising that the defendants' method of obtaining payment was questionable, declared itself unwilling, for policy reasons, to introduce a concept of 'lawful act duress'. Legally, although the defendants' conduct was 'unattractive' it did not amount to duress.

REMEDIES

Morgan v Fry [1968] 2 QB 710.

Lord Denning MR defined the tort of intimidation as follows:

"The essential ingredients are these: there must be a threat by one person to use unlawful means (such as violence or a tort or a breach of contract) so as to compel another to obey his wishes and the person so threatened must comply with the demand rather than risk the threat being carried into execution. In such circumstances the person damnified by the compliance can sue for intimidation."

D&C Builders v Rees [1966] 2 QB 617

In this case (which has been previously considered in relation to promissory estoppel), Lord Denning equated the undue pressure brought to bear on the plaintiffs with the tort of intimidation. His Lordship refused to exercise estoppel because of the wife's inequitable actions since she knew the builders needed the money.

Universe Tankships v ITWF [1982] 2 All ER 67

Lord Scarman said that : 'duress, if proved, not only renders voidable a transaction into which a person has entered under its compulsion but is actionable as a tort, if it causes damage or loss'.

1.23 UNDUE INFLUENCE IN EQUITY

INTRODUCTION

"Equity gives relief on the ground of undue influence where an agreement has been obtained by certain kinds of improper pressure which were thought not to amount to duress at common law because no element of violence to the person was involved" (GH Treitel, *The Law of Contract*).

A person who has been induced to enter into a transaction (eg, a gift, contract or guarantee) by the undue influence of another (the wrongdoer) is entitled to set that transaction aside as against the wrongdoer. The effect of undue influence, like duress, is to make the contract voidable.

Such undue influence is either actual or presumed. In *Barclays Bank v O'Brien* [1993] 4 All ER 417, the House of Lords adopted the following classification of undue influence chosen by the Court of Appeal in *BCCI v Aboody* [1989] 1 QB 923:

CLASS 1: ACTUAL UNDUE INFLUENCE

In these cases it is necessary for the claimant to prove affirmatively that the wrongdoer exerted undue influence on the complainant to enter into the particular transaction which is impugned. For example, see:

Williams v Bailey (1866) LR 1 HL 200.

Undue influence was described by Lindley LJ in *Allcard v Skinner* (1887) 36 Ch D 145, as "… some unfair and improper conduct, some coercion from outside, some overreaching, some form of cheating and generally, though not always, some personal advantage gained."

The House of Lords held in *CIBC Mortgages v Pitt* [1993] 4 All ER 433, that there is no further requirement in cases of this kind that the transaction must be shown to be to the manifest disadvantage of the party seeking to set it aside (disapproving *BCCI v Aboody* (1989) on this point).

CLASS 2: PRESUMED UNDUE INFLUENCE

In these cases the complainant only has to show, in the first instance, that there was a relationship of trust and confidence between the complainant and the wrongdoer of such a nature that it is fair to presume that the wrongdoer abused that relationship in procuring the complainant to enter the impugned transaction.

In class 2 cases therefore, there is no need to produce evidence that actual undue influence was exerted in relation to the particular transaction impugned: once a confidential relationship has been proved, the burden then shifts to the wrongdoer to prove that the complainant entered into the impugned transaction freely, for example by showing that the complainant had independent advice.

Note that it must also be shown that the transaction was manifestly disadvantageous to the party alleged to be influenced (*National Westminster Bank v Morgan* [1985] 1 All ER 821, below).

Such a confidential relationship can be established in two ways:

CLASS 2A

Certain relationships as a matter of law raise the presumption that undue influence has been exercised.

The relationships where undue influence is presumed have been held to be: parent & child (*Wright v Vanderplank* (1855); solicitor & client (*Wright v Carter* (1903)); doctor & patient (*Mitchell v Homfray* (1881)); trustee & beneficiary (*Ellis v Barker* (1871)); and religious adviser & disciple (*Roche v Sherrington* (1982)). For a case example see:

Allcard v Skinner (1887) 36 Ch D 145.

The relationship of husband and wife does not, as a matter of law, raise a presumption of undue influence within class 2A (*Midland Bank v Shepherd* (1988)). Nor does the rule apply between employer and employee (*Matthew v Bobbins* (1980)).

CLASS 2B

If the complainant proves the existence of a relationship under which the complainant generally reposed trust and confidence in the wrongdoer, the existence of such relationship raises the presumption of undue influence.

In a class 2B case therefore, in the absence of evidence disproving undue influence, the complainant will succeed in setting aside the impugned transaction merely by proof that the complainant reposed trust and confidence in the wrongdoer without having to prove that the wrongdoer exerted actual undue influence or otherwise abused such trust and confidence in relation to the particular transaction impugned.

The relation of banker and customer will not normally give rise to a presumption of undue influence, but it can do so in exceptional cases if the customer has placed himself entirely in the hands of the bank and has not been given any opportunity to seek independent advice. See:

Lloyd's Bank v Bundy [1974] 3 All ER 757
National Westminster Bank v Morgan [1985] 1 All ER 821

MANIFEST DISADVANTAGE

With both of the above presumptions (class 2A and 2B), the transaction must be to the 'manifest disadvantage' of the party claiming undue influence. See:

National Westminster Bank v Morgan [1985] 1 All ER 821
BCCI v Aboody [1989] 1 QB 923

UNDUE INFLUENCE AND THIRD PARTIES

Undue influence is now regularly invoked by wife-sureties where their relationship with the bank-creditor is manipulated when the debtor-husband acts as intermediary. For example, a husband persuading his wife to guarantee his company's overdraft with a bank, using the matrimonial home, of which she is joint owner, as security for the debt. In such situations the creditor may be 'tainted' by the undue influence of the intermediary. If a bank entrusts certain duties to a debtor-husband who, as intermediary, is capable of exerting some influence over his wife, the position is as follows:

1. If the transaction is one which is (a) on its face not to the financial advantage of the party seeking to set it aside, and (b) if there is a substantial risk of its having been obtained by undue influence, then the third party will have constructive notice of undue influence giving the right to set aside the transaction. The creditor must take reasonable steps to ensure that the wife's consent was properly obtained. See:

Barclays Bank v O'Brien [1993] 4 All ER 417.

2. However, if the transaction is not of this kind, but is on its face capable of benefiting the party who seeks to set it aside, the third party will not have constructive notice of any undue influence which may in fact have existed. See:

CIBC Mortgages v Pitt [1993] 4 All ER 433.

Note the opinion of the Court of Appeal in:

Barclays Bank v Coleman (2000) The Times LR, January 5

REBUTTING THE PRESUMPTION

The presumption of undue influence is rebutted if the party benefiting from the transaction shows that it was "the free exercise of independent will", even if no external advice was given or even though it was not taken (*Inche Noriah v Shaik Allie bin Omar* [1928] All ER 189). However, the most usual way of rebutting the presumption is to show that the other party had independent advice before entering into the transaction. Case examples include:

Re Craig [1970] 2 All ER 390
Re Brocklehurst [1978] 1 All ER 767.

Where a bank seeks to enforce its security against a wife who claims to have been induced by her husband's undue influence or misrepresentation to charge the matrimonial home by way of security, the principles which apply in determining whether the bank is able to rely on the fact that the wife received legal advice before entering into the charge to rebut the presumption of undue influence and imputed or constructive notice thereof and whether the bank ought to have been put on inquiry to ascertain whether the wife was subject to her husband's undue influence, were given by the Court of Appeal in:

Royal Bank of Scotland v Etridge (No 2) [1998] 4 All ER 705.

REMEDIES

The remedy in cases of undue influence is rescission. Damages are not available, but see below.

RESCISSION

Where rescission is ordered, the whole transaction will be set aside. See:

TSB Bank v Camfield [1995] 1 All ER 951
Dunbar Bank v Nadeem [1998] 3 All ER 876.

Bars to rescission:

(i) IMPOSSIBILITY OF RESTITUTION

However, the fact that *restitutio in integrum* is impossible will not be a bar to rescission:

O'Sullivan v Management Agency & Music Ltd [1985] 3 All ER 351
Cheese v Thomas [1994] 1 All ER 35
Mahoney v Purnell [1996] 3 All ER 61.

(ii) DELAY

Delay defeats equity. For example, see:

Allcard v Skinner (1887) 36 Ch D 145.

SEVERANCE

It may be possible for the court to sever from an instrument affected by undue influence the objectionable parts leaving the part uncontaminated by undue influence enforceable. See:

Barclays Bank v Caplan and Another (1997) The Times, December 12.

DAMAGES

Damages are not available for undue influence, but if a bank has broken a duty of care to a wife-surety damages may be available in negligence under *Hedley Byrne v Heller* (1964).

See also, *Royal Bank of Scotland v Etridge (No 2)* [1998] 4 All ER 705, note 8 at p706: solicitor owes a duty of care to the wife.

CASES ON UNDUE INFLUENCE

CLASS 1: ACTUAL UNDUE INFLUENCE

Williams v Bailey (1866) LR 1 HL 200

A son forged his father's signature on promissory notes and gave them to their bankers. At a meeting of all the parties at the bank, one of the bankers said to the father: "If the bills are yours we are all right; if they are not, we have only one course to pursue; we cannot be parties to compounding a felony." The bank's solicitor said it was a serious matter and the father's own solicitor added, "a case of transportation for life." After further discussion as to the son's financial liability the bank's solicitor said that they could only look to the father. The father then agreed to make an equitable mortgage to the bank in consideration of the return of the promissory notes. The father succeeded in an action for cancellation of the agreement.

It was held by Lord Westbury that the security given for the debt of the son by the father under such circumstances, was not the security of a man who acted with that freedom and power of deliberation that must be considered as necessary to validate a contract to give security for the debt of another.

CLASS 2: PRESUMED UNDUE INFLUENCE

CLASS 2A

Allcard v Skinner (1887) 36 Ch D 145

In 1867 an unmarried woman aged 27 sought a clergyman as a confessor. The following year she became an associate of the sisterhood of which he was spiritual director and in 1871 she was admitted a full member, taking vows of poverty, chastity and obedience. Without independent advice, she made gifts of money and stock to the mother superior on behalf of the sisterhood. She left the sisterhood in 1879 and in 1884 claimed the return of the stock. Proceedings to recover the stock were commenced in 1885.

It was held by the Court of Appeal that although the plaintiff's gifts were voidable because of undue influence brought to bear upon the plaintiff through the training she had received, she was disentitled to recover because of her conduct and the delay.

CLASS 2B

Lloyd's Bank v Bundy [1975] QB 326

A guarantee was given to the bank by an elderly farmer, a customer of the bank, for his son's debts. The guarantee was secured by a mortgage of Bundy's house in favour of the bank. An assistant manager of the bank, with the son, later told the father that they would only continue to support the son's company if he increased the guarantee and charge. The father did so, the assistant manager appreciating that the father relied on him implicitly to advise him about the transaction. The Court of Appeal set aside the guarantee and charge.

Lord Denning held that the relationship between the bank and the father was one of trust and confidence. The bank knew that the father relied on them implicitly to advise him about the transaction. The father trusted the bank. This gave the bank much influence on the father. Yet the bank failed in that trust. They allowed the father to charge the house to his ruin. There was also a conflict of interest between the bank and the father, yet the bank did not realise it, nor did they suggest that the father should get independent advice. If the father had gone to his solicitor or any man of business there is no doubt that they would have advised him not to enter the transaction as the house was his sole asset and the son's company was in a dangerous state.

Sir Eric Sachs made it clear that, in ordinary circumstances, a bank does not incur the duty consequent upon a special relationship where it obtains a guarantee from a customer. But once it is possible for a bank to be under that duty, it is, as in the present case, simply a question for "meticulous examination" of the particular facts to see whether that duty has arisen. On the special facts here it did arise and had been broken.

National Westminster Bank v Morgan [1985] 1 All ER 821

A husband and wife owned a home jointly. The husband was unable to meet his mortgage commitments and the building society threatened to seek possession for unpaid debts. The husband made refinancing arrangements with the bank secured by a mortgage in favour of the bank over the matrimonial home. The bank manager called at the home to get the wife to execute the charge. She did not wish the charge to cover her husband's business liabilities. The bank manager assured her, in good faith but incorrectly, that it did not. It was, in fact, unlimited in extent and could, therefore, extend to all the husband's liabilities to the bank, though it was the bank's intention to confine it to the amount needed to refinance the mortgage. The wife had not received independent legal advice before executing the mortgage. The husband and wife fell into arrears with their payments, and the bank obtained an order for possession of the home. Shortly afterwards, the husband died without owing the bank any business debts. The wife argued that the bank manager exercised undue influence over her and that a special relationship existed between her and the bank which required it to ensure that she received independent legal advice before entering into a further mortgage. She also sought to rely upon *Lloyd's Bank v Bundy*.

Lord Scarman came to the following conclusions:

1. A transaction would not be set aside on the grounds of undue influence unless it could be shown that it was manifestly disadvantageous to the party alleged to be influenced.
2. The basic principle was not a vague public policy (as formulated in *Allcard v Skinner*), but the prevention of victimisation of one party by another.
3. The transaction in the instant case was not unfair to the wife.
4. Although the doctrine of undue influence could extend to commercial transactions, including those between banker and customer, it could not be maintained on the present facts that the relationship was one in which the banker had a dominating influence.
5. The bank, therefore, was not under a duty to ensure that the wife had independent advice.

MANIFEST DISADVANTAGE

National Westminster Bank v Morgan [1985]

See point 1 above. Lord Scarman stated:

"A meticulous examination of the facts of the present case reveals that [the bank] never 'crossed the line'. Nor was the transaction unfair to the wife. The bank was, therefore, under no duty to ensure that she had independent advice. It was an ordinary banking transaction whereby the wife sought to save her home; and she obtained an honest and truthful explanation of the bank's intention which, notwithstanding the terms of the mortgage deed which in the circumstances the trial judge was right to dismiss as 'essentially theoretical', was correct; for no one had suggested that … the bank sought to make the wife liable, or to make her home the security, for any debt of her husband other than the loan and interest necessary to save the house from being taken away from them in discharge of their indebtedness to the building society."

BCCI v Aboody [1989] 2 WLR 759

A husband and wife owned a family company and the company's liabilities to its bank were secured, among other things, by charges of the wife's house. The bank sought to enforce the securities and the wife pleaded actual undue influence by the husband. Although the judge found that such influence had been established, he refused to set aside the charges as it had not been proved that they were manifestly disadvantageous to the wife (a point since overruled by the House of Lords in *CIBC Mortgages v Pitt* [1993]).

It was held by the Court of Appeal that manifest disadvantage for the purposes of the doctrine of undue influence had to be a disadvantage which was obvious as such to any independent and reasonable person who considered the transaction at the time with knowledge of all the relevant facts. The fact that the complaining party had been deprived of the power of choice (eg because his will had been overborne through the failure to draw his attention to the risks involved) was not of itself a manifest disadvantage rendering the transaction unconscionable. Furthermore, since the giving of a guarantee or charge always involved the risk that the guarantee might be called in or the charge enforced, the question whether the assumption of such a risk was manifestly disadvantageous to the giver of the guarantee or charge depended on balancing the seriousness of the risk of enforcement to the giver, in practical terms, against the benefits gained by the giver in accepting the risk.

There were no grounds for disagreeing with the judge's conclusion that on balance a manifest disadvantage had not been shown by the wife in respect of any of the six transactions, since although there were substantial potential liabilities and the family home was at risk as a result of the transactions, that was counterbalanced by the fact that the loans gave the company a reasonably good chance of surviving, in which case the potential benefits to the wife would have been substantial. Moreover, the evidence established that on balance the wife would have entered into the transactions in any event and accordingly it would not be right to grant her equitable relief as against the bank. The wife's appeal was therefore dismissed.

1.24 UNDUE INFLUENCE AND THIRD PARTIES

Barclays Bank v O'Brien [1993] 4 All ER 417

The husband was a shareholder in a company and arranged an overdraft facility of £135,000 for the company. The husband's liability to the bank was to be secured by a second charge over the matrimonial home, jointly owned by the husband and his wife. The husband persuaded the wife to sign the security documents by misrepresenting the situation, saying the facility was short-term and the charge was limited to £60,000. When the company's debts increased, the bank brought proceedings against the O'Briens to enforce the guarantee.

The judge gave judgment for the bank, finding that (1) the husband had not unduly influenced the wife and (2) that the husband had misrepresented the effect of the charge but that the bank was not responsible for that misrepresentation. The Court of Appeal held that the bank was under a duty, which it had not satisfied, to take reasonable steps to ensure that the wife had an adequate understanding of the transaction so that it was not enforceable against her except to the extent of £60,000. The bank's appeal to the House of Lords was dismissed, and they set aside the charge.

The House of Lords held that a wife who stood surety for her husband's debt and who had been induced by undue influence, misrepresentation or similar wrong had a right to have the transaction set aside if the third party (in this case the bank) had actual or constructive knowledge. Unless reasonable steps were taken to ascertain a) whether the transaction was of financial advantage to the wife, and b) if there were reasons to suspect that the debtor had committed a legal or equitable wrong which had induced the wife into the transaction, then there would be, at least, constructive knowledge. The bank, having failed to take any such steps to verify the situation, had constructive knowledge of the husband's wrongful misrepresentation. The wife was entitled to have the charge set aside.

The House also extended the principles applicable to husband and wife to (1) all cases where there is an emotional relationship between the cohabitees (whether homosexual or heterosexual), provided that the creditor is aware that the surety is cohabiting with the principal debtor; and (2) to other relationships (for example, parent and child) in which the creditor is aware that the surety reposes trust and confidence in relation to his financial affairs.

CIBC Mortgages v Pitt [1993] 4 All ER 433

A husband wanted to borrow money on the matrimonial home to buy stock market shares. The wife was unhappy about this but eventually agreed under pressure. They jointly applied for a loan, stating that the purpose of the loan was to pay off the existing mortgage and purchase a holiday home. The wife received no independent advice and no one suggested to

her that she should. She did not read the documents before signing them and did not know the amount being borrowed. When the stock market collapsed the husband defaulted on the loan repayments and the plaintiff applied for an order for possession of the house.

The judge held that the wife had been induced to sign by the husband's misrepresentation, fraud and duress but, since he had not acted as the bank's agent and this was not a case of the wife standing surety for the husband's debt but a loan jointly to husband and wife, the wife's claim failed. This decision was upheld on appeal.

The House of Lords held that while a claimant who could prove actual undue influence was entitled to have the challenged transaction set aside, the plaintiffs would only be affected if it could be established that they had actual or implied notice of the undue influence. In this case there was nothing to indicate that this was anything other than a normal loan to husband and wife's joint benefit. According to Lord Browne-Wilkinson, what distinguishes the case of the joint advance from the surety case is that, in the latter, there is the increased risk of undue influence having been exercised because, at least on its face, the guarantee by a wife of her husband's debts is not for her financial benefit. It is the combination of these two factors that puts the creditor on inquiry.

Barclays Bank v Coleman (2000) The Times, January 5.

The Court of Appeal held that manifest disadvantage, in the sense of clear and obvious disadvantage, remained a necessary ingredient of a wife's challenge on the ground of presumed undue influence of her husband to the validity of a bank's charge over the matrimonial home. But the House of Lords had signalled that it might not continue to be an essential ingredient indefinitely.

See photocopy of Law Report.

REBUTTING THE PRESUMPTION

Inche Noriah v Bin Omar [1928] All ER 189

The appellant brought an action against the respondent claiming that a deed of gift made between the parties should be set aside on the ground that the relationship between the parties at the time when the deed was executed was such as to raise a presumption of undue influence against the respondent, and that the presumption had not been rebutted.

Lord Hailsham LC stated: "But their Lordships are not prepared to accept the view that independent legal advice is the only way in which the presumption can be rebutted; nor are they prepared to affirm that independent legal advice, when given, does not rebut the presumption, unless it be shown that the advice was taken. It is necessary for the donee to prove that the gift was the result of the free exercise of independent will. The most obvious

way to prove this is by establishing that the gift was made after the nature and effect of the transaction had been fully explained to the donor by some independent and qualified person so completely as to satisfy the court that the donor was acting independently of any influence from the donee and with full appreciation of what he was doing…"

Re Craig (deceased) [1971] Ch 95

C, an old man of 84 years whose wife had died, employed Mrs M as secretary/companion. From the beginning she occupied a position of trust, and in addition to running the house she took a confidential part in running C's affairs. From the time of Mrs M's employment and C's death (January 1959 - August 1964) he gave her gifts worth £28,000 from his total assets of £40,000.

It was held by the Chancery Division that (1) All the gifts complained of were such as to satisfy the requirements to raise the presumption of undue influence, namely, that they could not be accounted for on the ground of the ordinary motives on which ordinary men act, and secondly, that the relationship between C and Mrs M involved such confidence by C in Mrs M as to place her in a position to exercise undue influence over him. (2) Mrs M failed to discharge the onus on her of establishing that the gifts were only made after 'full, free and informed discussion' so as to rebut the presumption of undue influence. The gifts would, therefore, be set aside.

Re Brocklehurst (deceased) [1978] Ch 14

Brocklehurst was a strong-minded, autocratic and eccentric old man who was used to commanding others and had served in the army in positions of command. He was impulsively generous. When he was in his eighties he lived alone and became friendly with the owner of a local garage. They had a common interest in shooting and B permitted the defendant to shoot rabbits on the estate. B wrote to the defendant saying that he wished to give him the shooting rights over his estate and pressed the defendant to instruct a solicitor to draw up a lease. B executed the lease. After B died, his executors brought an action against the defendant to have the lease set aside on the ground of undue influence. The Court of Appeal upheld the lease.

The Court of Appeal held that the nature of the relationship between the deceased and the defendant was not one of confidence and trust such as would give rise to a presumption of undue influence on the part of the defendant, for the evidence established that the relationship was one of friendship and did not indicate that it was such that the defendant had been under a duty to advise the deceased or had been in a position of dominance over him; on the contrary, it was the deceased who had tended to dominate the defendant.

But even if the relationship had been one that gave rise to a presumption of undue influence, the defendant had rebutted the presumption for in the circumstances the presumption was rebuttable not only by proof that the deceased had been independently

advised about the leases but also by proof that the gift of the leases had been the spontaneous and independent act of the deceased.

Royal Bank of Scotland v Etridge (No 2) [1998] 4 All ER 705

See photocopy of Law Report.

REMEDIES

TSB Bank v Camfield [1995] 1 All ER 951

Mr Camfield was a partner in a motor business. The partners requested the bank to provide the business with an overdraft facility of £30,000. The bank agreed, provided the partners executed a charge over their houses. Mrs Camfield duly executed the charge but did so under the impression, as the result of an innocent misrepresentation by the husband, that the maximum liability under the charge would be £15,000. That misapprehension was not corrected by the person advising her, even though the effect of the legal charge was to charge her beneficial interest in the house with an unlimited liability to meet the debts of the partnership, in which she had no financial interest. The business failed and the bank commenced proceedings against the Camfields.

The Court of Appeal held that where a wife was induced to execute a charge over the matrimonial home to meet the husband's debts by his innocent misrepresentation that the liability under the charge would not exceed a specified amount, whereas the charge in fact provided security for an unlimited liability, and the creditor was fixed with constructive notice of the husband's misrepresentation because it had failed to take reasonable steps to ensure that the wife understood the charge, the charge would be set aside in its entirety and could not be partially set aside or set aside on terms that it was a valid security for the specified amount for which the wife thought she was at risk. Since, on the evidence, the wife would not have entered into the charge if she had known its true nature and since her ignorance of the true nature of the charge resulted from the bank's failure to take reasonable steps to see that she was properly advised, it followed that the charge would be set aside in its entirety.

Dunbar Bank v Nadeem [1998] 3 All ER 876

See Law Report.

O'Sullivan v Management Agency & Music Ltd [1985] QB 428

The plaintiff sought to set aside for undue influence a number of management, sole agency, recording and publishing agreements and transfers of copyright. The defendant argued that the appropriate remedy, namely restitutio in integrum, was inapplicable in the

circumstances because the agreements had all been performed and the parties had irrevocably altered their positions, and that therefore the plaintiff was limited to obtaining damages instead of reconveyance of the copyrights and delivery up of the master tapes.

The Court of Appeal held that the plaintiff was not barred from having the contracts set aside by the fact that restitutio in integrum was impossible because the contracts had been performed. A contract entered into by a person in breach of a fiduciary relationship could be set aside in equity even though it was impossible to place the parties in the precise position in which they had been before, provided the court could achieve what was practically just between the parties by obliging the wrongdoer to give up his profits and advantages, while at the same time compensating him for any work he had actually performed under the contract.

Cheese v Thomas [1994] 1 All ER 35

The 88 year old plaintiff paid £43,000 to the defendant (his 36 year old great-nephew) to finance the purchase of a house in which the plaintiff was to live. The defendant borrowed £40,000 from a building society to make up the purchase price of £83,000 and the house, which it was agreed was to belong to the defendant on the plaintiff's death, was conveyed into the defendant's name and the plaintiff moved in. The plaintiff discovered that the defendant had allowed the mortgage payments to fall into arrears and decided to withdraw. He claimed repayment of the £43,000. The house was sold for £55,000 and £17,000 was left after redemption. The judge held that the transaction should be set aside because of the defendant's undue influence, and that the loss brought about by the fall in the value of the house should be shared between the parties in proportions of the purchase (ie, 43:40). The defendant appealed against the decision that the transaction was affected by undue influence; the plaintiff appealed against the decision that he should share a proportion of the loss.

The Court of Appeal held that justice required that each party should be returned as near to his original position as was possible and that the defendant should not be required to shoulder the whole of the loss brought about by the fall in the market value. Accordingly, each party should get back a proportionate share of the net proceeds of the house and the judge had correctly decided that the proceeds of sale should be divided between the parties in the proportions of 43:40. The appeals would therefore be dismissed.

Mahoney v Purnell [1996] 3 All ER 61

The plaintiff, M, operated a hotel business in partnership with P, his son-in-law. P wanted to run the hotel on his own. M was reluctant to sell his shares even though his financial position was precarious, but eventually he and P agreed a price of £200,000, calculated on the basis of an assessment of the company's assets and liabilities. The money was to be paid over ten years. The agreements were executed in March 1988. P later sold the hotel in 1989 for £3.275m and M commenced proceedings based on undue influence. Before trial of the

action, the company went into liquidation and the payments due to M under the agreements ceased, with some £80,000 outstanding. M's claims of undue influence against P succeeded and the question arose as to the appropriate equitable remedy in circumstances where the parties could not be restored to their former position.

The Court of Appeal held that since the company was in liquidation, the court was entitled in those circumstances to award compensation in equity to M equal to the March 1988 value of what he had surrendered under the agreements, with appropriate credit being given for what he had received under them. M was accordingly entitled to the sum of £202,131 in compensation from P.

Barclays Bank v Caplan (1997) The Times, December 12

It was held in the Chancery Division that at common law, where an instrument contained legally objectionable features which were unenforceable against one party, they might be severed from the rest of the instrument if (1) the unenforceable feature was capable of being removed by the excision of words, without the necessity of adding to or modifying the wording of what remained, and (2) its removal did not alter the character of the instrument or the balance of rights and obligations contained in it.

See Law Report.

1.25 DISCHARGE OF CONTRACT

A contract may be discharged by performance, agreement, breach, or frustration.

1. PERFORMANCE

THE GENERAL RULE

The general rule is that the parties must perform precisely all the terms of the contract in order to discharge their obligations.

For example, in contracts for the sale of goods, s13 Sale of Goods Act 1979 imposes the condition that the goods must correspond with the description. The precise requirement of s13 was illustrated in:

Re Moore and Landauer [1921] 2 KB 519.

The classic example of hardship caused by this rule is the case of:

Cutter v Powell (1795) 6 Term Rep 320.

MODIFICATION OF THE GENERAL RULE

The strict rule as to performance is mitigated in a number of instances:

A) DIVISIBLE CONTRACTS

A contract may be entire or divisible. An entire contract is one where the agreement provides that complete performance by one party is a condition precedent to contractual liability on the part of the other party. With a divisible contract, part of the consideration of one party is set off against part of the performance of the other. Contrast:

Sumpter v Hedges [1898] 1 QB 673
Roberts v Havelock (1832) 3 B. & Ad. 404.

B) ACCEPTANCE OF PARTIAL PERFORMANCE

Where the party to whom the promise of performance was made receives the benefit of partial performance of the promise under such circumstances that he is able to accept or reject the work and he accepts the work, then the promisee is obliged to pay a reasonable price for the benefit received.

But it must be possible to infer from the circumstances a fresh agreement by the parties that payment shall be made for the goods or services in fact supplied. See:

Christy v Row (1808) 1 Taunt 300.

C) COMPLETION OF PERFORMANCE PREVENTED BY THE PROMISEE

Where a party to an entire contract is prevented by the promisee from performing all his obligations, then he can recover a reasonable price for what he has in fact done on a quantum meruit basis in an action in quasi-contract. See:

Planche v Colburn (1831) 8 Bing 14.

D) SUBSTANTIAL PERFORMANCE

When a person fully performs the contract, but subject to such minor defects that he can be said to have substantially performed his promise, it is regarded as far more just to allow him to recover the contract price reduced by the extent to which his breach of contract lessened the value of what was done, than to leave him with no right of recovery at all. Contrast:

Dakin v Lee [1916] 1 KB 566
Bolton v Mahadeva [1972] 2 All ER 1322.

E) TENDER OF PERFORMANCE

Tender of performance is equivalent to performance in the situation where party (a) cannot complete performance without the assistance of party (b) and party (a) makes an offer to perform which party (b) refuses. See:

Startup v M'Donald (1843) 6 M&G 593.

STIPULATIONS AS TO TIME OF PERFORMANCE

At common law, in the absence of contrary intention, time was regarded as being of the essence. Thus if a party did not perform on time he could not enforce the contract against the other party. Section 41 Law of Property Act 1925 modified this common law rule by providing that the equitable principle shall prevail with the result that if time is not of the essence, a right to damages accrues but not a right to terminate the contract.

In equity time was not regarded as being of the essence, except in three circumstances:

A) The contract expressly states that time is of the essence.
B) Time was made of the essence by the giving of notice (during the currency of the contract) to perform within a reasonable time.
C) Where from the nature of the surrounding circumstances or from the subject matter of the contract it is clear that time is of the essence.

2. AGREEMENT

The general rule is that what has been created by agreement may be extinguished by agreement.

An agreement by the parties to an existing contract to extinguish the rights and obligations that have been created is itself a binding contract, provided that it is made under seal or supported by consideration. Where the agreement for discharge is not under seal, the legal position varies according to whether the discharge is bilateral or unilateral:

BILATERAL DISCHARGE

Bilateral discharge occurs whenever both parties to the contract have some right to surrender, eg where there has been non-performance by either party, or is partly performed by one or both parties.

The agreement by the parties to discharge their contract may be designed to have one of several effects:

(A) ACCORD AND SATISFACTION
The parties may intend to rescind their present agreement and nothing more. Where there

is an agreement mutually to release the other from the obligations under the first agreement, there is an accord and satisfaction.

(B) RESCISSION AND SUBSTITUTION
The parties may intend rescission of the original contract and substitution of a new contract.

(C) VARIATION
The parties may agree on the variation of an existing contract, ie modifying or altering the terms of the original agreement.

(D) WAIVER
Where one party voluntarily accedes to a request by another to forbear his right to strict performance of the contract, or where he represents to another that he will not insist upon his right to strict performance of the contract, the court may hold that he has waived his right to performance as initially contemplated by the parties.

UNILATERAL DISCHARGE

Unilateral discharge takes place where only one party has rights to surrender. Where one party has entirely performed his part of the agreement, he is no longer under obligations but has rights to compel the performance of the agreement by the other party.

For unilateral discharge, unless the agreement is under seal, consideration must be furnished in order to make the agreement enforceable, ie accord and satisfaction.

3. BREACH

A failure to perform the terms of a contract constitutes a breach. A breach which is serious enough to give the innocent party this option of treating the contract as discharged can occur in one of two ways:

· either one party may show by express words or by implications from his conduct at some time before performance is due that he does not intend to observe his obligations under the contract (anticipatory breach); or
· he may in fact break a condition or otherwise break the contract in such a way that it amounts to a substantial failure of consideration.

One preliminary question, in cases of anticipatory breach, is to ascertain whether, once repudiation has been communicated to the innocent party, that party accepts the repudiation or not. The question of whether silence/inaction can amount to acceptance of repudiation was considered in:

Vitol SA v Norelf Ltd [1996] 3 All ER 193.

The innocent party is not under any obligation to wait until the date fixed for performance before commencing his action, but may immediately treat the contract as at an end and sue for damages. See:

Hochster v De La Tour (1853) 2 E&B 678.

If within a reasonable time the innocent party does not indicate that he accepts the other party's repudiation so that the contract is discharged, then the contract remains open for the benefit of, and the risk of, both parties. The breach was not accepted in:

Avery v Bowden (1855) 5 E&B 714.

It appears that the right to keep the contract alive subsists even where the innocent party is increasing the amount, and not mitigating, the damages which he may receive from the party in breach. See:

White & Carter v McGregor [1962] AC 413.

Where the innocent party elects to treat the contract as continuing (ie, he affirms it) the affirmation can be regarded as a species of waiver. The innocent party waives his right to treat the contract as repudiated and may be estopped from changing his election. See:

Panchaud Freres SA v Establissments General Grain Co [1970] 1 Lloyd's Rep 53.

If the innocent party elects to affirm a contract after an anticipatory breach by the other party, he is not absolved from tendering further performance of his own obligations under the contract. Consequently, the repudiating party could escape liability if the affirming party was subsequently in breach of the contract. See:

Fercometal Sarl v Mediterranean Shipping Co [1988] 2 All ER 742.

Whether the anticipatory breach amounts to a repudiation depends on the actual circumstances of the case. Lord Selborne stated in *Mersey Steel v Naylor Benzon* (1884) 9 App Cas 434:

"you must examine what (the) conduct is to see whether it amounts to a renunciation, to an absolute refusal to perform the contract and whether the other party may accept it as a reason for not performing his part."

The difficulty that can arise in determining whether the conduct amounts to a repudiation is illustrated by a comparison of two decisions in the House of Lords:

Federal Commerce & Navigation v Molena Alpha [1979] AC 757
Woodar Investment v Wimpey Construction [1980] 1 WLR 277.

4. FRUSTRATION

The doctrine of frustration operates in situations where it is established that due to subsequent change in circumstances, the contract is rendered impossible to perform, or it has become deprived of its commercial purpose by an event not due to the act or default of either party.

Frustration is not to be confused with initial impossibility, which may render the contract void ab initio. See *Couturier v Hastie* (1856) 5 HL Cas 673 (Handout on Mistake).

TESTS FOR FRUSTRATION

There are two alternative tests for frustration:

(1) The implied term theory, as in:

Taylor v Caldwell (1863) 3 B&S 826.

Lord Loreburn explained in *FA Tamplin v Anglo-Mexican Petroleum* [1916] 2 AC 397, that the court:

'… can infer from the nature of the contract and the surrounding circumstances that a condition which was not expressed was a foundation on which the parties contracted … Were the altered conditions such that, had they thought of them, the parties would have taken their chance of them, or such that as sensible men they would have said "if that happens of course, it is all over between us".'

(2) The radical change in the obligation test. This was adopted by the majority of the House of Lords in:

Davis Contractors v Fareham UDC [1956] AC 696.

In *National Carriers v Panalpina* [1981] AC 675, Lord Wilberforce was reluctant to choose between the theories. He took the view that they merged one into the other and that the choice depends upon "what is most appropriate to the particular contract under consideration".

EXAMPLES OF FRUSTRATION

A) DESTRUCTION OF THE SPECIFIC OBJECT
ESSENTIAL FOR PERFORMANCE OF THE CONTRACT

The destruction of the specific object essential for performance of the contract will frustrate it. See:

Taylor v Caldwell (1863) (above).

B) PERSONAL INCAPACITY

Personal incapacity where the personality of one of the parties is significant may frustrate the contract:

Condor v The Baron Knights [1966] 1 WLR 87
Phillips v Alhambra Palace Co [1901] 1 QB 59
Graves v Cohen (1929) 46 TLR 121
FC Shepherd v Jeromm [1986] 3 All ER 589.

C) THE NON-OCCURENCE OF A SPECIFIED EVENT

The non-occurence of a specified event may frustrate the contract. Compare the leading cases:

Krell v Henry [1903] 2 KB 740
Herne Bay Steamboat Co v Hutton [1903] 2 KB 683.

D) INTERFERENCE BY THE GOVERNMENT

Interference by the government may frustrate a contract. See:

Metropolitan Water Board v Dick Kerr [1918] AC 119.

E) SUPERVENING ILLEGALITY

A contract may become frustrated if it later becomes illegal. See:

Denny, Mott & Dickinson v James Fraser [1944] AC 265
Re Shipton, Anderson and Harrison Brothers [1915] 3 KB 676.

F) DELAY

Inordinate and unexpected delay may frustrate a contract. The problem is to know how long a party must wait before the delay can be said to be frustrating. See:

Jackson v Union Marine Insurance (1873) LR 10 CP 125.

LIMITATIONS OF THE DOCTRINE

· 'The doctrine of frustration must be applied within very narrow limits', per Viscount Simmonds in *Tsakiroglou* [1961] (below).
· Lord Roskill said that the doctrine of frustration was 'not lightly to be invoked to relieve contracting parties of the normal consequences of imprudent commercial bargains', in *Pioneer Shipping v BTP Tioxide* [1982] AC 724.

A) EXPRESS PROVISION FOR FRUSTRATION

The doctrine of frustration cannot override express contractual provision for the frustrating event.

B) MERE INCREASE IN EXPENSE OR LOSS OF PROFIT

The mere increase in expense or loss of profit is not a ground for frustration. See:

Davis Contractors v Fareham UDC [1956] AC 696
Tsakiroglou v Noblee Thorl [1961] 2 All ER 179.

C) FRUSTRATION MUST NOT BE SELF-INDUCED

See:

Maritime National Fish v Ocean Trawlers [1935] AC 524.

D) FORESEEABILITY OF THE FRUSTRATING EVENT

A party cannot rely on an event which was, or should have been, foreseen by him but not by the other party. See:

Walton Harvey Ltd v Walker & Homfrays Ltd [1931] 1 Ch 274.

EFFECTS OF FRUSTRATION

The Law Reform (Frustrated Contracts) Act 1943 was passed to provide for a just apportionment of losses where a contract is discharged by frustration. (For the previous inflexible common law rules see ILEx Textbook, 13.5.4)

(A) RECOVERY OF MONEY PAID

Section 1(2) provides three rules:

· Money paid before the frustrating event is recoverable, and
· Money payable before the frustrating event ceases to be payable, whether or not there has been a total failure of consideration.
· If, however, the party to whom such sums are paid/payable incurred expenses before discharge in performance of the contract, the court may award him such expenses up to the limit of the money paid/payable before the frustrating event.

For an example, see:

Gamerco v ICM/Fair Warning (Agency) Ltd [1995] 1 WLR 1226.

(B) VALUABLE BENEFIT

Section 1(3) provides:

· If one party has, by reason of anything done by the other party in performance of the contract, obtained a valuable benefit (other than money) before the frustrating event, he may be ordered to pay a sum in respect of it, if the court considers it just, having regard to all the circumstances of the case.

A case has discussed, inter alia, the meaning of the words 'valuable benefit'. See:

BP Exploration v Hunt [1982] 1 All ER 925.

(C) SCOPE OF THE 1943 ACT

Section 2(3) permits contracting out.

Section 2(4) provides that the Act does not apply where wholly performed contractual obligations can be severed from those affected by the frustrating event.

Section 2(5) provides that the Act does not apply to:

· Contracts containing a provision to meet the case of frustration;
· Charterparties (except time charterparties or charterparties by demise);
· Contracts for the carriage of goods by sea;
· Contracts of insurance;
· Contracts for the sale of specific goods, which perish before the risk has passed to the buyer.

1.26 CASES ON DISCHARGE OF CONTRACT

1. PERFORMANCE

THE GENERAL RULE

Re Moore and Landauer [1921] 2 KB 519

There was an agreement for the sale of 3,000 tins of canned fruit packed in cases of 30 tins. When delivered it was discovered that half the cases contained only 24 tins although the total number of tins was still 3,000. The market value was not affected. The Court of Appeal held that notwithstanding that there was no loss to the buyer, he could reject the whole

consignment because of the breach of s13 of the Sale of Goods Act (goods must correspond with the description).

Cutter v Powell (1795) 6 Term Rep 320

A seaman who was to be paid his wages after the end of a voyage died just a few days away from port. His widow was not able to recover any of his wages because he had not completed performance of his contractual obligation. However, this situation is now provided for by the Merchant Shipping Act 1970.

MODIFICATION OF THE GENERAL RULE

Sumpter v Hedges [1898] 1 QB 673

The plaintiff agreed to erect upon the defendant's land two house and stables for £565. He did part of the work to the value of about £333 and then abandoned the contract. The defendant completed the buildings. The Court held that the plaintiff could not recover the value of the work done, as he had abandoned the contract.

Roberts v Havelock (1832) 3 B. & Ad. 404

A shipwright agreed to repair a ship. The contract did not expressly state when payment was to be made. He chose not to go on with the work. It was held that the shipwright was not bound to complete the repairs before claiming some payment.

Note: GH Treitel, *The Law of Contract*, states (at p702): In such cases the question whether a particular obligation is entire or severable is one of construction; and where a party agrees to do work under a contract, the courts are reluctant to construe the contract so as to require complete performance before any payment becomes due. "Contracts may be so made; but they require plain words to shew that such a bargain was really intended": *Button v Thompson* (1869) LR 4 CP.

Christy v Row (1808) 1 Taunt 300

A ship freighted to Hamburg was prevented 'by restraint of princes' from arriving. Consignees accepted the cargo at another port to which they had directed it to be delivered. The consignees were held liable upon an implied contract to pay freight pro rata itineris (ie, for freight at the contract rate for the proportion of the voyage originally undertaken which was actually accomplished). A contract was implied from their directions re alternative port of delivery.

Planche v Colburn (1831) 8 Bing 14

The plaintiff was to write a book on 'Costume and Ancient Armour' for a series, and was to receive £100 on completion of the book. After he had done the necessary research but

before the book had been written, the publishers abandoned the series. He claimed alternatively on the original contract and on a quantum meruit.

The court held that: (a) the original contract had been discharged by the defendants' breach; (b) no new contract had been substituted; and (c) the plaintiff could obtain 50 guineas as reasonable remuneration on a quantum meruit. This claim was independent of the original contract and was based on quasi-contract.

Dakin v Lee [1916] 1 KB 566

The defendants promised to build a house according to specification and failed to carry out exactly all the specifications, for example, concrete not four feet deep as specified, wrong joining of certain rolled steel joists and concrete not properly mixed. The Court of Appeal held that the builders were entitled to recover the contract price, less so much as ought to be allowed in respect of the items found to be defective.

Bolton v Mahadeva [1972] 2 All ER 1322

The plaintiff agreed with the defendant that he would install central heating in the defendant's house for a lump sum of £560. When the work was completed, the defendant complained that it was defective and refused to pay. The judge found that the flue was defective so that it gave off fumes making the rooms uncomfortable, and the system was inefficient in that the amount of heat varied from one room to another. The cost of rectifying these defects was £174. The Court of Appeal held that the plaintiff was not entitled to recover as there had been no substantial performance.

Startup v M'Donald (1843) 6 M&G 593

The plaintiffs agreed to sell 10 tons of oil to the defendant and to deliver it to him 'within the last 14 days of March', payment to be in cash at the end of that period. Delivery was tendered at 8.30pm on 31 March. The defendant refused to accept or pay for the goods because of the late hour. The court held that the tender was equivalent to performance and the plaintiffs were entitled to recover damages for non-acceptance. Today note s29(5) SGA 1979: Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour; and what is a reasonable hour is a question of fact.

2. AGREEMENT

No cases.

3. BREACH

Vitol SA v Norelf Ltd [1996] 3 All ER 193

The repudiating party notified the other that they considered the contract at an end. However, no action was taken by the innocent party, either to act on the repudiation or to

affirm the contract, on receipt of this information. The Court of Appeal stated that inactivity did not show the party's intentions one way or another and did not amount to acceptance of repudiation or serve as affirmation either. This decision was reversed by the House of Lords, who held that silence or inaction can amount to acceptance of a wrongful repudiation of a contract.

Hochster v De La Tour (1853) 2 E&B 678

An employer told is employee (a travelling courier) before the time for performance arrived that he would not require his services. The courier sued for damages at once. The court held that he was entitled to do so.

Avery v Bowden (1855) 5 E&B 714

A charterparty provided that a ship should proceed to Odessa and there take a cargo from the charterer's agent. The ship arrived at Odessa and the master demaned a cargo, but the agent could not provide one. The ship's master continued to ask for one. A war broke out. The charterer sued. The court held, inter alia, that if the agent's conduct amounted to an anticipatory repudiation of the contract, the master had elected to keep the contract alive until it was discharged by frustration on the outbreak of war.

White & Carter v McGregor [1961] 3 All ER 1178

The plaintiff advertising contractors agreed with the defendant garage proprietor to display advertisements for his garage for three years. The defendant repudiated the agreement and cancelled on the same day. The plaintiffs refused to cancel and performed their obligations. They sued for the contract price. The House of Lords held, by a majority of 3:2 that they were entitled to the full contract price.

See law report.

Panchaud Freres SA v Establissments General Grain Co [1970] 1 Lloyd's Rep 53

Buyers of maize rejected it on a ground which was subsequently found to be inadequate. Three years later, they discovered that the grain had not been shipped within the period stipulated for in the contract. They, therefore, sought to justify their rejection on this ground. The Court of Appeal held that they were not entitled to do so. Lord Denning MR stated that the buyers were estopped by their conduct from setting up late delivery as a ground for rejection because they had led the sellers to believe they would not do so.

Fercometal Sarl v Mediterranean Shipping Co [1988] 2 All ER 742

Charterers entered into a charterparty with the shipowners. The charterers cancelled the charterparty and engaged a different vessel. The owners did not accept the repudiation which was premature because it was given in advance of the cancellation date. When the

vessel arrived the owners gave notice of readiness even though they were not in fact ready to load the charterers' cargo. The charterers rejected the notice and proceeded to load their cargo onto the other vessel. The shipowners brought an action for damages.

The House of Lords held that where a party to a contract wrongfully repudiated his contractual obligations before he was required to perform those obligations, the innocent party could either affirm the contract, treating it as still in force, or treat it as being discharged. If he elected to affirm the contract he was not absolved from tendering his own performance under the contract. Thus if a repudiation by the anticipatory breach was followed by affirmation of the contract, the repudiating party could escape liability if the affirming party was subsequently in breach of his obligations under the contract.

On the facts of the case the owners, having affirmed the contract when they refused to accept the charterers premature repudiation, could avoid the cancellation clause in the charterparty only by tendering the vessel ready to load on time, which they had failed to do, or by establishing, which they could not do, that their failure was due to their acting on a representation by the charterers that they had given up their option to cancel.

Federal Commerce & Navigation v Molena Alpha [1979] AC 757

Clause 9 of a charter provided that the charterers were to sign bills of lading stating the freight had been correctly paid. After a dispute arose concerning deductions made by the charterers, the shipowners withdrew this authority contrary to the terms of the charter. The master was instructed not to sign bills of lading with the indorsement 'freight pre paid' or which did not contain an indorsement giving the shipowners a lien over the cargo for freight. This meant that the charterers were put in an impossible position commercially. The charterers treated the owner's actions as a repudiation of the charter.

The House of Lords held that although the term broken was not a condition, the breach went to the root of the contract by depriving the charterers of virtually the whole benefit of the contract because the issue of such bills was essential to the charterers' trade. Therefore, the owner's conduct constituted a wrongful repudiation of the contract.

Woodar Investment v Wimpey Construction [1980] 1 WLR 277

Wimpey contracted to buy land for £850,000 and agreed to pay £150,000 on completion to a third party, Transworld Trade Ltd. The contract allowed the purchaser to rescind the contract if before completion a statutory authority 'shall have commenced' to acquire the property by compulsory purchase. At the date of the contract both parties knew that a draft compulsory purchase order had been made. Wimpey purported to terminate relying on this provision, and Woodar sought damages alleging that this amounted to a wrongful repudiation. Their damages claim included the loss suffered by the third party (as to which, see Privity of Contract).

The House of Lords held, by a majority of 3:2, that in order to constitute a renunciation of the contract there had to be an intention to abandon the contract and instead of abandoning the contract Wimpey were relying on its terms as justifying their right to terminate.

4. FRUSTRATION

Taylor v Caldwell (1863) 3 B&S 826

For facts, see below. Blackburn J stated: "The principle seems to us to be that, in contracts in which the performance depends on the continued existence of a given person or thing, a condition is implied that the impossibility of performance arising from the perishing of the person or thing shall excuse the performance."

Davis Contractors v Fareham UDC [1956] AC 696

For facts, see below. Lords Reid and Radcliffe stated that the 'radical change in the obligation' test required the court to:

1. Construe the contractual terms in the light of the contract and surrounding circumstances at the time of its creation.
2. Examine the new circumstances and decide what would happen if the existing terms are applied to it.
3. Compare the two contractual obligations and see if there is a radical or fundamental change.

Taylor v Caldwell (1863) 3 B&S 826

Caldwell agreed to let a music hall to Taylor so that four concerts could be held there. Before the date of the first concert, the hall was destroyed by fire. Taylor claimed damages for Caldwell's failure to make the premises available. The court held that the claim for breach of contract must fail since it had become impossible to fulfil. The contractual obligation was dependent upon the continued existence of a particular object. See above for the quote of Blackburn J.

Condor v The Baron Knights [1966] 1 WLR 87

A drummer engaged to play in a pop group was contractually bound to work on seven nights a week when work was available. After an illness, Condor's doctor advised that it was only safe to employ him on four nights a week, although Condor himself was willing to work every night. It was necessary to engage another drummer who could safely work on seven nights each week. The court held that Condor's contract of employment had been frustrated in a commercial sense. It was impracticable to engage a stand-in for the three nights a week

when Condor could not work, since this involved double rehearsals of the group's music and comedy routines.

Phillips v Alhambra Palace Co [1901] 1 QB 59

One partner in a firm of music hall proprietors died after a troupe of performers had been engaged. The contract with the performers was held not to be frustrated because the contract was not of a personal nature, and could be enforced against the surviving partners.

Graves v Cohen (1929) 46 TLR 121

The court held that the death of a racehorse owner frustrated the contract with his employee, a jockey, because the contract created a relationship of mutual confidence.

FC Shepherd v Jeromm [1986] 3 All ER 589

The Court of Appeal held that a sentence of imprisonment imposed on an employee was capable of frustrating the employee's contract of employment if the sentence was such that it rendered the performance of the contract radically different from that which the parties contemplated when they entered into the contract.

Krell v Henry [1903] 2 KB 740

Henry hired a room from Krell for two days, to be used as a position from which to view the coronation procession of Edward VII, but the contract itself made no reference to that intended use. The King's illness caused a postponement of the procession. It was held that Henry was excused from paying the rent for the room. The holding of the procession on the dates planned was regarded by both parties as basic to enforcement of the contract.

Herne Bay Steamboat Co v Hutton [1903] 2 KB 683

Herne Bay agreed to hire a steamboat to Hutton for a period of two days for the purpose of taking passengers to Spithead to cruise round the fleet and see the naval review on the occasion of Edward VII's coronation. The review was cancelled, but the boat could have been used to cruise round the assembled fleet. It was held that the contract was not frustrated. The holding of the naval review was not the only event upon which the intended use of the boat was dependent. The other object of the contract was to cruise round the fleet, and this remained capable of fulfilment.

Metropolitan Water Board v Dick Kerr [1918] AC 119

Kerr agreed to build a reservoir for the Water Board within six years. After two years, Kerr were required by a wartime statute to cease work on the contract and to sell their plant. The contract was held to be frustrated because the interruption was of such a nature as to make the contract, if resumed, a different contract.

Denny, Mott & Dickinson v James Fraser [1944] AC 265

A contract for the sale and purchase of timber contained an option to purchase a timber yard. By a wartime control order, trading under the agreement became illegal. One party wanted to exercise the option. It was held that the order had frustrated the contract so the option could not be exercised.

Re Shipton, Anderson and Harrison Brothers [1915] 3 KB 676

A contract was concluded for the sale of wheat lying in a warehouse. The Government requisitioned the wheat, in pursuance of wartime emergency regulations for the control of food supplies, before it had been delivered, and also before ownership in the goods had passed to the buyer under the terms of the contract. It was held that the seller was excused from further performance of the contract as it was now impossible to deliver the goods due to the Government's lawful requisition.

Jackson v Union Marine Insurance (1873) LR 10 CP 125

A ship was chartered in November 1871 to proceed with all possible despatch, danger and accidents of navigation excepted, from Liverpool to Newport where it was to load a cargo of iron rails for carriage to San Francisco. She sailed on 2 January, but the next day ran aground in Caernarvon Bay. She was refloated by 18 February and taken to Liverpool, where she underwent extensive repairs, which lasted till August. On 15 February, the charterers repudiated the contract.

The court held that such time was so long as to put an end in a commercial sense to the commercial speculation entered upon by the shipowner and the charterers. The express exceptions were not intended to cover an accident causing such extensive damage. The contract was to be considered frustrated.

LIMITATIONS OF THE DOCTRINE

Davis Contractors v Fareham UDC [1956] AC 696

The plaintiff agreed to build 78 houses in eight months at a fixed price. Due to bad weather, and labour shortages, the work took 22 months and cost £17,000 more than anticipated. The builders said that the weather and labour shortages, which were unforeseen, had frustrated the contract, and that they were entitled to recover £17,000 by way of a quantum meruit. The House of Lords held that the fact that unforeseen events made a contract more onerous than was anticipated did not frustrate it.

Tsakiroglou v Noblee Thorl [1961] 2 All ER 179

T agreed to sell Sudanese groundnuts to NT, the nuts to be shipped from Port Sudan to Hamburg, November/December 1956. As a result of the 'Suez crisis', the Suez Canal was closed from 2 November 1956 until April 1957. T failed to deliver, arguing that shipment round the Cape of Africa was commercially and fundamentally different. The court held that the contract was not frustrated. T were, therefore, liable for breach - the change in circumstances was not fundamental.

Maritime National Fish v Ocean Trawlers [1935] AC 524

Maritime chartered from Ocean a vessel which could only operate with an otter trawl. Both parties realised that it was an offence to use such a trawl without a government licence. Maritime was granted three such licences, but chose to use them in respect of three other vessels, with the result that Ocean's vessels could not be used. It was held that the charterparty had not been frustrated. Consequently Maritime was liable to pay the charter fee. Maritime freely elected not to licence Ocean's vessel, consequently their inability to use it was a direct result of their own deliberate act.

Walton Harvey Ltd v Walker & Homfrays Ltd [1931] 1 Ch 274

The defendant's granted the plaintiffs the right to display an advertising sign on the defendant's hotel for seven years. Within this period the hotel was compulsorily acquired, and demolished, by a local authority acting under statutory powers. The defendants were held liable in damages. The contract was not frustrated because the defendant's knew, and the plaintiffs did not, of the risk of compulsory acquisition. They could have provided against that risk, but they did not.

EFFECTS OF FRUSTRATION

Gamerco v ICM/Fair Warning (Agency) Ltd [1995] 1 WLR 1226

The plaintiffs, pop concert promoters, agreed to promote a concert to be held by the defendant group at a stadium in Spain. However, the stadium was found by engineers to be unsafe and the authorities banned its use and revoked the plaintiffs' permit to hold the concert. No alternative site was at that time available and the concert was cancelled. Both parties had incurred expenses in preparation for the concert; in particular the plaintiffs had paid the defendants $412,500 on account. The plaintiffs sought to recover the advance payment under s1(2) Law reform (Frustrated Contracts) Act 1943, and the defendants counterclaimed for breach of contract by the plaintiffs in failing to secure the permit for the concert.

It was an implied term of the contract that the plaintiffs would use all reasonable endeavours to obtain a permit, yet once the permit was granted they could not be required to guarantee that it would not be withdrawn. The contract was frustrated essentially because the stadium was found to be unsafe, a circumstance beyond the control of the

plaintiffs. The revocation of the permit, subsequent to its being obtained by the plaintiffs, was not the frustrating event; the ban on the use of the stadium was. Under s1 of the 1943 Act, the plaintiffs were entitled to recover advance payments made to the defendants. The court did have a discretion to allow the defendants to offset their losses against this, but in all the circumstances of the present case the court felt that no deduction should be made in favour of the defendants and their counterclaim should be dismissed.

BP Exploration v Hunt [1982] 1 All ER 925

See law report at p939C-p940C.

LAW REFORM (FRUSTRATED CONTRACTS) ACT 1943

1. Adjustment of rights and liabilities of parties to frustrated contracts.

(1) Where a contract governed by English law has become impossible of performance or been otherwise frustrated, and the parties thereto have for that reason been discharged from the further performance of the contract, the following provisions of this section shall subject to the provisions of section two of this Act, have effect in relation thereto.

(2) All sums paid or payable to any party in pursuance of the contract before the time when the parties were so discharged (in this Act referred to as "the time of discharge") shall, in the case of sums so paid, be recoverable from him as money received by him for the use of the party by whom the sums were paid, and, in the case of sums so payable, cease to be so payable:
Provided that, if the party to whom the sums were so paid or payable incurred expenses before the time of discharge in, or for the purpose of, the performance of the contract, the court may, if it considers it just to do so having regard to all the circumstances of the case, allow him to retain or, as the case may be, recover the whole or any part of the sums so paid or payable, not being an amount in excess of the expenses so incurred.

(3) Where any party to the contract has, by reason of anything done by any other party thereto in, or for the purpose of, the performance of the contract, obtained a valuable benefit (other than a payment of money to which the last foregoing subsection applies) before the time of discharge there shall be recoverable from him by the said other party such sum (if any), not exceeding the value of the said benefit to the party obtaining it, as the court considers just, having regard to all the circumstances of the case and, in particular,-
(a) the amount of any expenses incurred before the time of discharge by the benefited party in, or for the purpose of, the performance of the contract, including any sums paid or payable by him to any other party in pursuance of the contract and retained or recoverable by that party under the last foregoing subsection, and
(b) the effect, in relation to the said benefit, of the circumstances giving rise to the frustration of the contract.

(4) In estimating, for the purposes of the foregoing provisions of this section, the amount of any expenses incurred by any party to the contract, the court may, without prejudice to the generality of the said provisions, include such sum as appears to be reasonable in respect of overhead expenses and in respect of any work or services performed personally by the said party.

(5) In considering whether any sum ought to be recovered or retained under the foregoing provisions of this section by any party to the contract, the court shall not take into account any sums which have, by reason of the circumstances giving rise to the frustration of the contract, become payable to that party under any contract of insurance unless there was an obligation to insure imposed by an express term of the frustrated contract or by or under any enactment.

(6) Where any person has assumed obligations under the contract in consideration of the conferring of a benefit by any other party to the contract upon any other person, whether a party to the contract or not, the court may, if in all the circumstances of the case it considers it just to do so, treat for the purposes of subsection (3) of this section any benefit so conferred as a benefit obtained by the person who has assumed the obligations as aforesaid.

2. Provision as to application of this Act.

(1) This Act shall apply to contracts, whether made before or after the commencement of this Act, as respects which the time of discharge is on or after the first day of July, nineteen hundred and forty-three, but not to contracts as respects which the time of discharge is before the said date.
(2) This Act shall apply to contracts to which the Crown is a party in like manner as to contracts between subjects.

(3) Where any contract to which this Act applies contains any provision which, upon the true construction of the contract, is intended to have effect in the event of circumstances arising which operate, or would but for the said provision operate, to frustrate the contract, or is intended to have effect whether such circumstances arise or not, the court shall give effect to the said provision and shall only give effect to the foregoing section of this Act to such extent, if any, as appears to the court to be consistent with the said provision.

(4) Where it appears to the court that a part of any contract to which this Act applies can properly be severed from the remainder of the contract, being a part wholly performed before the time of discharge, or so performed except for the payment in respect of that part of the contract of sums which are or can be ascertained under the contract, the court shall treat that part of the contract as if it were a separate contract and had not been frustrated and shall treat the foregoing section of this Act as only applicable to the remainder of that contract.

(5) This Act shall not apply-
(a) to any charterparty, except a time charterparty or a charterparty by way of demise, or to any contract (other than a charterparty) for the carriage of goods by sea; or
(b) to any contract of insurance, save as is provided by subsection (5) of the foregoing section; or
(c) to any contract to which [section 7 of the Sale of Goods Act 1979] (which avoids contracts for the sale of specific goods which perish before the risk has passed to the buyer) applies, or to any other contract for the sale, or for the sale and delivery, of specific goods, where the contract is frustrated by reason of the fact that the goods have perished.

3. Short title and interpretation.

(1) This Act may be cited as the Law Reform (Frustrated Contracts) Act, 1943.

(2) In this Act the expression "court" means, in relation to any matter, the court or arbitrator by or before whom the matter falls to be determined.

1.27 REMEDIES FOR BREACH 1 - DAMAGES

1. CAUSATION

The plaintiff must show that his loss was one which resulted from a breach of contract by the defendant (a direct causal link).

An act of the defendant in a sequence of events leading to a loss might not be held to be the cause of the loss. For example, a shipowner was not liable to a charterer when, as a result of delay, the ship ran into a typhoon, as such a catastrophe may occur anywhere: *The Monarch SS Co Case* [1949] AC 196.

If there are two causes of the state of affairs resulting in damage, and both causes have equal effect, one will be sufficient to carry a judgment for damages. See:

Smith, Hogg & Co v Black Sea Insurance [1940] AC 997.

An intervening act of a third party which itself causes the loss to the plaintiff, or aggravates the loss, caused by the defendant's breach, will not absolve the defendant from liability if the intervening act was reasonably foreseeable (the *Victoria Laundry* and *The Heron II* principles, below). Compare:

Stansbie v Troman [1948] 2 KB 48
Weld-Blundell v Stephens [1920] AC 956.

2. REMOTENESS OF DAMAGE

Not every type of damage caused to the plaintiff as a result of the breach of contract will be recoverable. If the loss flowing from the breach of contract is too remote then it cannot be recovered. Losses, to be recoverable, must have been within the reasonable contemplation of the parties. See:

Hadley v Baxendale (1849) 9 Exch 341.

Damages are recoverable under two limbs under *Hadley v Baxendale*: (i) Damages which may fairly and reasonably be considered as arising naturally from the breach; (ii) Damages which may reasonably be supposed to have been in the contemplation of the parties, as liable to result from the breach, at the time of the contract.

The Court of Appeal took the opportunity to review and restate the principles governing the measure of damages in:

Victoria Laundry v Newman Industries [1949] 2 KB 528.

The principles relating to remoteness of damage were further considered in the House of Lords and given greater refinement in:

The Heron II [1969] 1 AC 350.

The effect of "the two limbs" in *Hadley v Baxendale* is as follows:-

Losses which occur "in the ordinary course of things" only are recoverable under the first limb. See:

Pilkington v Wood [1953] Ch 770.

The defendant's knowledge of special circumstances under the second limb is not in itself sufficient to make him liable. There must be knowledge and acceptance by the defendant of the purpose and intention of the plaintiff. Compare:

Horne v Midland Railway (1873) LR 8 CP 131
Simpson v L & N Railway (1876) 1 QBD 274.

3. MITIGATION OF LOSS

It is the duty of every plaintiff to mitigate his loss, that is, to do his best not to increase the amount of damage done. There are three rules:

(i) The plaintiff cannot recover for loss which the plaintiff could have avoided by taking reasonable steps.

(ii) The plaintiff cannot recover for any loss he has actually avoided, even though he took more steps than were necessary in compliance with the above rule.
(iii) The plaintiff may recover loss incurred in taking reasonable steps to mitigate his loss, even though he did not succeed.

The plaintiff must minimise the loss resulting from the breach by taking all reasonable steps available to him. If he fails to do so, then he cannot recover anything in respect of that extra loss. See:

Payzu v Saunders [1919] 2 KB 581.

However, the plaintiff is not expected to take risks in order to mitigate losses caused by the defendant's breach:

Pilkington v Wood [1953] Ch 770.

If the plaintiff obtains any benefits as a result of his mitigation, these must be taken into account. See:

British Westinghouse v Underground Electric Railway of London [1912] AC 673.

Note the case of *White & Carter v McGregor* [1962] AC 413; an exception to the general rule?

4. PURPOSE OF DAMAGES

Damages are meant to compensate the injured party for any consequences of the breach of contract. The underlying principle is to put the injured party financially as near as possible, into the position he would have been in had the promise been fulfilled.

In *Addis v Gramaphone Co Ltd* [1909] AC 488, Lord Atkinson said: "I have always understood that damages for breach of contract were in the nature of compensation, not punishment."

5. HEADS OF DAMAGE & CALCULATION

There are several ways in which the plaintiff can be compensated for his loss and the plaintiff is entitled to choose whichever form of compensation he feels is most appropriate to his case.

HEADS OF DAMAGE

(i) LOSS OF BARGAIN

Damages for loss of bargain are assessable to put the plaintiff, so far as money can do it, in the same situation as if the contract had been performed. For example, in a contract for the sale of goods which are defective, the plaintiff will (under this head) be entitled to damages reflecting the differences between the price paid under the contract and the actual value of the defective goods.

(ii) RELIANCE LOSS

Damages for reliance loss are designed to put the plaintiff in the position he would have been, if the contract had never been made, by compensating him for expenses he has incurred in his abortive performance. See:

McRae v Commonwealth Disposals (1950) 84 CLR 377
Anglia Television v Reed [1972] 1 QB 60.

(iii) RESTITUTION
Where a bargain is made and the price paid, but the defendant fails to deliver the goods, then the plaintiff is entitled to recover the price paid plus interest thereon.

NOTE: Incidental losses are those which the plaintiff incurs after the breach has come to his notice. They include the administrative costs of buying a substitute, or sending back defective goods, or hiring a replacement in the meantime. Consequential losses may be loss of profits, for example, reliance loss, or further harm such as personal injury or damage to property.

The plaintiff's choice of claim may be aided by the fact that more than one of the claims is available to him. In such cases, the plaintiff can combine the claims:

Millar's Machinery Co v David Way (1935) 40 Com Cas 240.

TIME FOR ASSESSMENT OF LOSS

The general rule is that damages are to be assessed at the time of the breach. However, the court can postpone the date for assessment of damages to a more appropriate time. See:

Johnson v Agnew [1980] 1 All ER 883.

CALCULATION OF DAMAGES FOR LOSS OF BARGAIN

Where the plaintiff claims for loss of bargain and that he be put in the position as if the contract had been performed, two bases of assessment are available: cost of cure and difference in value. See:

Peevyhouse v Garland Coal Co (1962) 382 P 2d 109.

In the majority of cases where there is a discretion, the court will exercise this to use the most appropriate basis of assessment in the case. However, certain rules do exist for working out the appropriate mode of assessment:

(i) In sale of goods contracts if a defect can be cured at a reasonable cost, the cost of cure will be awarded, otherwise the difference in value is awarded.
(ii) In building contracts, cost of cure basis is usual, and the builder must put the defects right. However, if the cost of cure is greater than the whole value of the building, then only the difference in value will be awarded. This issue was considered by the House of Lords in:

Ruxley Electronics & Construction v Forsyth [1995] 3 WLR 118.

ACTUAL AND MARKET VALUES

Where damages are based on the difference in value principle, then market values may be taken into account to assess the plaintiff's loss. For example, where the defendant fails to deliver goods or render services, then the plaintiff can go into the market and obtain these goods or services at the prevailing price. Therefore the plaintiff's damages will be the difference between the market price and the price of the goods or services in the contract. There are two rules:

(i) Under s51 SGA 1979, where a seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may maintain an action against the seller for damages for non-delivery. But such an action will not allow the seller to recover for anything more than the difference between the market value and the contract value.

(ii) If the defendant wrongfully refuses to accept and pay for the goods, then the plaintiff can sue for the loss of profit on that transaction in certain circumstances. Compare:

Thompson v Robinson (Gunmakers) Ltd [1955] Ch 177
Charter v Sullivan [1957] 2 QB 117.

DAMAGES WHICH ARE IRRECOVERABLE

The plaintiff may be able to recover damages for injury to feelings in tort, but in contract such damages are irrecoverable. See:

Addis v Gramaphone Company [1909] AC 488.

This principle was reaffirmed by the Court of Appeal in *Bliss v South East Thames Regional Health Authority* [1985] IRLR 308 (an unfair dismissal case).

OTHER TYPES OF DAMAGE

(i) Discomfort, vexation and disappointment
In *Jarvis v Swan Tours* [1973] 2 QB 233, the plaintiff solicitor, went on a Swan Tour and sued

for damages because the hotels and buses fell short of the standards promised. It was held that the plaintiff could recover damages for the disappointment and discomfort he had been caused as a result. See also *Jackson v Horizon Holidays*.

However, there is a limit to damages for distress for breach of contract. In *Bliss*, Dillon LJ stated that such damages should be confined to cases "where the contract which has been broken was itself a contract to provide peace of mind or freedom from distress". Recently, the Court of Appeal made it clear that they were not prepared to extend the circumstances in which damages for distress or disappointment might be granted:

Alexander v Rolls Royce Motor Cars [1995] TLR 254.

(ii) Inconvenience
In *Bailey v Bullock* [1950] 2 All ER 1167, a solicitor failed to take proceedings to recover his client's house for him and was held liable in damages for the inconvenience caused by reason of the client having to live with his wife's parents for two years.

(iii) Diminution of future prospects
In *Dunk v George Waller* [1970] 2 QB 163, an apprentice was wrongfully dismissed, but had he been allowed to complete his apprenticeship he would have got a certificate entitling him to certain jobs at certain wages. Without this certificate, his chances were lessened and he claimed damages for diminution of future prospects. He was held to be entitled to damages on this basis as the object of his apprenticeship was to enable him to get better employment.

(iv) Speculative damages
If the plaintiff's loss is the chance of doing something or benefiting from doing something, and this contingency is outside the control of the parties, then he is entitled to damages if the defendant's breach of contract denies him this chance. For example, in *Chaplin v Hicks* [1911] 2 KB 786, the plaintiff recovered damages for loss of the chance to take part in a beauty contest.

6. LIQUIDATED DAMAGES & PENALTY CLAUSES

The parties to the contract may make a genuine assessment of the losses which are likely to result in the event of a breach, and stipulate that such sum shall be payable in the event of a breach. Such clauses are known as liquidated damages clauses and will be effective in the event of a breach, and the plaintiff will not recover more than that sum. (No action for unliquidated damages will be allowed.)

If, however, the clause is not an assessment of losses, but is intended as punishment on the contract-breaker, then the clause is a penalty clause and is void. In an action for breach of contract it is disregarded.

The parties may often be in dispute over whether the clause was a penalty or a liquidated damages clause. Various rules have been formulated to deal with such contingencies. See:

Dunlop Pneumatic Tyre Co v New Garage [1915] AC 79.

Where the contract has underestimated damages in the event of a breach, either because of inflation or through bad bargaining, damages will be limited to the amount stipulated by the contract. See:

Cellulose Acetate v Widnes Foundries [1933] AC 20.

If the clause is in fact a penalty clause, then as it is void, the plaintiff can ignore it and sue for his actual loss:

Wall v Rederiaktiebolaget Luggude [1915] 3 KB 66.

1.28 REMEDIES FOR BREACH 2 - EQUITABLE REMEDIES

INTRODUCTION

Sometimes the remedy of damages will be inadequate compensation to the victim of a breach of contract. For example, the plaintiff may have contracted to purchase a particular plot of land from the defendant for which compensation cannot provide a satisfactory equivalent in the event of the defendant's breach. Equity therefore developed a number of remedies, discretionary in nature, directed towards ensuring that a plaintiff was not unjustly treated by his being confined to the common law remedy of damages. Two such remedies will now be considered: specific performance and injunctions.

SPECIFIC PERFORMANCE

An order for specific performance will compel the addressee to fulfil the terms of a contract. These terms must be positive in nature, whereas negative stipulations are normally enforced by an injunction.

Any case concerning specific performance inevitably requires a consideration of three issues:

(1) DAMAGES INADEQUATE

If the plaintiff can show that damages are inadequate, then the court may grant his claim for specific performance. Damages will be inadequate in the following circumstances:

(i) Where the plaintiff cannot get a satisfactory substitute:

Nutbrown v Thornton (1804) 10 Ves 159
Cohen v Roche [1927] 1 KB 169.

(ii) Where the award of damages would be unfair to the plaintiff:

Beswick v Beswick [1968] AC 58.

(iii)Where the quantum of damages is difficult to assess.

(iv) Under s52 SGA 1979, the seller refuses to deliver 'specific or ascertained' goods.

Remedies for breach of contract

Specific Performance

Nutbrown v Thornton (1804) 10 Ves 159

Specific performance was ordered of a contract to supply machinery which could not be readily obtained elsewhere.

Cohen v Roche [1927] 1 KB 169

The court refused specific performance to a buyer of a set of Hepplewhite chairs saying that they were 'ordinary articles of commerce and of no special value or interest'. Note: the buyer was contracting with a view to resale and for personal use.

Beswick v Beswick [1968] AC 58

A nephew promised his Uncle to pay an annuity to his Aunty in consideration of the Uncle transferring the goodwill of the business to the nephew. The Aunty was not a party to the contract. The court held that it could be specifically enforced by the Uncle's personal representative (the Aunty) against the nephew. Damages would have been purely nominal as the promisee or his estate had suffered no loss. The nephew would have been unjustly enriched by being allowed to retain the entire benefit of the uncle's performance without performing his own promise.

Walters v Morgan (1861)

The defendant agreed to grant the plaintiff a mining lease over land he had just bought. Specific performance was refused as the plaintiff had produced a draft lease and induced the defendant to sign the agreement in ignorance of the value of the property. The plaintiff had hurried the defendant into signing the lease before he knew the value of the property.

Lamare v Dixon (1873) LR 6 HL 414

The plaintiff induced the defendant to agree to take a lease of cellars by orally promising they would be made dry. The promise had no effect as a misrepresentation as it related to

the future. The court refused the plaintiff specific performance since he had made no attempt to perform his promise.

Patel v Ali [1984] 1 All ER 978

The vendor and her husband were co-owners of the house they contracted to sell in 1979. The husband's bankruptcy caused delay in completion. After the contract the vendor got bone cancer, had a leg amputated and later gave birth to her second and third children. The purchaser obtained specific performance, against which the vendor appealed on grounds of hardship. She spoke little English and relied on friends and relatives for help, hence it would be hardship to leave the house and move away. It was held that the court could in a proper case refuse specific performance on the grounds of hardship subsequent to the contract, even if not caused by the plaintiff and not related to the subject matter. On the facts, there would be hardship amounting to injustice, therefore damages were awarded.

(2) JUDICIAL DISCRETION

"Equity will only grant specific performance if, under all the circumstances, it is just and equitable to do so" (Stickney v Keeble [1915] AC 386). However, the exercise of this discretion is circumscribed by a number of well-known rules:

(i) There must be mutuality before specific performance is available. "The court does not grant specific performance unless it can give full relief to both parties" per Lord Cranworth LC in *Blackett v Bates* (1865) LR 1 Ch App 117.

(ii) Specific performance will not be ordered if it is impossible for the defendant to comply with the order, eg, in a contract for the sale of land not owned by the vendor as in *Watts v Spence* [1976] Ch 165.

(iii) Specific performance will be refused if the plaintiff has acted unfairly or dishonestly. The equitable principle is that the plaintiff must come to equity with clean hands. See:

Walters v Morgan (1861).

(iv) Specific performance will be refused if the plaintiff fails to perform a promise which induced the defendant to contract. See:

Lamare v Dixon (1873) LR 6 HL 414.

(v) Specific performance will be refused if it would cause severe hardship to the defendant. See:

Patel v Ali [1984] 1 All ER 978.

(3) TYPE OF CONTRACT

The final consideration is the type of contract as traditionally equity will not order specific performance of contracts involving personal service and building contracts (see below). Finally, if the contract is entire and cannot be severed, the court will not order specific performance of part of that contract, as in *Ryan v Mutual Tontine* (1893).

(i) The court will not order specific performance of personal service contracts. Also note that s16 of the Trade Union and Labour Relations Act 1974 states that no court shall compel an employee to do any work by ordering specific performance of a contract of employment, or by restraining the breach of such contract by injunction.

An employer cannot be forced to employ somebody against his wishes, and the general rule is that the court will not order re-engagement of an employee, but will instead award compensation. Note that an industrial tribunal can order reinstatement or re-engagement under the Employment Protection (Consolidation) Act 1978.

(ii) The court will not generally order specific performance of building contracts. The justification is that damages may be an adequate remedy as the plaintiff can engage another builder, the difficulty of continually supervising the building work and the building specifications are often too imprecise. However, for an exceptional case see:

Wolverhampton Corp v Emmons [1901] 1 KB 515.

The difficulty of a court's supervising continuous contractual duties may also prevent specific performance in a variety of other situations. For example, an agreement to provide a porter for a block of flats. Contrast the following cases:

Ryan v Mutual Tontine Assoc [1893] 1 Ch 116
Posner v Scott-Lewis [1987] 3 All ER 513.

The most recent case is the decision of the House of Lords in:

Co-Op Insurance v Argyll Stores [1997] 3 All ER 297.

INJUNCTION

A court may be able to restrain a party from committing a breach of contract by injunction. There are three types of injunction:

· Interlocutory injunctions are designed to regulate the position of the parties pending a hearing.

· A prohibitory injunction orders a defendant not to do something in breach of contract.
· A mandatory injunction requires a defendant to reverse the effects of an existing breach.

With prohibitive injunctions, a court, in the exercise of its discretion, will not be influenced by the fact that the defendant's compliance with the injunction would be unduly onerous or that the breach would cause the plaintiff little prejudice. However, with mandatory injunctions, a court will apply the 'balance of convenience' test, refusing relief if the hardship caused to the defendant by compliance with the order outweighs the consequential advantages to the plaintiff.

The general rule is that an injunction will not be granted if the effect is to directly or indirectly compel the defendant to do acts for which the plaintiff could not have specific performance. For example, to require performance of a contract for personal services. See:

Page One Records v Britton [1968] 1 WLR 157.

However, there are some important exceptions to this rule:

(i) A service contract may contain negative obligations which can be enforced by injunction without compelling positive performance of the whole contract. See:

Lumley v Wagner (1852)

(ii) A negative stipulation which is too wide can be severed and enforced in part. See:

Warner Bros v Nelson [1937] 1 KB 209.

DAMAGES IN LIEU OR IN ADDITION

Damages were originally only available at common law. However, s2 of the Chancery Amendment Act 1858 (Lord Cairns Act), gave the Court of Chancery a discretion to award damages in lieu of, or in addition to specific performance provided the contract is of a type that is specifically enforceable.

This power is now contained in s50 of the Supreme Court Act 1981. Where the Court of Appeal or High Court has jurisdiction to entertain an application for an injunction or specific performance, it may award damages in addition to, or in substitution for, an injunction or specific performance.

For an example of damages being awarded in addition to specific performance, see:

Grant v Dawkins [1973] 1 WLR 1406.

1.29 CASES ON EQUITABLE REMEDIES

SPECIFIC PERFORMANCE

Nutbrown v Thornton (1804) 10 Ves 159

Specific performance was ordered of a contract to supply machinery which could not be readily obtained elsewhere.

Cohen v Roche [1927] 1 KB 169

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friends and relatives for help, hence it would be hardship to leave the house and move away. It was held that the court could in a proper case refuse specific performance on the grounds of hardship subsequent to the contract, even if not caused by the plaintiff and not related to the subject matter. On the facts, there would be hardship amounting to injustice, therefore damages were awarded.

Wolverhampton Corp v Emmons [1901] 1 KB 515

The plaintiff acquired land for an improvement scheme and sold part of it to the defendant, who covenanted to demolish houses on it and build new ones. The demolition was carried out and plans for new houses approved. The defendant then refused to continue. It was held that specific performance would be ordered since the defendant's obligations were precisely defined by the plans, and damages would be inadequate because the defendant had possession of the site, and the plaintiff could not get the work done by employing another contractor.

Ryan v Mutual Tontine Assoc [1893] 1 Ch 116

A lease of a service flat provided that the lessors should provide a porter who was to be 'constantly in attendance'. It was held that this undertaking could not be specifically enforced. It would require 'that constant superintendence by the court which the court has always in such cases declined to give'.

Posner v Scott-Lewis [1987] 3 All ER 513

The court granted an application for specific performance of a lessor's covenant to employ a resident porter for certain duties. The court distinguished *Ryan v Mutual Tontine*, where supervision of the execution of the undertaking had been required. Here neither personal services, nor a continuous series of acts, were required, but merely the execution of an agreement containing provisions for such services.

Co-Op Insurance v Argyll Stores [1997] 3 All ER 297

The defendants leased a shopping unit for 35 years and covenanted to use it as a supermarket and keep it open during the usual hours of business. The defendant gave notice to the plaintiffs of their intention to close the supermarket, which had made a substantial loss the previous trading year.

The House of Lords held that a covenant in a lease of retail premises to keep open for trade during the usual hours of business was not, other than in exceptional circumstances, specifically enforceable, since it was the settled practice of the court not to make an order requiring a person to carry on a business. That practice was based on sound sense, as such an order required constant supervision, was only enforceable by the quasi-criminal procedure of punishment for contempt and might cause injustice by allowing the plaintiff to enrich himself at the defendant's expense if the defendant was forced to run a business at a loss.

INJUNCTION

Page One Records v Britton [1968] 1 WLR 157

The Troggs, a pop group, contracted to appoint the plaintiff as their sole agent and manager for five years, and agreed not to act themselves in such capacity and not to appoint any other person for that time. They fell out with the manager and wanted to replace him. The plaintiff sought an injunction. It was held that an injunction must be refused because to grant it would, in effect, compel The Troggs to continue to employ the plaintiff, and thus would amount to enforcing the performance of a contract for personal services.

Lumley v Wagner (1852)

The defendant contracted to sing for the plaintiff in his theatre for three months and, at the same time, not to sing elsewhere during this time without the plaintiff's consent. A third party, Gye, offered the defendant a larger sum to sing for him. The court stated that they had no power to make the defendant sing or encourage her to sing at the plaintiff's theatre. However, the court could persuade her to do so by preventing her singing elsewhere by imposing an injunction to that effect.

Warner Bros v Nelson [1937] 1 KB 209

The defendant, an actress, agreed (1) to act for the plaintiff and, at the same time, (2) not to act or sing for anybody else for two years without the plaintiff's written consent, and (3) no other employment could be taken up during this period without the plaintiff's consent. It was held that the defendant could be restrained by injunction from breaking the second undertaking. She would not be forced to act for the plaintiff because she could earn a living by doing other work.

DAMAGES IN LIEU OR IN ADDITION

Grant v Dawkins [1973] 1 WLR 1406

The vendor's title to land was subject to an encumbrance which amounted to a breach of contract. It was held that the plaintiff could get specific performance of what title the defendant had, plus damages based on the cost of discharging the encumbrance.

Topic 2 THE MALAYSIAN LEGAL SYSTEM

LEARNING OUTCOMES

By the end of this topic, you will be able to:

1. Describe and discuss the multidimensional nature of organizational change.
2. Analyze the change situations in terms of the different types of change experienced.
3. Critically evaluate the theoretical perspectives relating to the types of change.

2.1 Types of Legal System in the World

There are various definitions of the term “legal system”. A Legal System is the framework of rules and institutions within a nation regulating individual’s relations with one another and between them and the government. In this world, there are many types of legal systems, but the few major legal systems of the world today are civil law, common law, customary law, religious law, socialist and mixed law systems.

The origin of civil law is from the Roman law. The civil law is a set out of comprehensive system of rules which are applied and interpreted by judges. Besides that, civil law is older, more widely distributed and in many ways more influential than the common law.
Common law is a system of law that is derived from judges’ decisions, rather than statutes or constitutions. It is based on tradition, past practices and legal precedents set by courts through interpretation of statues, legal legislation, and past rulings. It is English origin and is found in United States and other countries with strong English influences.

Customary law is a traditional common rule or practice that has become an intrinsic part of the accepted and expected conduct in a community, profession, or trade and is treated as a legal requirement. Not many countries in the world today will operate under a legal system which could be wholly customary. However, customary law still plays a significant role, like in the matters of personal conduct, in many countries or political entities with mixed legal systems.

Islamic law is derived from the interpretation of the Koran. Its primary objective is social justice, but also includes property rights, economic decision making, and types of economic freedom. Islamic law is mostly found in Pakistan, Iran, and other Islamic states.
Socialist law is based on fundamental tenets of Marxist-socialist state and centre on concept of economic, political, and social policies of the state. It can be found in some independent states of the former Soviet Union, China, and other Marxist-socialist states.

A mixed legal system is a mixture of two or more legal system practised by some countries.

2.2 Malaysia’s Legal System

Different country practices different types of legal system. Some country practices one type of legal system while others practice the mixed legal system which means a combination of two or more legal systems. Malaysia for example, practices the mixed legal system which includes the Common Law, Islamic law, and Customary Law. Malaysia’s legal system comprises laws which have arisen from three significant periods in Malaysian history dating from the Malacca Sultanate to the spread of Islam to Southeast Asia and following the absorption into the indigenous culture of British colonial rule which introduced a constitutional government and the common law. Malaysia’s unique legal system is designed to balance the delicate racial and religious needs of its heterogeneous people. The Malaysian legal system law can be classified into two categories which is the “Written” and “Unwritten law”.

2.3 Unwritten Law

The "Unwritten law" does not mean that the law is literally unwritten. It refers to the laws which are not enacted by the Legislature, and which are not found in the Federal and State constitutions. This category of law comes from cases decided by the Courts and the local customs, which is otherwise known as "common law". The "unwritten law" mainly comprised of the English law, judicial decisions, and custom law.

2.3.1 English Law

The English Law can be divided into two which are the English Commercial Law and English Land Law. In section 5(1) of the Civil Law Act 1956 provides that the English Commercial Law is applicable in Peninsular Malaysia except Penang and Malacca as it stood on 7 April 1956 in the absence of local legislation. On the other hand, Section 5(2) of the same act, applies in Penang, Malacca, Sabah, and Sarawak as the law administered in these states will be the same as law administered in England, in the like case at corresponding period. As for the English Land Law, none of the English Land Law concerning the tenure, conveyance, assurance of or succession to any immovable property or any estate, right or interest therein applies in Malaysia. In Malaysia, National Land Code is the law that governs the land matters. There is no any allowance for English land law, except in so far, the National Land Code might expressly provide.

2.3.2 Judiciary Decision/ Malaysian Court

Approaching the judicial decision, judges do not decide arbitrarily. Instead, they are bound to follow certain accepted principles known as precedents. Precedents are defined as 'a judgement or decision of a court of law cited as an authority for the legal principle embodied in its decision". The system of binding judicial precedent is called *stare decisis.* It is created by the English judges and introduced into Malaysia upon colonization.

The Malaysian Court structure is greatly influenced by the English Court system and is divided into the Subordinate Courts and the Superior Courts. The lowest level of the Subordinate Courts is the Penghulu Courts, presided over by a headman appointed by the State government for the district. The equivalent in Sabah and Sarawak are the Native Courts relating to the native customs of the indigenous people in those two States. Above these Courts are the Magistrate's Courts which deals with minor criminal and civil cases. The Sessions Courts are the highest of the Subordinate Courts. The Superior Courts comprises of the High Court, the Court of Appeal, and the Federal Court (which is the highest court in the land).

2.3.3 Customary Law

Customs are another important source of unwritten law. Every race has its own customs. Hindu and Chinese customary law applied to the Hindus and Chinese respectively. Besides that, natives in Sabah and Sarawak have their own customary law which relates to the land and family matters. In Malaysia, there are two types of Adat which is the *Adat Perpateh* and *Adat Temenggung. Adat Perpateh* is practiced among the Malays in *Negeri Sembilan* and *Nanning* in Malacca. It uses the matrilineal system which belongs to mother's

lineage, meaning to say it involves the inheritance of property, names or titles from mother to daughters. It also concerns with matters such as land tenure, lineage, inheritance and election of members of *lembaga* and *Yang di-Pertuan Besa*r. As for *Adat Temenggung*, it is practiced in other states, and it uses the patrilineal system which belongs to father's lineage.

2.4 Written Law

On the other hand, "Written law" refers to the laws contained in the Federal and State Constitutions and in a code or a statute. The written laws are much influenced by English laws as the Malaysian legal system retains many characteristics of the English legal system. The "Written law" includes the Federal and State Constitution, Legislation and Subsidiary Legislation.

2.4.1 The Federal and State Constitution

Malaysia is a federation of 13 states with a Federal Constitution and 13 State Constitution. The Federation Constitution is the supreme law of the country. The Federal Constitution also provides for the "*Yang di-Pertuan Agong*" who owes his position to the Constitution and act accordance with it. The Constitution can only be changed by a two-thirds majority of the total number of members of the legislature. The Federal Constitution comprises many Articles concerning the religion of the federation and many other related subjects. Besides the Federal Constitution, there is a state constitution where each state has their own constitution regulating the government of that state.

2.4.2 Legislation

Legislations refers to the laws that are established by the Parliaments at federal level and by the State Legislative Assemblies at the state level.... The Parliament and State Legislatures are not supreme and so they have to enact laws subject to the provisions set out in the Federal and State Constitution. In the Federal Constitution, Article 74, it states that parliament may make law with referring to matters provided in the List I of the Ninth Schedule while the state legislatives may make law with referring to matter provided in List II. As for matters on List III which is the Concurrent list, are in the authority of both parliament and state legislatives. Matters that are not in the lists are within the authority of the States.

2.4.3 Subsidiary Legislations/ Executive

Subsidiary Legislations are made by the people or bodies who are authorized by the legislatures. The Interpretation Act 1967 defines subsidiary legislation as rules, regulations, by laws, order, notifications made under legislations. The Legislatures provide basic law, so subsidiary legislation is very important is insufficient to govern day-to-day matters. That is why the authority is delegated to delegate their legislative powers. In Article 150 of Federal Constitution, Parliament can pass the power to legislate any subsidiary legislation during emergency, even if there are any contradictions with the Federal Constitutions involved.

The people or bodies who are authorized by the legislatures are the *Yang di-Pertuan Agong who* is the nominal head of the executive, and the Prime Minister and cabinet is the real executive. The Cabinet is answerable to the *Yang di-Pertuan Agong* as the nominal head of the executive in the country. However, according to the democratic ruling system, the Chief Executive is the Prime Minister. This does not mean that the *Yang di-Pertuan Agong* is unable to voice any opinion, but rather that he must act on government advice, whatever his personal view might be. The *Yang di-Pertuan Agong* appoints a Cabinet to advise him on country's matter. The Cabinet consists of the Prime Minister and several Ministers who must all be members of Parliament. Besides that, the Government has set up various agencies to ensure the smooth enforcement of the law. It comprised of three main components, namely ministries, departments, and statutory bodies.

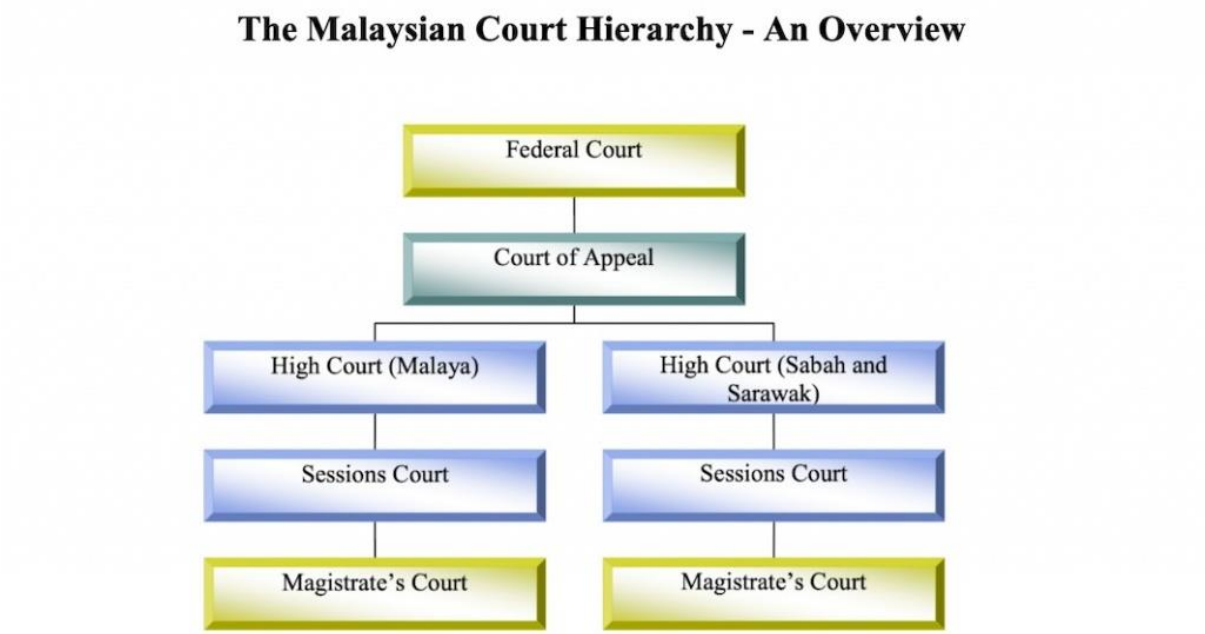
2.5 Islamic Law

Finally, Islamic law is also a major source of Malaysian law which is enacted under the Federal Constitution. It is only applicable to Muslims and is administered by a separate court system, the *Syariah* Courts. The State legislature has authority over the constitution, organization and procedure of the Syariah Courts and is also allowed to make Islamic laws pertaining to persons professing the religion of Islam.

2.6 The Malaysian Court Hierarchy – An Overview

The courts in Malaysia are divided into the subordinate courts (governed by the Subordinate Courts Act 1948) and the superior courts (governed by the Courts of Judicature Act 1964). The subordinate courts consist of the Sessions Courts and the Magistrates courts. Not depicted in the chart above is the Court for Children, which has the same jurisdiction with the Magistrate's Court.

On the other hand, the superior courts are the High Court, the Court of Appeal, and the Federal Court. Outside the court hierarchy are the Syariah Courts, Native Courts, and Special Court which will not be discussed in this article. It should be noted that there is no jury system in Malaysia for criminal matters as it was effectively abolished on 1st January 1995.



Source: Malaysian Legal System, Sharifah Suhana Ahmad, 1999

Magistrates Court

Civil matters

A court's original jurisdiction in the Magistrates is governed by monetary limits.

As per changes in Subordinate Courts (Amendment) Act 2010, a First Class Magistrate shall have jurisdiction to try all actions and suits of a civil nature where the amount in dispute or value of the subject matter does not exceed RM100,000.00. The monetary jurisdiction of a Second Class Magistrate is now RM10,000.00.

Additionally, the Magistrates also have the power to deal with small claims procedures where the value in dispute/subject matter does not exceed RM 5,000. An important difference of a small claims procedure is that parties cannot be represented by a lawyer unless legally required to by virtue of Order 93, rule 7 of the Rules of Court 2012.

Subject to limitations contained in the Subordinate Courts Act 1948 ("SCA"), a First Class Magistrate has jurisdiction to try all offences for which the maximum term of imprisonment provided by law does not exceed ten years imprisonment or which are punishable with fine only and offences under sections 392 and 457 of the Penal Code. This is pursuant to Section 85 of SCA.

In regards to sentencing, a First Class Magistrate may pass any sentence allowed by law not exceeding, five years' imprisonment, a fine of RM 10 000, whipping up to twelve strokes or any sentence combining any of the sentences mentioned. This is pursuant to Section 87 of SCA.

For Second Class Magistrates, under Section 88 of SCA, a Second Class Magistrate shall only have jurisdiction to try offences for which the maximum term of imprisonment provided by law does not exceed twelve months' imprisonment of either description or which are punishable with fine only. Provided that a Second Class Magistrate is of the opinion that if a conviction should result, the powers of punishment which he possesses would be inadequate, he shall take the necessary steps to adjourn the case for trial by a First Class Magistrate.

In regards to sentencing, a Second Class Magistrate may pass any sentence allowed by law not exceeding six months' imprisonment, a fine of not more than RM 1000, or any sentence combining either of the sentences mentioned.

Sessions Court

Civil matters

As per changes in Subordinate Courts (Amendment) Act 2010 , the monetary jurisdiction of the Sessions Court is now RM1,000,000. They also have unlimited jurisdiction to try all actions and suits of a civil nature in respect of motor vehicle accidents, landlord and tenant and distress actions. Furthermore, by virtue of Section 65(3) SCA, the parties to a legal action may enter into an agreement in writing to grant jurisdiction to the Sessions Court to try an action beyond the prescribed monetary jurisdiction.

Criminal matters

Under Sections 63 and 64 SCA, a Sessions Court shall have jurisdiction to try all offences other than offences punishable with death and may pass any sentence allowed by law other than the sentence of death.

High Court

Civil matters

Generally, the High Court has unlimited jurisdiction and there is no limit on the value of claims they can decide on. All proceedings at a High Court are generally heard and disposed of before a single judge. Under the Courts of Judicature Act 1964 (CJA), it has original and appellate jurisdiction. For example, if your claim exceeds both the Magistrates and Sessions Court jurisdiction, you can start your case in the High Court. This also means you have the right to appeal to the High Court if you started your case in the Magistrates or Sessions Court (subject to conditions). However, no appeal shall lie to the High Court from a decision of a subordinate court in any civil cause or matter where the amount in dispute or the value of the subject-matter is RM 10 000 or less except on a question of law.

The High Court also has general supervisory and revisionary jurisdiction over all subordinate courts. Over the years, specialised courts within the High Courts have been established such as the Construction Court, Intellectual Property Court, and the Admiralty Court the Admiralty Court.

Criminal matters

Under Section 22 of the CJA, the High Court has jurisdiction to try all offences. This includes offences that carry the death penalty which exceeds the jurisdiction of the Magistrates and Sessions Courts. Appeals from subordinate courts may also be heard here.

Court of Appeal

As per the CJA, every proceeding in the Court of Appeal shall be heard and disposed of by three Judges or such greater uneven number of Judges as the President may in any particular case determine. Proceedings shall be decided in accordance with the opinion of the majority of the Judges composing the Court. Wherever application may be made either to the High Court or to the Court of Appeal, it shall be made in the first instance to the High Court.

Civil matters

The Court of Appeal has jurisdiction to hear and determine appeals from any judgment or order of any High Court in any civil cause or matter, whether made in the exercise of its original or of its appellate jurisdiction, subject to written laws regulating the terms and conditions the appeals shall be brought. However, no appeal shall be brought to the Court of Appeal in cases

where the amount or value of the subject-matter of the claim (exclusive of interest) is less than RM250 000 except with the Court's leave.

Criminal matters

The Court of Appeal has jurisdiction to hear and determine any appeal against any decision made by the High Court.

Federal Court

Similarly ,to the Court of Appeal, the Federal Court is an appellate court. It is the highest court in Malaysia, hence the final court of appeal for both civil and criminal cases. Under the CJA, every proceeding in the Federal Court is heard and disposed of by three Judges or such greater uneven number of Judges as the Chief Justice may in any particular case determine. Proceedings shall be decided in accordance with the opinion of the majority of the Judges composing the Court. Whenever an application may be made either to the Court of Appeal or to the Federal Court, it shall be made in the first instance to the Court of Appeal. Additionally, it also has original jurisdiction under Article 128(1) and (2) of the Constitution to determine any matters concerning constitutional law. Thus, it has advisory jurisdiction in providing Yang di-Pertuan Agong to give its opinion as to the effect of any provisions in the Federal Constitution which is to be pronounced in open court.

2.7 Cause of Action

To sue, or not to sue. That is a question that ponders the mind of the practising lawyer day by day. But the truth really is, that few things delight lawyers more than having the opportunity to sue. Litigating, besides being part of the lawyer's source of bread and butter, also gives the opportunity for the lawyer to honour his literacy and oratory skills, and nothing gives a better high then a successful day in court. But before one can even sue, one needs to bear in mind the procedures involved. And none of a procedure is more important than having a valid cause of action.

A cause of action has been defined in various cases from being "every fact which is material to be proved to entitle the plaintiff to succeed" in *Cooke v Gill* (1873) LR 8 CP 107 to "every fact which it would be necessary to support his right to the judgment of the court" in the case of *Read v Brown* (1888) 22 QBD 128.

Some instances of questionable causes of action might make the subject matter clearer in the following cases. In *Taib bin Awang b Mohamad bin Abdullah* [1983] 2 MLJ for example, the plaintiff was convicted in the Kadi's court and he appealed. But before his appeal could be heard he commenced an action for malicious prosecution and it was so held that since the appeal has yet to be heard, and the issue had yet to be disposed of, how could malicious prosecution be established? The cause of action was therefore premature. In the case of *Sio Koon Lin v SB Mehra* [1981] 1 MLJ 225 the plaintiff commenced an action for recovery of arrears that where in fact not yet due at the time of the claim. Needless to say the claim was thrown out. A similar situation occurred in *Simetech (M) Sdn Bhd v Yeoh Cheng Liam Construction Sdn Bhd* [1992] 1 MLJ 11.

A valid cause of action also depends on other factors, such as whether the claim would be made within the proscribed time. Malaysia's general statute of limitations is the Limitation

Act 1953. Section 6(1) of the Act says that action for breach of contract or a tort are six years from the date on which they accrue.
The case of *Sivapira v Lim Yoke Kong* [1992] 2 MLJ 381 illustrates the principle that a limitation period may not be used to aid fraud, or the enforcement of the equitable maxim that equity will not allow a statute to be used as an instrument of fraud. In this case the plaintiff was knocked down by the defendant on a motorcycle on the 1st day of April 1977, and then the plaintiff's solicitors sought to identify the defendant's insurers but to no avail until the 28th day of March 1984, that is, when the six year limitation period had passed. The defendant predictably alleged that the claim was time barred. The High Court held that the defendants had wilfully concealed themselves from the knowledge of the plaintiff and thus the case came under fraud as defined in section 29 of the Act. The plaintiff's claim therefore, was not time barred after all. It must be noted at this point that failure to add a party to the action does not come within Section 29 of the Act as illustrated in the English case of *RB Policies v Butler* (1950) 1 KB 76 where the thief of a car stolen in 1940 was only identified that year and so the claim was time barred.

There are limitation periods proscribed by other Acts of Parliament as well. Section 7(5) of the Civil Law Act 1956 for example states that in a dependency claim where the negligent act had caused the death of a person, the period of limitation shall be three years (a bit harsh and unfair, isn't it?) and section 2 of the Public Authorities Protection Act 1948 provides that where public authorities act in the pursuance of any public duty, the period of limitation where any action accrues shall be limited to 36 months. In the case of *Lee Hock Ning v Government of Malaysia* [1972] 2 MLJ 12 the non-payment of monies due under a series of building contracts entered between the appellant and the Government of Malaysia was not in pursuance of any public duty and therefore the relevant provision of the Act did not apply. In the Railways Act 1991 (which has ceased to apply to Peninsular Malaysia following the passage of the Land Public Transport Act 2010) it is proscribed that any suit involving the railway authorities shall be limited to three years.
Lastly, one must consider whether one has an interest in the subject matter one sues in. The judge in the case of G*overnment of Malaysia v Lim Kit Siang* [1988] 1 CLJ 219 said that every legal system has a built-in mechanism to protect its judicial process from abuse by busy bodies, cranks and other mischief makers by insisting that a plaintiff should have a special interest in the proceedings he institutes. This takes the form of a nexus between himself and the other party and is known as a *locus standi.* This is demonstrated clearly in the case of *Atip Bin Ali v Josephine Doris Nunis* [1987] 1 MLJ 82 where one woman filed a suit against a former chief minister of a certain state in Malaysia for breach of promise to marry and later discontinued the suit. The members of the political party of that former chief oddly believed that she was insulting their honour and sued for defamation. Luckily defamation was held to be personal to the ex-minister involved, and not to the members.

Cause of Action means the cause or the set of circumstances which leads up to an action in court. Cause of action also refers to every fact, which is necessary to the plaintiff to prove in order to entitle him to an order or judgment in an action. It is in other words a bundle of essential facts, which was necessary for the plaintiff to prove before he can succeed in an action.
The cause of action is a condition precedent to the commencement of an action and every

claim must disclose a cause of action before the court will be able to proceed to adjudicate the dispute. If there is no cause of action, the court cannot provide any remedy. In the case of **Government of Malaysia v Lim Kit Siang**, Lord President, Tun Salleh Abas observed that " cause of action is a statement of facts alleging that a plaintiff's right, either by law or by statue, has, in some way or another, been adversely affected or prejudiced by the act of defendant in an action".

In **Letang v Cooper**, the judge defined 'a cause of action' mean a factual situation, the existence of which entitles one person to obtain from the court a remedy against another person. Meanwhile, in **Hock Hua Bank Bhd v Leong Yew Chin**, Syed Agil Barakbah SCJ, observed that " a cause of action is simply a factual situation the existence of which entitle plaintiff to obtain from the court a remedy against the defendant". A cause of action founded on contract accrues on its breach. In the case **Board of Trade v Cayzer, Irvine & Co.**, the judge describes the cause of action as that which makes action possible. What makes possible an action founded on a contract is its breach. In other words, a cause of action founded on a contract accrues on its breach. In the case of actions founded on contract, therefore, time runs from breach. In the case of actions founded on any other right, time runs from the date on which right is infringed or there is a threat of infringement.

2.8 The Limitation Period in Malaysia

If you ever need to sue someone, there's one important factor most people would probably would never think of: there's a time limit to sue. Certain lawsuits have an "expiration date" for you to take action, whereby you may no longer be able to sue the person if the time limit has passed. While this may sound unfair, especially if you suffered a heavy loss, there's a reason for this limit. As expressed in the case of *Credit Corporation (M) Sdn Bhd v Fong Tak Sin*:

"The limitation law is promulgated for the primary object of discouraging plaintiffs from sleeping on their actions and more importantly, to have a definite end to litigation." - Hashim Yeop Sani, then Chief Justice Malaya

So in a way, the time limit is another way to be fair to both parties. Imagine if you're suddenly sued out of the blue for an incident 10 years ago that you didn't even realize happened… Not very fair, right?

So why is suing on time important?

Limitation periods only apply to civil suits (between two people) and not criminal cases (government coming after someone). In civil cases, if you exceed the "expiration date" to bring a case, courts are generally reluctant to hear it. But this doesn't mean that you don't have the right to bring an action anymore, it means you can't get the remedy. A remedy is what you want to get at the end of the lawsuit - what are you suing the other party for, such as the enforcement of a contract, monetary compensation, etc.

Let's take two guys - Chan and Dan.

Say Chan got into a car accident with Dan on January 1st 2000 and Dan is at fault. Chan has a right to compensation from Dan for the damage to Chan's car, but Chan doesn't sue Dan for it until January 2007.

Here, the time limitation will take effect. So while technically Chan is entitled to sue Dan, the compensation is no longer valid… Which is why you'd want to sue in the first place… Which makes suing pointless.

 *Right?*

Judges have to deal with a lot of cases, and it wouldn't be strange to have a time-limited case thrown out. Because why sue if there's no point to it? Hence it's important that you sue within the time limit, which brings us to…

How do you determine when is the last day you can sue someone?

There are a few factors that will be taken into consideration, but mainly it will depend on your cause of action and *who you are suing*. If you are suing an individual or a company, the time limit depends on what type of dispute it is, but if you're going after the government, the time limit is different as we'll discuss later below. Here are a few common types of civil cases that get brought to court:

Contract - 6 Years

If you have a contract with someone and they breached it, under Section 6(1)(a) Limitation Act 1953, you have 6 years from the date the contract was breached to sue:

...actions shall not be brought after the expiration of six years from the date on which the cause of action accrued, that is to say actions founded on a contract or on tort...

Here's an example:

On January 1st 2017, Ali entered into a contract where Muthu will deliver him a bouquet of flowers every day till December 31st 2017. Unfortunately, Muthu failed to deliver a bouquet on February 14th 2017.

If Ali decides to sue Muthu, the time period he can do so is from February 15th 2017 to February 14th 2023.

On the other hand, for rental agreements, if your tenant doesn't pay the rent, Section 20 Limitation Act 1963 specifically bars recovery of arrears (outstanding payment) of rental 6 years after the due date. Section 20 states that:

"No action shall be brought, or distress made, to recover arrears of rent, or damages in respect thereof, after the expiration of six years from the date on which the arrears became due."

Don't wait around to sue this kind of tenant! Image from TheLandlordDoctor.

Tort - 6 years

In law, if a person wrongfully harms you, it will fall within this category of law called tort. It governs claims by victims seeking compensation against the person that caused them to suffer. This would include claims involving an accident, medical negligence, or even assault. Section 6(1)(a) Limitation Act 1963 specifies that you will only have 6 years from when the damage occurred to sue. It doesn't matter if you don't initially see the damage or if you're unsure of the identity of your attacker - the timer starts from the date you were harmed.

Land disputes - 12 years

Section 9(1) Limitation Act 1953 governs the action to recover land and, unlike the areas mentioned above, it has a slightly longer time limit of 12 years. The Act provides that:

No action shall be brought by any person to recover any land after the expiration of twelve years from the date on which the right of action accrued to him, or if it first accrued to some person through whom he claims, to that person.

Here's an example scenario of recovery of land:

Raju paid the purchase price to Ah Chong for a piece of land but, a year later, Ah Chong still refuses to transfer the property to Raju. Raju will have 12 years to sue Ah Chong in court and force Ah Chong to take the steps necessary to transfer the property to Raju.

What if you are suing a government agency or a public servant?

According to the Public Authorities Protection Act, you only have 3 years to sue starting from when you were harmed. However, this only comes into play when it involves a public authority carrying out his or her duty; like if a policeman in a patrol car hits you. But, if the same policeman got sued for late rental payment (which is unrelated to his job), this special rule will not apply.

Section 2 Public Authorities Protection Act 1948:

... any suit, action, prosecution or other proceeding ... shall not lie or be instituted unless it is commenced within thirty-six months next after the act, neglect or default complained of or, in

the case of a continuance of injury or damage, within thirty-six months next after the ceasing thereof...

It is important to note that while there is this limit of 3 years for private citizens, the government is not bound by this. The normal limitation periods apply if the government wants to sue you. So if a police car crashed into your car, you have 3 years to sue for damages. But if you crashed into a police car, the police have 6 years to sue you for damages.

Can you sue a person who's already dead?

This might be surprising to some, but the answer is actually.... Yes.

Yes, even death is not considered a time limit. The details get a little tricky, but it doesn't mean you can't sue a person who's no longer alive. In these cases, the deceased person will be represented by a personal representative such as an executor of his/her estate or an administrator (one of the people in charge of distributing the inheritance). The time limits in the Limitation Act don't change, with the exception of torts, where section 8 of the Civil Law Act may apply:

Section 8(3) Civil Law Act 1956:

No proceedings shall be maintainable in respect of a cause of action in tort which by virtue of this section has survived against the estate of a deceased person, unless proceedings against him in respect of that cause of action either—

(a) were pending at the date of his death; or

(b) are taken not later than six months after his personal representative took out representation.

Basically, what the section in (b) says is that If you're in the process of suing someone over tort law and the person dies, you only have 6 months to sue from when a grant of representation has been issued. A grant of representation is a court order that gives the administrator or executor the power to manage the deceased's estate. Here's an example:

You want to sue Ahmad but he is dead. You find out that Ahmad's wife took out a grant of representation from court to be in charge of Ahmad's estate on January 1st 2017.

This means you have 6 months from January 1st 2017 to sue Ahmad (or rather, his estate).

What happens to a lawsuit if the person you are suing died midway through the action?

Well, if the person dies while the suit is still ongoing, the trial will continue unless it's a suit involving defamation or seduction under Section 8(1) of the Civil Law Act. In these cases, the case will thrown out of court since the person involved is already dead.

If you think you have a case, you might want to act fast!
While there are exceptions and ways to extend the time period, you shouldn't use it as a reason to procrastinate. If you feel that you have a cause of action against someone, it's best to seek out a lawyer for consultation and advice on how to further proceed with your claim.

Too Little, Too Late?

Ooi Chih-wen *discusses the proposed new section 6A of the Limitation Act 1953.*

On 4 April 2018, the Limitation (Amendment) Act 2018 ("Act") was passed by the Malaysian Parliament. The Act was subsequently granted Royal Assent by the Yang di-Pertuan Agong and gazetted on 27 April 2018 and 4 May 2018 respectively, and will come into force on a date to be appointed by the Minister.

The objectives of the act are :

1. postpone the commencement of the limitation period when a person is under a disability at the time the cause of action accrued; and
2. extend the limitation period in cases of negligence not involving personal injury and the damage was not discoverable prior to the expiry of the statutory limitation period.

This article focuses on section 6A of the Act which addresses the latter.

As Sarawak and Sabah have their own legislation on limitation, the legislatures of those States will have to consider whether there is a need to amend their laws to be consistence with section 6A.

2.9 THE LIMITATIONS OF THE LIMITATION ACT 1953

Section 6(1)(a) of the Limitation Act 1953 ("Limitation Act") provides that any action must be brought within six years from when a cause of action accrued. In tortious claims, the limitation period starts when a plaintiff suffers damage. The 6-year limitation period applies regardless of when the plaintiff discovers such damage. This position has been affirmed by the Court of Appeal in *AmBank (M) Bhd v Abdul Aziz Hassan & Ors* [2010] 3 MLJ 784. When presented with the argument of postponing or extending the statutory limitation period for negligence claims based on the discovery of the damage, the Court of Appeal held that section 6(1)(a) of the Limitation Act should be interpreted in a literal manner. Further, the Court of Appeal ruled that the notion of postponing or extending limitation to include the element of discovery is not provided for in the Limitation Act or and other Malaysian laws. The approach in *Abdul Aziz* may seem unfair, particularly in cases of latent defects. In relation to construction works, latent defects are defects that are not immediately apparent

upon inspection; sometimes such defects are only discovered after six years. This is amply illustrated in the English case of *Pirelli General Cable Works Ltd v Oscar Faber & Partners (A Firm) [1983] 2 AC 1, wherein the defendant engineers designed a chimney for the plaintiff's factory, the construction of which was completed in July 1969. Although cracks started appearing on the top of the chimney by April 1970, the plaintiff only became aware of the defect in November 1977 which was at that point two years after the 6-year limitation period. The House of Lords dismissed the plaintiff's claim for damages, holding that the claim was time barred. The injustice caused in Pirelli led to the passing of the Latent Damage Act 1986 in the United Kingdom, a statute recognising latent defects and allowing for the extension of the limitation period in such cases.*The Malaysian Courts have since come to acknowledge the deficiency of *Abdul Aziz*. Harmindar Singh Dhaliwal J (as he then was) commented in *Sharikat Ying Mui Sdn Bhd v Hoh Kiang Po* [2015] MLJU 621, that:

"Despite the evident injustice that would arise in cases of latent damage, our law in the form of s. 29 of the Limitation Act 1953, only recognizes postponement of the limitation period in cases of fraud, concealment or mistake. There are of course other provisions but none of which concern situations where a plaintiff may not have known or with reasonable diligence had discovered that he has a cause of action. This deficiency is in my view a matter for Parliament and the time is perhaps overdue for a review of the limitation laws in keeping with the developments in other common law jurisdictions."

SAVED BY THE ACT

Perhaps it is long overdue, but the Act arguably redresses the perceived injustice of *Abdul Aziz* by the introduction of section 6A.

It must first be noted that the 6-year limitation period remains the starting point. Section 6A only applies to actions brought **after** the expiration of the said six years, and where the claim is for damages for negligence not involving personal injury. Further, such action must be brought within three years from the "*starting date*" and is subject to a longstop of 15 years. In this respect, the Act is similar to the corresponding legislation in the United Kingdom and Singapore.

The expression "*starting date*", as defined in section 6A(4)(a), means "*the earliest date on which the plaintiff or any person in whom the cause of action was vested before him first had both the knowledge required … and a right to bring such action*."

Accordingly, the commencement of the limitation period hinges on when a person first had knowledge. Section 6A(4)(b) provides that a person is deemed to have the requisite knowledge when he knows of:

1. the material facts about the damage for which damages are claimed; and
2. other facts relevant to the action, including: (i) that the damage is attributable in whole or in part to the alleged negligence; (ii) the identity of the defendant; and (iii) where it is alleged that the act or omission was by a third party, the identity of the third party and the additional facts supporting the action against the defendant.

A plaintiff is deemed to have knowledge of facts which he, or any person in whom the cause of action was vested before him, might be reasonably expected to have acquired from facts observable or ascertainable by him, or with the help of appropriate expert advice which is reasonable for him to seek.

MORE OR LESS THAN IT SEEMS?

Read on its own, section 6A of the Act appears to be wide enough to cover all instances of negligence. However, is that necessarily the case?

The explanatory statement in the Bill initially states that the provision is intended "*to enable a person to take action founded in negligence not involving personal injuries by allowing an extended limitation period of three years from the date of knowledge of the person having the cause of action.*" However, it then goes on to explain that the provision "*considers negligence cases involving latent damage in construction cases, where the damage was not discoverable through general inspection* ..." **(***emphasisadded***)**.

It appears from the above that Parliament intends for section 6A to apply only to latent damage in construction cases. There are two factors in support of this contention. Firstly, according to the Minister's statement in the Hansard of 4 April 2018, section 6A "*would permit a plaintiff to take action based on negligence involving latent damage in construction cases by extending the limitation period by three years …*" Secondly, all four illustrations provided in section 6A to describe the operation of certain sub-sections are premised on construction cases.

However, the English courts have not restricted the application of section 14A of the UK's Limitation Act 1980 (the equivalent of section 6A) to construction cases. In *Haward and others v Fawcetts (a firm)* [2006] 3 All ER 497, the House of Lords applied section 14A to a claim against an accounting firm for negligent investment advice but found that the plaintiff had discovered the damage before the statutory limitation period expired.

Similarly, in *Blakemores LDP (in administration) v Scott and others* [2015] EWCA Civ 999, the English Court of Appeal applied section 14A in a professional negligence claim against solicitors.

It remains to be seen whether the Malaysian courts will apply section 6A to negligence cases that do not involve latent defects in construction cases.

Prior to the introduction of the Act, the Court of Appeal in *AmBank (M) Bhd v Kamariyah bt Hamdan & Anor* [2013] 5 MLJ 448 attempted to remedy the injustice caused by the strict interpretation of section 6(1)(a) of the Limitation Act in *Abdul Aziz* by introducing the "*discoverability rule*". Jeffrey Tan JCA (as he then was) considered the Canadian case of *Central Trust Co v Rafuse* [1986] 2SCR147andobserved:

"… the Supreme Court of Canada pronounced 'that the judgment of the majority in Kamloops

laid down a general rule that a cause of action arises for purposes of a limitation period when the material facts on which it is based have been discovered or ought to have been discovered by the plaintiff by the exercise of reasonable diligence … There is no principled reason, in my opinion, for distinguishing in this regard between an action for injury to property and an action for the recovery of purely financial loss caused by professional negligence …' … Likewise, in the instant case, the appellant … could not have discovered whatever negligence on the part of the respondent by the exercise of any reasonable diligence ..."

His Lordship ruled that limitation should run from the date damage was discovered or ought to have been discovered. When invited to consider *Abdul Aziz*, the learned judge held, "… *we must respectfully decline to defer to the ruling that time would run regardless of whether damage was or could be discovered."*

An example of the "*discoverability rule*" being considered in a case involving latent defects would be *The Ara Joint Management Body v Mammoth Land & Development Sdn Bhd* [2017] MLJU 631. The case involved latent defects discovered in the buildings and compound of The Ara Bangsar development. Construction was completed in 2007 but the alleged defects were only discovered sometime in 2014. The plaintiff, the joint management body of the development, brought an action on behalf of the residents against the developer for latent defects in October 2016, some 9 years after the construction had been completed. The developer, relying on *Abdul Aziz*, applied to strike out the case on grounds that the claim was time-barred. The plaintiff, on the other hand, argued that the "*discoverability rule*" should be adopted. Lee Swee Seng J, in dismissing the developer's striking-out application, opined that the issue as to whether the developer would be estopped from raising the defence of limitation would be fact-centric and was a matter to be determined at trial.

The principle enunciated in *Kamariyah* has been applied in several other cases, which include negligence against a financial institution and its officer (*CIMB Bank Bhd v Lee Kim Kee & Ors and another appeal* [2018] 3 MLJ 72 (CA)), negligence of a solicitors' firm (*Export-Import Bank of Malaysia Bhd v Hisham Sobri & Kadir* [2018] 6 CLJ 82 (HC) where the court applied the tests in both *Abdul Aziz* and *Kamariyah*), negligence of a civil and structural engineer (*CB Land Sdn Bhd v Perunding Hashim & Neh Sdn Bhd* [2016] 6 MLJ 320 (CA)) and the tort of conversion (*Peninsular Concord Sdn Bhd v Syarikat Bekalan Air Selangor* [2015]3CLJ682(HC)).

CONCLUSION

Given the introduction of section 6A, one must question whether *Kamariyah* and its wide-ranging effect should remain good law or should be overruled.

It should be noted that *Central Trust Co v Rafuse* is no longer good authority in Canada. The case was decided by the Supreme Court of Canada in 1986 and remained good law in the province of Nova Scotia until 2014 when the Limitation of Actions Act of Nova Scotia was passed. Section 8 of the said Act provides that any action, negligence or otherwise may not be brought two years after the date the action was discovered and fifteen years from the date the act or omission on which the action is based on occurred.

Upon section 6A coming into effect, there will be three tests to determine limitation for negligence not amounting to personal injury, namely *Abdul Aziz*, *Kamariyah* and section 6A. Will the new statutory provision override both *Abdul Aziz* and *Kamariyah* and apply to all claims for damages for negligence not involving personal injury, or will it only apply to construction cases involving latent damage and thereby subsist alongside section 6(1)(a) of the Act? If it is the latter, it remains to be seen whether *Abdul Aziz* or *Kamariyah* will ultimately prevail in the interpretation of section 6(1)(a).

If you ever need to sue someone, there's one important factor most people would probably would never think of: there's a time limit to sue. Certain lawsuits have an "expiration date" for you to take action, whereby you may no longer be able to sue the person if the time limit has passed. While this may sound unfair, especially if you suffered a heavy loss, there's a reason for this limit. As expressed in the case of *Credit Corporation (M) Sdn Bhd v Fong Tak Sin*:
"The limitation law is promulgated for the primary object of discouraging plaintiffs from sleeping on their actions and more importantly, to have a definite end to litigation." - Hashim Yeop Sani, then Chief Justice Malaya
So in a way, the time limit is another way to be fair to both parties. Imagine if you're suddenly sued out of the blue for an incident 10 years ago that you didn't even realize happened… Not very fair, right?

Topic 3 ▸ Employment Law

By the end of this topic, you will be able to:

4. Describe and discuss the multidimensional nature of organizational change.
5. Analyze the change situations in terms of the different types of change experienced.
6. Critically evaluate the theoretical perspectives relating to the types of change.

3.0 INTRODUCTION

This article is dedicated to all the employers, employees or the soon-to-be employers or employees in Malaysia.

The employment law in the private sector in Malaysia is mainly provided in the *Employment Act 1955* ("**the EA**"), among others sources of law, which shall be applicable in the Peninsular Malaysia and the Federal Territory of Labuan.

In light of the impending extensive amendments to the EA which is now at its final stages of public engagement before tabling in the Parliament, this article serves to provide a basic understanding of the current state of the law before the amendments set in.The proposed amendments to the Employment Act 1955 can be seen in the Ministry of Human Resource web link as follows:-

Table of Proposed Amendments to the Employment Act 1955

There is, however, a different set of employment law in the public sector which governs the civil servant under the purview of the Public Service Commission.

3.1 SOURCES OF LAW

For clarity, the sources of employment law in Malaysia are basically found in:-

(a) *the statutes, being the Parliament made law or an Act of Parliament*

For examples:

- Industrial Relation Act 1967;
- Holidays Act 1951;
- Weekly Holidays Act 1950;
- Income Tax Act 1967 (Schedular Tax Deduction);
- Children and Young Person (Employment) Act 1966;
- Employees Provident Fund Act 1991;
- Employees Social Security Act 1969;
- Minimum Retirement Age Act 2012;
- National Wages Consultative Council Act 2011;
- Employment Insurance System Act 2017); and

(b) *subsidiary legislation, being the ministerial orders or regulations made under the relevant empowering statutes*

For examples:

-
  - Employment (Part-time Employees) Regulations 2010; and
  - Minimum Wages Order 2016); and

(c) *case laws refer to such judicial precedents found in the law reports for future similar cases to be treated alike.*

3.2 APPLICABILITY OF THE EA

It is important to note that the EA only covers the following categories of employees as stated in the First Schedule of the EA.

Further clarifications on this can be found in Categories of Employee covered under the Employment Act 1955:-

(a) *any person, irrespective of his occupation, who has entered a contract of service with an employer under which such person's wages do not exceed RM2,000 a month; and*
(b) *any person whose wages exceed RM2,000 a month has entered into a contract of service with an employer in pursuance of which:-*

(i) is engaged in manual labour;
(ii) is engaged in the operation or maintenance of any mechanically propelled vehicle operated;
(iii) supervises or oversees other employees engaged in manual labour;
(iv) is engaged in any capacity in any vessel registered in Malaysia; or
(v) is engaged as a domestic servant.

There is no distinction between 'contract of service' and employment contract in law. But, one must distinguish that from 'contract for service' is a contract to engage independent contractors who are self-employed, for their work.

All in all, the Malaysian employment law *does not recognize* a contract with a mixture of both 'contract of service' and 'contract for service'.

A *contract of service* also includes an apprenticeship contract which is a written contract entered into by a person with an employer who undertakes to employ that person and train or have him trained systematically for a trade for a specified period which shall not be less than two years in the course of which the apprentice is bound to work in the employer's service.
However, it must be noted that such apprenticeship contract must be distinguished from the master and pupil relationship under the Legal Profession Act 1976.

In fact, the Rules and Rulings of the Bar Council 10.09 provides that a master shall not, under any circumstance enter into any contract of or for service, with his/her pupil.
In another word, there cannot be employer-employee relationship in the case of master and pupil.

For the employee who does not cover by the EA, his employment relationship with the employer boiled down to the employment contract or contract of service, subject to such other statutes and case law mentioned above in the sources of employment law.

3.3 STATUTORY RIGHTS OF EMPLOYEE UNDER EA

1. **Terms less favourable than the EA shall be void**

Provided that the employee covered under the EA as stated in the First Schedule, it is the law that any term and condition of the employment contract or contract of service, which is less favorable than the provisions under the EA or any other regulations made thereunder shall be **'void'**, as per Section 7 of the EA. Section 7 of the EA further states that such term which is less favorable shall be substituted by those prescribed under the EA.

At this juncture, it is worth noting the other 6 Interesting Facts about Employment Contracts in Malaysia at the outset.

2. **In writing**

Section 2 of the EA defines a 'contract of service' as an agreement, be it **oral or in writing**, whether by implied or express conditions, where a person is engaged as an employee to serves his employer.

Notwithstanding that, Section 10 of the EA provides that such contract of service or employment contract shall be in writing if the **period of employment is more than a month**. It shall also include a termination clause by either party.

3. **Time for payment of wages**

Section 19 of the EA provides that every employer shall pay to each of his employees *no later than the 7th day* after the last day of any wage period. Depending on the employment contract, wage period will normally be 1 month.

If there is no wage period mentioned in the employment contract, the wage period shall be deemed to be 1 month.

'***Wages***' means the basic wages and all other payments in cash payable to an employee for work done in respect of his employment contract *excluding* such allowances, expenses and lawful deductions in the course of his employment.

4. **Probation**

There is basically no legal provisions for the required period of probation. Normally, it ranges from 1 to 6 months depending on the industries the employees are in.

Probation refers to a trial period of employment which can be culminated in the employees being confirmed or terminated.

Termination of probationer must, however, be subjected to '*just cause and excuse*' as provided under Section 20 of the Industrial Relation Act 1967.

As a general rule, there is no 'automatic confirmation', even though the probationary period has lapsed and an employee is neither terminated nor confirmed.

5. Termination

Under EA, either the employer or the employee may give notice or payment in lieu of notice to terminate the contract of service, as provided under section 12 of the EA.

The length of such notice shall not be less than the following depending on the employee's tenure of employment:-

Length of Notice of Termination	**Tenure of Employment ('X')**
4 weeks	X < 2 years
6 weeks	2 years ≤ X < 5 years
8 weeks	5 years ≤ X

Termination of an employee by the employer must also be subject to '*just cause and excuse*' as provided under Section 20 of the Industrial Relation Act 1967.

6. EPF & SOCSO & other contributions

Regardless of whether the employee falls under the purview of EA, the employer is *under legal obligations* to make the following statutory contributions:-

(a) Employees Provident Fund ('EPF')

(b) Social Security Organization ('SOCSO')

(c) Employee Insurance System ('EIS') Scheme

(d) Schedular Tax Deduction or 'Potongan Cukai Berjadual' ('PCB')

(e) Trade Union Subscription Fees or PTPTN loan repayment (subjected to a request in writing by the employee must first be obtained)

Rates of the above contributions can be found in Malaysian Employment Law: 5 Compulsory Statutory Contributions or Deductions

7. Annual Leave

According to Section 60E of the EA, every employee is entitled to the number of paid annual leave as follows depending on his or her tenure of employment:-

Annual Leave	Tenure of Employment ('X')
8 days	1 year ≤ X < 2 years
12 days	2 years ≤ X < 5 years
16 days	5 years ≤ X

For the incomplete 12 months of service, the employee's entitlement to paid annual leave shall be in direct proportion to the number of completed months of service.

8. Sick Leave

Under Section 60F of the EA, every employee's shall be entitled to the number of paid sick leave as follows where no hospitalization is necessary, depending on his or her tenure of employment:-

Sick Leave	Tenure of Employment ('X')
14 days	X < 2 years
18 days	2 years ≤ X < 5 years
22 days	5 years ≤ X

However, if hospitalization is necessary, every employee shall be entitled to *paid sick leave of 60 days* in the aggregate in each calendar year, as may be certified by such registered medical practitioner or medical officer.

It must be noted that the number of sick leave and hospitalization leave per year that every employee is entitled *shall not exceed* 60 days in total.

9. Maternity Leave and Paternity Leave

Regardless of whether the employee falls under the purview of EA, Section 44A of the EA provides that all female employees are *entitled to 60 consecutive days* of paid maternity leave.

Details of law in this respect can be found in 6 Legal Facts about Maternity Protection in Malaysia

There is so far no statutory requirement for employers in Malaysia to provide paternity leave to new fathers.

10. Public Holiday

The law, as provided under Section 60D(1) of the EA states that every employee shall be entitled to 11 gazetted public holidays, 5 of which shall be as follows:-

(a) the National Day;

(b) the Birthday of Yang-Di Pertuan Agong;

(c) the Birthday of the Ruler or Yang di-Pertua Negeri or Federal Territory day (all of which varies in different states);

(d) the Workers' day; and

(e) the Malaysia Day (16 September).

The employer is then free to *choose* the remaining 6 gazetted public holidays to make up the 11 days, and these chosen days must be effectively communicated with the employees either through notice or stated in the employment contract:-

(a) Birthday of the Prophet Muhammad (s.a.w)

(b) Chinese New Year (2 days, except 1 day in the states of Terengganu and Kelantan)

(c) Wesak Day,

(d) Hari Raya Puasa (2 days)

(e) Hari Raya Haji (1 day, except 2 days in the states of Terengganu and Kelantan)

(f) Deepavali

(g) Christmas day

(h) Nuzul Al-Quran – only in Federal Territory of Kuala Lumpur, Putrajaya, Labuan

Regardless of whether the employee falls under the purview of EA, all Malaysian employees shall also be entitled to any days which are appointed as a public holiday under section 8 of the Holidays Act 1951 which commonly known as Ad Hoc Public Holiday.

In the event an employee is required to work on a public holiday, he shall be paid *not less than 3 times* his daily rate of pay. The same principle applies should he be required to work overtime on the said public holiday.

Details of law on public holidays can be found in: It's Public Holiday Again!

11. Hours of Work and Rest day

Section 60A(1) of the EA says that an employee shall not be required under his contract of service to work:-

(a) more than 5 consecutive hours without a period of leisure of not less than 30 minutes duration;

(b) more than 8 hours in 1 day;

(c) in excess of a spread over a period of 10 hours in 1 day;

(d) more than 48 hours in 1 week.

Section 59 of the EA provides that every employee shall be allowed in each week a paid **rest day** of one whole day as may be determined from time to time by the employer.

Should the employee is required to work on a rest day, he shall be paid *not less than 2 times* his daily rate of pay. The same principle applies should he be required to work overtime on the said rest day.

12. Overtime

Section 60A(3) of the EA provides that any number of hours of work carried out in excess of the normal hours of work per day shall be classified as **overtime work**.

For any overtime work carried out in excess of the normal hours of work, the employee shall be paid at a rate *not less than 1 ½ time* his hourly rate of pay.

Under 60I of the EA, the hourly rate of pay means the ordinary rate of pay divided by the normal hours of work. The ordinary rate of pay shall be calculated according to the following formula: **Monthly salary/26 days**

Details of law on hours of work and overtime work can be found in Hours of Work and Overtime Work in Malaysia

13. Restraint of Trade Union

Section 8 of the EA prohibits any term in any contract of service that restrains the right of an employee to:-

(a) join a trade union;

(b) participate in trade union activities; and

(c) to associate with any persons with regards to a trade union.

Hence, any such provisions in the contract of service or employment contract are void.

14. Sexual Harassment

Section 81A – 81G of the EA provides that the law against sexual harassment are basically applicable to all employees regardless of whether they fall under the purview of EA.

The law now sets out the employer's duty to act by inquiring into the complaint of sexual harassment, failing which shall be liable to fine not exceeding RM 10,000.

Details of law on sexual harassment can be found in Sexual Harassment Law at Private Employment in Malaysia

15. Termination or Lay-off Benefits

Generally, it is the right of the employer to reorganize business for the purpose of the economy and convenience provided it acted bona fide:

Section 60J of the EA provides that the Human Resource Minister may provide for the employees:-

(a) termination benefits

(b) lay-off benefits

(c) retirement benefits

According to Regulation 6 of the Employment (Termination and Lay-Off Benefits) Regulations 1980, employees are entitled to the termination and lay-off benefits as stated below, depending on their tenure of employment:-

Number of Days' Wage for Each Year of Employment	**Tenure of Employment ('X')**
10 days	X < 2 years
15 days	2 years ≤ X < 5 years
20 days	5 years ≤ X

and pro-rata as respect an incomplete year, calculated to the nearest month.

16. Retirement Benefits

Retirement benefits are not compulsory benefit under the law unless if it is provided in the employment contract.

Other Relevant Provisions:-

1.

A. *It is pertinent to note that the **Minimum Wages Order 2018** and **Minimum Wages Order (Amendment) 2018** as enacted under Section 23 of the National Wages Consultative Council Act provides that the minimum wages rates*

payable to an employee shall be RM 1,100 per month. Details of which can be found in Employment Law: Minimum Wages in Malaysia.

B. ***Minimum Retirement Age Act 2012*** *provides that with effective from 01.07.2013, the employee's retirement age for the private sector is 60 years old, details of which can be found in Law on Retirement Age in Malaysia.*

C. *Pursuant to* ***Personal Data Protection Act 2010****, effective from 15.11.2013, 'active' measures need to be taken by the employer to comply with the Personal Data Protection Act 2010 and its regulations or risk facing prosecution with a maximum fine of RM 500,000 or up to three years in jail, or both. These are recommended compliance exercise to be undertaken by the employer:-*

(a) obtain a certificate of registration; and

(b) notify its employee of the privacy policy.

Details of which can be found in the Basics of Personal Data Protection for Employers

1.

D. *Any of such clauses in the employment contract for the purpose of restraining employee from pursuing a same career for after the termination of the employment contract is invalid in view of its direct contradiction with* ***Section 28 of the Contracts Act 1950*** *which states that "Every agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void." Detailed explanations can be found in The Legal Effect of Restraint of Trade clause in Employment Contracts*

3.4 OFFENSES AND PENALTY

Section 99A of the EA provides that any person who commits any offence under, or contravenes any provision of EA or any regulations made thereunder, in respect of which no penalty is provided, shall be liable, on conviction, to a fine not exceeding RM 10,000.

3.5 CONCLUSION

The above notes would be informative to deserved employers or employees out there, who earn an honest living through their very own efforts.

Lastly, let's also not lose sight of the part-time employee's rights whose average hours of work per week ranges between 30% – 70% compare to that of a full time employee.

3.6 EMPLOYMENT LAW II

There are three broad categories of employment relationships in Malaysia.

The most common category is employment relationships in the private sector between an employer and an employee. Given that this is a contractual relationship, the terms of the employment contract determine the rights and duties of the employer and the employee thereunder. Malaysian case law also recognises employees' implied rights and duties, including the implied terms of mutual trust and confidence, and the implied duty of fidelity. Private sector employment relationships are also regulated by statutory law in respect of many of the terms of employment, such as working hours, overtime, minimum wages, dismissal benefits, holidays, retirement age, statutory pension, and social security insurance benefits. Employees have a right to register a trade union, which, upon recognition by the employer, may commence collective bargaining on behalf of the employees. A registered trade union may also take industrial action, such as engaging in strikes and picketing. However, strikes are rare as there are many statutory restrictions to these actions.

Another category is employment relationships within the public sector, for those who hold public offices, such as members of the armed forces, the judicial and legal service, the general public service of Malaysia, the police force, the joint federal and state public services, and the education service and public service in each state. Employees who are in this type of employment relationship are afforded special protection under Article 135 of the Federal Constitution. Public officers are protected from dismissal or reduction in rank without being given a reasonable opportunity to be heard under Article 135(2) of the Federal Constitution.

The third category of employment relationship is a hybrid of the first two categories, and applies to employees of statutory authorities, such as those under a statutory body corporate or a local council. They are not employees as

provided in the definition of public service under Article 132 of the Federal Constitution and as such cannot be regarded as public servants under the Constitution. They are not regarded as private sector employees either, as they are employed by statutory bodies or authorities and perform 'public' functions. See Section III.i, which highlights the rights of such an employee in applying for *certiorari* to challenge a dismissal from employment.[2]

3.7 JURISDICTION TO DETERMINE EMPLOYMENT DISPUTES

Jurisdiction to determine employment disputes

The civil courts of first instance consist of magistrates' courts, the sessions courts and the high courts. If a claim is for monetary compensation for breach of an employment contract, these civil courts have the jurisdiction to hear the case. For example, if the claim is for salary in lieu of notice for dismissal on short notice or resignation given, respectively, by an employer or an employee, the civil courts can hear the case and award damages.

Apart from the civil courts, under the Employment Act 1955 (EA), the Director General of Labour (DGL) can hear employment disputes relating to the terms of a contract of employment or disputes relating to a breach of a provision of the EA or Wages Council Act 1947.[3] These disputes are brought before the Labour Court, which is presided over by the DGL; however, the DGL can hear cases only for employees earning 5,000 ringgit or less.

The civil courts and the Labour Court cannot order specific performance of an employment contract, which is prohibited under Section 20(1)(b) of the Specific Relief Act 1950. The courts that may order specific performance of an employment contract are the industrial courts, established under the Industrial Relations Act 1967 (IRA). The industrial courts have the power to order reinstatement,[4] grant back wages and grant compensation in lieu of reinstatement.

Public servants and employees of a statutory authority cannot file claims for reinstatement in an industrial court.[5] The only available remedy for a public servant or employees of a statutory authority is to apply for a judicial review and to challenge the dismissal in a high court. The usual remedy is a *certiorari* [6] to quash the decision for dismissal.

The high courts also exercise a supervisory function over the industrial courts and an appellate function over the Labour Court. Thus, the high courts have the power to hear judicial review applications to quash decisions by the industrial courts.[7] Furthermore, with effect from 1 January 2021, they also have the power to hear appeals from the industrial courts.[8] In the past, the high courts had limited powers to hear applications from the

industrial courts on questions of law only. Now they can hear appeals on questions of both law and fact. The high courts can also hear appeals of decisions by the Labour Court.[9]

Year in review

Parliament has passed the Minimum Wages Order 2020, which came into effect on 1 February 2020[10] and is applicable to all employees except domestic servants.[11] The minimum wage for an employee is increased to 1,200 ringgit per month for employees who work in specified cities and municipal council areas as set out the Schedule.[12] For other areas that are not specified in the Schedule, the minimum wage for an employee 1,100 ringgit.[13]

The Employees Provident Fund Act (the EPF Act) was also amended[14] and came into effect on 15 March 2020 save for Sections 6, 8 and 11, which came into effect on 1 October 2020.[15] The amendments, among others, allow a male employee to transfer 2 per cent of the 11 per cent of his monthly contributions into the account of his lawful wife.[16] Additionally, an employee who is more than 55 years old but is not yet 60 years old can withdraw his or her contribution if he or she is (1) physically or mentally incapacitated from engaging in an employment, or (2) not a Malaysian citizen and is about to leave Malaysia and has no intention of returning.[17]

As the year 2020 was an exceptional year because of the spread of covid-19, the Malaysian Parliament has also enacted the Temporary Measures for Reducing the Impact of Coronavirus Disease 2019 (Covid-19) Act 2020 (the Covid-19 Act) to reduce the impact of the pandemic on all Malaysian citizens. The temporary measures include, among others, the protection or deferment of rights under contract and extension or deferment of the statutory limitation periods to take action. For example, an employee has 60 days from the date of cessation of employment to lodge a complaint with the Industrial Relations Department under the IRA. The Covid-19 Act extends the period for lodging such a complaint by excluding the period from 18 March 2020 to 9 June 2020 for the purposes of calculation of the limitation period. This excluded period is also applicable for the purposes of calculation of the time frame for according recognition of a union or notification of non-recognition of a union under the IRA. Therefore, employers who had dismissed employees shortly before or during the excluded period must be vigilant to look out for notification from the Director General of Industrial Relations (DGIR) to attend a conciliation meeting even outside the 60-day period.

The Workers' Minimum Standards of Housing and Amenities (Amendment) Act 2019 (the WMSHA Amendment Act) came into force on 1 June 2020, and The Employees' Minimum Standards of Housing, Accommodations and Amenities (Accommodation and Centralized Accommodation) Regulations 2020 (the EMSHAA Regulations) came into force on 1 September 2020. All employers who provide accommodation for their employees must comply with the requirements laid down in the WMSHA Amendment Act and the EMSHAA Regulations. The requirements, among others, are that employers must:

a. obtain a certificate for accommodation from the DGL if they intend to provide accommodation for employees on their premises;

b. inform the DGL within 30 days of the date an employee occupies the accommodation;

c. comply with the safety and health requirements under the WMSHA Amendment Act and the EMSHAA Regulations;

d. comply with the minimum standards under the WMSHA Amendment Act and the EMSHAA Regulations; and

e. ensure that decent and adequate amenities are provided.

Significant cases

i Ahmad Zahri Mirza Abdul Hamid v. AIMS Cyberjaya Sdn Bhd[18]

In this case, the appellant was hired for several years on the basis of successive fixed-term contracts. When the contract was due for renewal, the parties could not agree on certain terms and the respondent chose not to renew the contract.

The Federal Court considered two questions of law, namely, whether (1) the need for a work permit is a material consideration in determining whether an employment contract is a genuine fixed-term contract and (2) a contract of employment that is renewed successively without application by the employee and without any breaks in between is actually permanent employment. In answering the first question, the Federal Court considered whether the corporate veil of a group of companies can be lifted to find that they are common employers, as the employer used to be AIMS Data Centre 2 Sdn Bhd (ADC) prior to a consolidation into the respondent company. The Court held that ADC and the respondent company were not two separate legal entities and there was an essential unity of group enterprise. As such, it was held that the appellant's contract of employment was a continuous one from ADC to the respondent company. The Court affirmed the decision in *Hotel Jaya Puri Bhd v. National Union of Hotel, Bar & Restaurant Workers & Anor*[19] and stated that it is still good law.

The Court also stated that in deciding whether the fixed-term contract is actually a permanent contract, several factors had to be considered, such as the intention of the parties, the employer's subsequent conduct during the course of employment, the nature of the employer's business and the nature of the work that an employee is engaged to perform. On the facts, the Court held that the appellant's employment with ADC was not one-off, seasonal or temporary employment, as it was continuous employment without a break from 2009 to 2013. Hence, the corporate veil should have been lifted.

The work permit was not an issue in this case because the Court opined that all workers should be treated with fairness, dignity and equality, consonant with Article 8(1) of the Federal Constitution. Citizenship of the appellant had no bearing in deciding whether the appellant was a permanent employee or was under fixed-term contract.

ii Rajendiran Manickam & Anor v. Palmamide Sdn Bhd & Anor[20]

In this case, the plaintiffs (being employees of the defendants) suffered severe burns as a result of an explosion and fire resulting from welding work being done in another part of the factory by the employers' contractors. The plaintiffs received compensation from the board of the Social Security Organisation (SOCSO) but were also claiming for damages for negligence, breach of statutory duties and occupiers' liability arising out of the injuries they sustained.

The Court of Appeal had to decide on the issue of whether or not Section 31 of the Employees Social Security Act 1969 (the SOCSO Act) bars common law claims for negligence. Under Malaysian law, an employer will make a monthly contribution under the SOCSO Act and if there is an accident at work resulting in injury, the injured employee will receive certain compensation under the SOCSO Act. Section 31 of the Act provides that the employee, or his or her dependants, shall not be entitled to receive or recover from the employer any compensation or damages under any other law for the time being in force in respect of an employment injury sustained as an employee under SOCSO.

The Court held that the SOCSO Act is a social piece of legislation and there is no reason why an employer is immunised against all claims for aggravated and exemplary damages by contributing towards a SOCSO compensation scheme if the employers are negligent in providing a safe place of work for their employees. The Court of Appeal further stated that if there is any ambiguity in the legislation, it has to be resolved in favour of the injured employee. The Court of Appeal also relied on Section 28A of the Civil Law Act 1956, which stipulates that, when assessing damages for personal injury, the court should not take into account 'any sum that has been or will or may be paid under any written law relating to the payment of any benefit or compensation whatsoever in respect of the personal injury'. Therefore, this an issue that needs to be determined in a full trial and it is not plain and obvious for the claim to be struck out. The matter was ordered to be remitted to the Sessions Court for trial.

Basics of entering into an employment relationship

i Employment relationship

A contract of employment may be made in writing or orally. However, for employment positions governed under the EA, a contract must be in writing if it is for a service for a specified period exceeding one month or for the performance of a specified piece of work where the time reasonably required for completion of the work exceeds one month.[21] A

written contract must include a clause setting out the manner in which the contract may be terminated by either party.[22] It must be signed by both parties and may be altered only by mutual consent.

Not all terms of employment are found in an employment contract. Some may be found in an employment handbook, which is usually incorporated by reference in the employment contract.

An employment contract can be for a fixed term, and a genuine fixed-term contract is recognised in Malaysia. However, a court will look at the substance rather than the form of the fixed-term arrangement. A fixed-term contract that has been repeatedly renewed may be regarded as a sham arrangement and may be treated as a permanent contract of employment.

Under the Minimum Retirement Age Act 2012 (MRAA), a fixed-term contract that exceeds the period stipulated in the Schedule to the MRAA can end only when the employee reaches retirement age.[23] Therefore, a fixed-term contract loses its efficacy if it is for a fixed term (inclusive of any extension) that is longer than the period permitted under the MRAA.[24] In these circumstances, the fixed-term contract in substance becomes a permanent contract, whereby it will only end when the employee reaches retirement age (which is 60 years).

ii Probationary periods

The law in Malaysia recognises probationary periods. There is no statutory minimum notice of dismissal for a probationer and, as such, termination is a matter of contractual right. Nevertheless, for employees governed under the EA, when the reason for dismissal falls within certain categories, such as redundancy or closure of business, there are minimum periods of notice that must be given to the employee.[25] A probationer has a right to lodge a complaint for unfair dismissal under the IRA.

iii Establishing a presence

There is no legislation that prohibits a foreign company from hiring employees without being officially registered to conduct business in Malaysia. However, the foreign company itself must not conduct business in Malaysia.[26] Merely hiring an employee may not by itself be regarded as conducting business in Malaysia. If, however, these employees are actively soliciting business in Malaysia, and concluding contracts in Malaysia, there is a risk that the foreign company may be regarded as conducting business in Malaysia.

There is also no legislation that prohibits a foreign company from engaging an independent contractor without registering in Malaysia. However, the foreign company must consider whether engaging an independent contractor or an employee may give rise to the foreign company having a permanent establishment (PE) in Malaysia. A foreign company is regarded as having a PE in Malaysia if the independent contractor or employee:

a. continues supervisory activities in Malaysia in connection with a building or work site or a construction, an installation or an assembly project;

b. acts on behalf of the foreign company in Malaysia and has the authority to conclude contracts on its behalf and habitually does so, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification; or

c. maintains a stock of goods in a place in Malaysia from which the independent contractor or employee delivers goods, or regularly fills orders on the company's behalf.

The consequence of having a PE in Malaysia is that income generated by the business will be subject to Malaysian income tax.

If a company hires employees in Malaysia, the employer is obliged to pay benefits due under the following:

- an employee provident fund;

- SOCSO (social security protection); and

- an employment insurance system (EIS).

Income tax will be deducted at source as a monthly tax deduction. In practice, it would be difficult for a foreign company to comply with the above requirements without a locally registered company. Typically, payroll companies will be employed by foreign companies to perform payments of the above statutory contributions and deductions.

Restrictive covenants

An agreement in restraint of trade is void and unenforceable pursuant to Section 28 of the Malaysian Contracts Act 1950 (CA). Unlike other common law jurisdictions where an agreement in restraint of trade may be valid depending on the 'reasonableness'[27] of the restraint, in Malaysia, once a clause is found to be an agreement in restraint of trade, it is automatically void regardless of the reasonableness of the restraint.[28]

The non-enforceability of an agreement in restraint of trade applies only to post-contractual restraint. Therefore, a non-compete restraint that is imposed on an employee during the life of the contract for employment is not a covenant in restraint of trade and is not rendered void under Section 28 of the CA.

Although post-termination non-compete clauses are clearly void by reason of Section 28 of the CA, a non-solicitation clause may be upheld if it is regarded as reasonable.[29]

Wages

i Working time

There is no regulated or fixed number of working hours except for employees who are governed by the EA. Under Section 60A of the EA, employees must not be required to work for more than five consecutive hours without a period of leisure of not less than 30 minutes, or for more than eight hours in one day, or spread over a period of more than 10 hours in one day, and for no more than 48 hours in one week. Furthermore, no employer is allowed to require any female employee to work in any industrial undertaking between 10pm and 5am, nor work for a day without having had a period of 11 consecutive hours free from the work.[30] The DGL has the power to provide a written exemption to any female employee, or classes of female employees, from any restriction in Section 34 of the EA. In practice, these exemptions have been given.[31] There is also a blanket exemption given for all employers, provided that certain conditions are met.[32]

ii Overtime

An employee is entitled to a minimum overtime rate of one and a half times the usual hourly rate of pay for work beyond the employee's normal hours of work per day.[33] For work carried out in excess of the normal hours of work on a rest day, the employee is entitled to twice the hourly rate of pay.[34] For work carried out in excess of the normal hours of work on a public holiday, an EA employee is entitled to three times the hourly rate of pay.[35] Employees cannot work more than 104 hours of overtime in one month.[36]

Foreign workers

The Immigration Department, as a matter of practice, draws a distinction between 'foreign workers', who are blue-collar workers in manufacturing, construction, plantation, agriculture and services, and 'expatriates', who are white-collar workers. To hire expatriates, an employer must apply for passes, such as an employment pass and a professional visit pass, via the Expatriate Services Division website. As part of the government's initiative to provide employment opportunities to local people, companies in Malaysia are now required to advertise job vacancies in Malaysia through the JobsMalaysia online portal for a minimum of 30 days before employment pass applications for expatriates can be submitted for approval.[37] Companies may only proceed with the relevant employment pass applications if no local candidate has been successfully hired for an advertised role and an acknowledgement letter will be issued by JobsMalaysia. Implementation of this policy takes effect on 1 January 2021.

As regards the hiring of a foreign worker, the employer must apply in advance for immigration security clearance (ISC) at an ISC centre in the source country and for a visa with reference from the Immigration Department. An employer who employs a foreign worker must furnish the DGL with the particulars of the foreign worker, within 14 days of employment, by forwarding the particulars to the nearest office of the DGL.[38] In respect of registration, the employer must prepare and keep one or more registers containing

information regarding each foreign worker it has employed. There is currently no express limitation on the number of foreign workers that a company may employ but a maximum quota of foreign workers must be obtained by employers and companies from the Ministry of Home Affairs.[39]

Employers must apply to the Immigration Department for the necessary visa and visit passes for foreign workers. New foreign workers starting work in Malaysia on or after 1 January 2019 will have to be registered by their employers with SOCSO under the Employment Injury Scheme. The employer or company is also required to make EIS contributions to the relevant employment insurance fund. This EIS fund provides for a number of benefits, such as re-employment allowance, reduced income allowance, training allowance and assistance with finding a job.

Generally, employers do not have to contribute to an employee provident fund unless the foreign worker elects to contribute. In such a case, the employer's share of the contribution is five ringgit per month. Foreign workers who leave Malaysia permanently may withdraw their contributions when leaving.

Foreign workers are protected under the local employment law. Workers whose wages do not exceed 2,000 ringgit or whose nature of work falls under the First Schedule of the EA are protected by the EA. The EA prescribes certain minimum benefits and rights of an employee. A foreign worker is also protected from unfair dismissal.[40]

An employer will not be permitted to obtain an employee's bank account information as it is protected by banking secrecy laws.[41] Written consent is required from the employee before a bank will disclose this type of information.

See also Section XII regarding data protection and background checks.

Global policies

There is no express legal requirement for a company to have internal disciplinary rules. Nevertheless, it is good practice to maintain such policies and procedures. An employer has the management prerogative to set down guidelines for the discipline and protection of its employees and to meet its legitimate business interests.[42] Therefore, there is no need for an employer to obtain approval from the employees or representative body for its rules.

An employer is required to investigate any claim by an employee that he or she has been sexually harassed and must inform the complainant within 30 days. If the employer chooses not to investigate, it must have reasons for that decision. An employer may refuse to investigate if the claim has been investigated previously, or if the claim is frivolous or not made in good faith. If the employer is satisfied that a case for sexual harassment has been proven, the employer must take disciplinary action against the accused employee, which

may include dismissal, demotion or any other lesser punishment as the employer deems just and fit. If a suspension without wages is imposed, it must not exceed two weeks.

Further, a complainant who is dissatisfied with the refusal by his or her employer to investigate a complaint of sexual harassment may refer the matter to the DGL. The DGL may direct the employer to conduct an inquiry if the DGL thinks the matter warrants it.

Although it is not mandatory for a company to have rules relating to the prevention of corruption, it is highly advisable to do so. Section 17A of the Malaysian Anti-Corruption Commission Act 2009 (the MACC Act), which came into force on 1 June 2020, imposes liability on a commercial organisation if a person associated[43] with that organisation is involved in corrupt activities. In this regard, Section 17A(1) of the MACC Act provides that it is a defence for the commercial organisation to prove that it had 'adequate procedures' in place to prevent persons associated with the organisation from undertaking any corrupt activity.

There is no requirement for the rules in this respect to be written in the local language. It is also not a requirement for the rules to be signed by employees; it is sufficient that the rules are brought to the attention of employees.[44] In this regard, it is sufficient if the rules are posted on the company's intranet and reference to this is incorporated in the employment contract.[45]

It is common in Malaysia for disciplinary rules to be set out in full in an employment handbook and incorporated by reference in employment contracts.

Parental leave

A female employee is entitled to 60 days of maternity leave for each and every birth. A female employee is also entitled to a maternity allowance (which is paid maternity leave) if she fulfils two conditions: (1) she must have no more than five surviving children at the time she gives birth; and (2) she must have worked with the employer for at least 90 days during the nine months before she gives birth and at least one day in the four months before she gives birth.

Save and except for termination of an employment contract on the ground of closure of business, an employer is prohibited from dismissing a female employee during the period she is entitled to maternity leave.[46] If an employee remains absent from work after the expiry of her maternity leave because of an illness arising out of her pregnancy and confinement that results in her being unable to work, an employer can only terminate her services if she remains absent for more than 90 days after the expiry of her maternity leave.[47]

Translation

For an employer with employees who are governed by the EA, there is an obligation to maintain one or more registers containing information regarding each of those employees.[48] The details must include, among other things, the name, gender and age of the employee, and the terms and conditions of employment, such as rates of pay, allowances, overtime rates, agreed hours of work, annual leave, sick leave, holidays and other benefits.[49]

Employees must have the right to examine the register, which must be maintained and kept in a place where every employee can have access to it. The register must be in the national language (i.e., Malay).[50] Failure to translate any documents as necessary will render the employer subject to a fine.

Although there is no express statutory provision for a contract of employment to be in Malay, some labour officers take the view that because the register that contains the terms and conditions of employment must be in Malay, it follows that the contract of employment must also be in Malay. Therefore, for employees governed by the EA, it is preferable that their employment contracts are translated into Malay.

Employee representation

Employees in Malaysia have an unfettered right to join a trade union and this right cannot be restricted by contract.[51] Before a trade union can represent its employees, however, it must satisfy two requirements: (1) it must be registered under the Trade Unions Act 1959 (TUA); and (2) it must be recognised by the employer under the IRA.

Once a trade union is duly registered, it may serve on an employer a claim for recognition. The employer can refuse to recognise the trade union; if it does so, the matter will be referred to the DGIR for a decision. The DGIR will make enquiries as to the competency of the trade union and to conduct a membership verification. A secret ballot will be carried out to ascertain whether the trade union commands the requisite majority to represent the employees in the establishment.

When a trade union has been accorded recognition in respect of any worker or class of worker, no other trade union shall make any claim for recognition in respect of the same workers or class of workers unless three years have elapsed since the initial recognition, or the original trade union no longer exists.

A trade union representative cannot be dismissed or discriminated against by reason of his or her position as an officer of the trade union.[52]

Data protection

The Personal Data Protection Act 2010 (PDPA) seeks to regulate the processing of any information that relates directly or indirectly to an identifiable individual (the data subject), in commercial transactions (personal data) by any party who processes personal data, or has

control over or authorises the processing of personal data (the data user). An employer would be the data user and an employee would be the data subject.

The PDPA applies to a person's personal data if the person is established in Malaysia and the personal data is processed in Malaysia. The PDPA does not apply to any personal data processed outside Malaysia unless the intention is for it to be processed further in Malaysia.

i Requirements for registration

The PDPA requires the registration of certain classes of data users, which are described in the Personal Data Protection (Class of Data Users) Order 2013. A data user who belongs to two or more classes of data users must make a separate application for registration for each class to which the data user belongs.

ii Cross-border data transfers

Data users cannot transfer personal data outside Malaysia unless the transfer is to a location specified by the Communications and Multimedia Minister. The Minister has issued a public consultation paper on the Personal Data Protection (Transfer of Personal Data to Places Outside Malaysia) Order 2017, though the Order has yet to be finalised and published in the *Official Gazette*. Notwithstanding the foregoing, data users may transfer any personal data to a place outside Malaysia under certain conditions, for instance, if an employee has consented to the transfer, the transfer is necessary to conclude a contract between an employee and an employer, or the transfer is for the purpose of any legal proceedings.

iii Sensitive personal data

Sensitive personal data means any personal data consisting of information about the physical or mental health or condition of a data subject, his or her political opinions, religious beliefs or other beliefs of a similar nature, or the commission or alleged commission of any offence. An example of sensitive personal data is an employee's medical information.

iv Background checks

There is no express prohibition of background checks. An employer may carry out credit checks on an employee through a licensed credit reporting agency in Malaysia. Nevertheless, credit reporting agencies usually require the consent of employees before divulging any information.

Criminal checks are more difficult to procure, as the cooperation and assistance of the police is required. However, for offences under the MACC Act, an employer or future employer may carry out an initial filter or check on a prospective employee by searching the records of corruption offenders on the MACC website.[53]

Discontinuing employment

i Dismissal

Any termination of employment in Malaysia must be for 'just cause or excuse'.[54] The following are the commonly recognised categories of just cause or excuse for termination of a contract of employment:

- misconduct;
- retrenchment;
- poor performance;
- retirement;
- expiry of a genuine fixed-term contract;
- resignation; and
- by mutual agreement.

In an unfair dismissal case, the burden is on the company to prove that the contract of employment is terminated with just cause or excuse. An employee who believes that he or she has been dismissed without just cause or excuse can make representations in writing to the DGIR to be reinstated to his or her former employment.[55] These representations may then be referred to an industrial court, if the DGIR is of the view that there is no likelihood of these representations being settled.[56]

There is no notification requirement for termination of employment in Malaysia. However, for termination by reason of retrenchment or under a voluntary separation scheme, the employer will need to file the requisite PK Forms I to IV at least 30 days before the date of cessation of employment.[57] Thereafter, the employer will also need to file PK Forms V and VI. There is no duty to notify the trade union of any termination of employment unless it is expressly provided for in the collective agreement.

For termination by reason of misconduct, no notice is required as an employee may be summarily dismissed. However, it is generally accepted practice that this step of summary dismissal is taken only after having conducted an inquiry for the employee to be given a chance to defend himself or herself. The requirement for due inquiry is even more important in terms of EA employees by reason of Section 14(1) of the EA.

If the ground for termination is redundancy or poor performance, the employer should comply with the notice requirement provided for in the contract. The notice may be waived by either party, or the employer may decide to pay salary in lieu of notice.

ii Redundancies

Retrenchment is a term to describe instances where a business entity terminates the services of employees who it considers as surplus and redundant to its business requirement. It is the right and privilege of an employer to reorganise his or her business in any manner he or she sees fit, so long as the procedure is bona fide and does not have any collateral purpose.[58]

Note, however, that an ill-planned retrenchment exercise may be challenged by the employees by way of unfair dismissal representations to the DGIR, which subsequently may be referred for adjudication at an industrial court. In the event that the legality of the retrenchment exercise is challenged, the onus is on the company or employer to show that there was a real redundancy situation and the retrenchment is justified to safeguard its interest.[59] The relevant questions for consideration are (1) whether there is a real redundancy situation leading to the retrenchment exercise and, if so, (2) was the consequential retrenchment exercise made in compliance or in conformity with accepted standards of procedure?

There is no legal difference between multiple redundancies, collective dismissal or reduction in force. However, practically, if there are multiple redundancies, or there is a collective dismissal or reduction in force, it would be more difficult for an employee to contend that he or she was negatively affected as the retrenchment is affecting a number of employees within the organisation, not just one employee.

A company should try to comply with the Code of Conduct for Industrial Harmony (the Code), which is relevant in redundancy situations.[60] Although the Code does not have the force of law, the industrial courts frequently use it as a reference guide when deciding whether an employee has been properly retrenched using fair procedures. The Code sets out the steps that should be taken by an employer in circumstances where redundancy is likely to occur, such as to limit recruitment, to restrict overtime work, to restrict work on the weekly day of rest, to restrict the number of shifts or days worked per week, to restrict the number of hours of work and to retrain or transfer employees to other departments or types of work.[61]

A company is required to give sufficient notice of termination to its employees as provided for in the employment contract. For employees governed by the EA, however, an employer is obliged to give a minimum notice of termination (as set forth in the EA)[62] to employees before the date of retrenchment. Either party may waive the right to the requisite notice. If notice is not given, however, the employer would be liable to pay employees an indemnity for the lack of notice equivalent to the notice period.

There is also a requirement to pay retrenchment benefits for employees governed by the EA provided they have worked for a continuous period of 12 months or more.[63]

For unionised employees, an employer must consider the terms of the collective agreement and determine whether there are clauses dealing with retrenchment or termination

benefits. If so, the employer should pay in accordance with the terms of the collective agreement.

The employer should also consider the terms of the contract of employment and the employment handbook and determine whether retrenchment or termination benefits are provided for in the contract or handbook. If so, the employer should pay in accordance with the terms of the contract or the handbook if the terms are more favourable than the statutory termination benefits.

Although a genuine retrenchment is recognised by the industrial courts as a valid ground for termination of employment, some companies prefer to offer a voluntary separation scheme (VSS) to reduce the number of employees. By its nature, a VSS is on a voluntary basis, offered at the discretion of the employer to the employees, who may choose to accept or reject the VSS. It is common for companies to offer a VSS before a retrenchment exercise.

Occasionally, instead of conducting a VSS, a company might decide to enter into a one-to-one negotiation with each employee to agree to a mutual separation agreement. This is also an acceptable manner to end a contract of employment. However, the company must be cautious so as not to be accused of coercing or forcing an employee to sign a mutual separation agreement.

Transfer of business

Although statutory termination benefits are normally payable to employees governed by the EA by reason of redundancy, this is not necessarily the case if the termination of employment is by reason of a change of business ownership. Termination benefits are not payable if, within seven days of the change of ownership, the transferee offers to continue to employ the employee on terms and conditions of employment that are no less favourable than those under which the employee has been employed before the change occurs, and the employee unreasonably refuses that offer.[64]

Outlook

There have been significant amendments to the IRA by the Industrial Relations (Amendment) Act 2020 (IR(A)A), which came into force on 1 January 2021 (except for Sections 4, 5(c), 5(d), 5(e), 5(f), 8(b), 10, 11(a), 11(b), 11(c), 18, 33 and 34). By reason of the amendments to the IRA coming into force, the DGIR will be required to refer complaints of unfair dismissal to an industrial court for an award in the event that parties are unable to reach a settlement and the referral does not involve any exercise of discretion on the part of the DGIR.[65] This means that all cases that cannot be resolved at a conciliation stage will automatically be referred to an industrial court for adjudication. This may lead to a flood of cases being referred to the industrial courts, including frivolous claims.

Another significant amendment to the IRA is with regard to the industrial courts' powers to continue with legal proceedings notwithstanding the death of a worker. Prior to the 2021 amendments to the IRA, a claim for unfair dismissal under the IRA was regarded as a personal claim and the cause of action abates upon the death of the employee. Thus, the deceased employee's claim under the IRA comes to an end and the personal representative or next of kin of the employee cannot continue with the action on behalf of the deceased employee's estate. Under the amended IRA, the industrial court has the power to order for proceedings to continue and even award compensation to a deceased employee's next of kin.[66]

The amendments to the IRA include a right of appeal against an industrial court decision to a high court. With this amendment, any party has 14 days from the date of receipt of the award to appeal to a high court.[67] The procedures for the appeal will follow the Rules of Court 2012 and will be treated as an appeal from a sessions court to a high court, with necessary modifications. This may render it no longer necessary for litigants to resort to the cumbersome method of judicial review as a primary form of challenge to an industrial court award. The right to apply for judicial review against an industrial court award will still apply for awards made in relation to a reference under Section 20(3) before 1 January 2021.[68]

Employers in Malaysia will also need to prepare for the implementation of amendments to the EA. The proposed amendments are, among others, to expressly prohibit employers from discriminating against jobseekers or current employees on the grounds of gender, religion, race, disability, language, marital status or pregnancy, reducing working hours, and to require employers to have a written code of prevention of sexual harassment at the place of employment. Employers must not engage in discriminatory conduct.

With regard to the TUA, one of the proposed amendments is to revoke the Director General of Trade Union's discretion to refuse the registration of a trade union unless there are compelling reasons to do so. Trade unions are no longer restricted to representing members of a particular trade, establishment, occupation or industry.

Another important piece of legislation is the Occupational Safety and Health Act 1994 (OSHA) and a number of proposed significant amendments under the Occupational Safety and Health (Amendment) Bill 2020. Once the latter is passed, application of the OSHA will be widened to ensure that the safety, health and welfare of all employees from all the industries are given protection. Employers as well as principals will also need to take up additional responsibilities, such as those that may be required to deal with emergencies and a new duty to conduct risk assessments at the workplace. The proposed amendment to the OSHA makes it compulsory for employers to carry out hazard identification, risk assessment and risk control measures. To provide more protection for employees, the amendment also allows an employee (subject to certain conditions) to remove himself or herself from any danger or work if there is reasonable justification to believe that there is an imminent danger.

3.0 Ethical issues in Employment laws

INTRODUCTION:

There are two acts particularly deal with employment relation in Malaysia, The Employment Act (EA) 1955 and Industrial Relation Act (IRA) 1967. Both acts define what the word 'employee' in Malaysia means is.

While Industrial Relation Act 1967 describe 'Employee/Workman' as any person, including an trainee, employed by an employer under a contract of employment to work for appoint or repayment and for the functions of any measures related to a trade dispute involve any such person who has been dismissed, discharged in relation with or as a effect of that dispute .

2. Relationship between employer and employee:

One of the most important questions in employment law is how to conclude the Relationship between employer and employee?

Determining employer and employee relations is an important part of business, not only because it determines the obligations and responsibility of both the employer and the employee but also because the survival of such relationship vests an employer with certain rights and duties.

Employer employee relations regard to the communication that takes place between representatives of employees and employers. Much of the employee relations engage employees and employers working together.

The employment contract must compile with local labor laws that establish minimum employment standards such as the minimum wage minimum benefits and rights.

Employees and Employers have responsibilities to each other; they must also look forward to their rights to be upheld. These rights and responsibilities relating to areas such as Health and Safety, the provision of Terms and Conditions of Employment,

The relationship between employer and employee is ruling by the Employment Act 1955. The act covers all instruction manual workers and non-manual workers gain below RM 1500. Current, amendments to the Act as well permits for all workers to complain to the employment Department if his or her employer infringes any circumstances within the employee's contract of service.

2.1 The relationship between the employee and the employer under the Employment Law 1955.

employment relationship.gif

The Employment Act 1955 regulates the employment relationship between the employer and employee in addition to the terms and conditions under which employers may employ employees. The employment relationship foreseen by the Act is the old “master and servant” relationship, i.e. the well-known “contract of service” relationship. And among the terms and conditions regulated by the Act are the hours of work wages and the benefits, as well as other terms and conditions, of employment and work.

2.3 Employment contract:

When you want to determining any legal relationship, you have to look at the agreement or a contract between the parties.

The instant an applicant totally accepts your offer of a job, a contract of employment comes into existence. The terms of the contract can be oral, written, implied or a mixture of all three.

Hitchcock v Post Office (1980) :

Mr. Hitchcock ran a sub-post office. The post office exercised some control over his activities, such as the payments of benefits, sale of stamps etc. but he could delegate his work to others and took the risk of profit or loss.

Court held he was an independent contractor. The control the post office did have was due the need to ensure financial control and security rather than to control his role as a manger.

Even if you do not issue a written contract, you are under a legal duty to provide most employees with a written report of main employment details within two months of the start of their employment with you. If you have an employee who is going to work overseas for more than a month within two months of beginning work, you must give them their written statement before they leave. The written statement is not itself the contract but it can provide proof of the terms and conditions of employment between you and the employee if there is an argument later on. These direct lays out your legal obligations when issuing a contract of employment or a written statement.

3.0 The rights and responsibilities of an Employer:

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As with the employee, the employer must take all reasonable steps to make it possible for the employee to perform his or her part of the agreement and must not divest the employee of the opportunity to perform the work. The law increasingly has been suggesting that an employer does not have the right to just have someone sitting around so long as the employer pays him or her. In short, there may also be a responsibility to give an employee something essential to do. This is still a growing area of law and if an employer has no work to provide it may lead to the employee’s reduction of expenditure.

The common law provides rights of employer are implied into contracts of employment as well as those covered by the employment Act 1955.

3.1 The rights:

The common law rights of employer include among others-

Right to be indemnified by the employee

Referring to the employment act 1955, employer has right to secure that employee is going to use his or her all skills, awareness and capabilities to achieve the tasks will be assigned by employer.

Right to be obeyed in lawful orders by employee

Employer has the rights to receive compliance from employee in lawful orders, the lawful orders according to the employment contract, they have signed. And if employees will not comply with, he will be termed unruliness and he has to be disciplined.

Right to be rendered service from employee

The employer has right to receive services which will be provided by employee according to the employment act 1955. And if the employee does not comply the disciplinary will be taken upon him or her.

Right to be complied with statutory obligations by employee

The employer has to receive the statutory obligations from employee, it means the employee has to carry out his lawful duties and a responsibility according to the employment act instance employee has to show good faith to the employer.

Right to receive service from employee in relation to the work during spare time

This means employees are to work for their employer in their working time according to the employment contract, and allowed to work elsewhere when it is different kind of business, it does not interfere with normal work and conducted during spare time.

Right to receive reasonable skill and knowledge from employee

An employee has to implement reasonable care and skills in the performance of his work to the employer. And this right ought to be practical to work for which the employee has been hired to do and which he has claimed he is competent to do.

3.2 The duties (responsibilities):

The common law provides duties of employer are implied into contracts of employment including those covered by the employment Act 1955.

Employer be obligated the following duties to their employees-

The duty to pay remuneration:

This duty normally exists even if there is no work to be done, particularly in relative to fixed-term contracts. on the other hand, instead of offering a wage, some employers may choose to pay an employee for work done or services provided by means of commission, fee, or receipt of tips from customers. Nevertheless, it ought to be well-known that this duty is affected by legislation or award provisions which successfully allow an employer to legally stand down employees in certain situation.

The obligation to provide work:

The justification being that workers paid by time ought to be paid for being ready, able and willing to work for the period of the agreed hours. There is commonly no duty to provide work if pay is still ongoing . On the other hand, it has been pointed out that in these days a man has, by insinuation in the employment contract, a right to work, whether or not the employer has this obligation is dependent on the category of employment contract.

The duty to indemnify:

The employer ought to indemnify the employee for all expenses, sufferers and liabilities legally incurred by the employee in while performing the work instructed. nevertheless, the employer is absolved of this duty in cases where-

The employee knew that he was doing an unlawful act; or

The employee knew that the employer had no right to give the order in matter

Duty of care:

The employer has to provide-

Safe environment and make sure that the equipment which the employee uses is safe; and

A safe scheme of work.

The employer is only requisite to take reasonable care, but where there are strange situation, particular safety procedures should be taken. however employers are not bound to provide total safety to employees, based on the normal of reasonableness required for employers, they are still liable for-

Intrinsic risks, reasonable foresee ability risk of damage, seriousness of the risk, cost.

Janata Bank v Ahmed (1981) :

Mr., Ahmed worked as a bank manager. Over several years he had agreed to give bank loans and mortgages to customers who were obviously bad credit risks. The bank supposed that in

doing so he had been negligent in performing his duties. After dismissing him, Janata sued him for damages amounting to $ 34 640.

Court held: Janata's claim was upheld because Ahmed failed to exercise the good care and skill required under his contract of employment

Duty to treat employee with respect and trust:

There appears to be a trend issued by recent cases that an employee ought to be treated and trust and not in a random or vindictive manner.

Isle of Wight Tourist Board v Coombes (1976) :

A manager was overheard discussion to another employee. He said that his personal secretary was 'an intolerable bitch on a Monday morning'. She was upset and resigned.

Court held the manager had breached the duty of trust and respect.

Duty to give testimonials and references:

An employer is not lawfully obliged to offer a reference. Although, when the employer does so it have to be true and fair to the best of his awareness. every statement must not be misleading. An employer owes a duty of care together to the subject of the reference and to the receiver, and has to take reasonable care in its groundwork. Ought to an employer fail to do so, he might negligent in a civil action if the employee or the recipient suffers damage consequently.

Duty to comply with statutory obligations:

An employer ought to abide by all related legislation, e.g. worker's compensation, occupational health and safety, etc.

3.3 Malaysian Case:

Court Award (1)

ZAINUDIN BIN KASSIM V. JOHAN CERAMIC BERHAD (2008):

Right to be obeyed in lawful orders by employee:

Whether there is justification for the Claimant in refusing to comply with the directive given by his superior? Whether an employee is required to obey orders if it is doubtful whether the orders are legal or not.

This is a Ministerial reference to the Industrial Court under section 20(3) of the Industrial Relations Act 1967 made on 28th August 2006 for an award in respect of the dismissal of Zainudin bin Kassim ("the Claimant") by Johan Ceramic Berhad ("the Company").

Facts from this case

In this case, The Claimant commenced employment with the Company on 11th August 1983 and was subsequently confirmed on 16th November 1983. The Claimant has worked in various positions in the Company and in 2005; he was assigned to work in the spray dryer section. On 26th November 2005 the Claimant reported to work on the morning shift at 7.00 am and started to work at the Spray Dryer Section. At about 8.30 am the Claimant's superior, the Production Superintendent came to the spray dryer section and directed the Claimant to do mixing and sieving. The supervisor had been directed to do some other work. A day prior to 26th November 2005, the Production Superintendent had rearranged the work schedule of the Claimant by arranging another worker to take over the duties of the Claimant. A problem arose, when the Claimant refused to comply with the directive given and questioned it.

Held

There is now a respectable line of authority for the proposition that an employee owes a duty to his employer to comply with any lawful direction.

It is generally held that the proper course for an employee is to obey the orders when it is given and protest about its illegality in separate proceedings.

The right to control employees is a distinguishing feature of the contract of employment. The right to control implies the right to ask the employee what work to do.

generally true that willful disobedience of an order will justify summary dismissal, since willful disobedience of a lawful and reasonable order shows a disregard – a complete disregard – of a condition essential to the contract of service, namely, the condition that the servant must obey the proper orders of the master

Decision court in this case:

In conclusion, for the reasons given, it is the finding of the Court that the dismissal is for just cause or excuse.

Order

The claim is hereby dismissed.

Court Award (2)

Lim Kim Hai electric sdn. Bhd. (1984)

The duty to pay remuneration:

This is an appeal against the decision of the assistant commissioner for labor at port kelang. The respondent claimed that he was entitled to overtime payments and payments for work

during public holidays and annual leave on the basis that he was an employee of the appellant, who on the other hand, said that the respondent was an independent contractor. The main issue was whether the relationship between the two was based on a contract of service, or a contract for service.

The respondent and a friend went to look for employment as guards at the appellant's business premises. The appellant was willing to pay them $250,000 per month each. Upon the respondent's friend refusing the appointment, the respondent was offered $500, 00 per month which the respondent accepted. In addition to monthly payment, the respondent also received "ang pows" for Hari Raya Puasa and Chinese New Year. The working hours were fixed. After the appellant moved into new premises, the respondent was required to clock in at every two hours, beginning at 10 p.m. when on leave, the respondent arranged for an employee of the appellant to replace him.

Held

For a contract of service to exist, the following four factors should be present:

The master's power of selection of his servant;

The payment of wages or other remuneration;

The master's right to control the method of doing the work' and

The master's right of suspension or dismissal.

From the facts, there was no doubt that the appellant selected the respondent for employment as a guard. Although it was difficult to conclude positively as to whether the monthly remuneration was wages or security fees, nevertheless it was clear that based on the facts, the appellant had the right to determine what work the respondent had to do, and also how to perform the guard duties not as a person in a business of his own. Thus, he was employed on a contract of service. As for the master's right of suspension or dismissal, the appellant had the right to dismiss the respondent for misconduct during duty hours and also the right to terminate the respondent's services which in fact is dismissal, for industrial misconduct.

4. Unfair dismissal:

dismissial.jpg

4.1 Definition:

Termination of a contract of employment for unfair or inadmissible reasons, When challenged in a court, the employer ought to establish that the dismissal was based on a good reason such as disgusting misconduct, require of qualification, powerlessness to

perform assigned duties, or joblessness. In such cases, the courts frequently take the employee's statutory rights into thought. [6]

4.2 unfair dismissal in the common law:

At common law an employer can legally dismiss an employee by giving him the requisite notice of dismissal. The sacked employee if he be able to show that he has been wrongfully dismissed. The law on unfair dismissal seeks to remedy this situation by giving the employee the right only to be legally dismissed if that dismissal can be exposed to be fair. An unfair dismissal claim is a statutory claim. Claims for unfair dismissal can only be through to the Employment Tribunal.

4.3 What is unfair dismissal:

There are a number of ways your dismissal might be unfair:

your employer does not have a just reason for dismissing you (ex. if there was nothing incorrect with your job performance)

your employer did not comply with a process when dismissing you (ex. if they have not followed their company dismissal processes)

you were dismissed for an automatically unfair reason (ex. since you required to take maternity leave)

4.4 Automatic unjust dismissal

There are a little reasons for dismissal that are automatically unjust, ex. for the reason that of your gender or age. If you are dismissed for any of these reasons then you ought to be able to make a claim to and Employment Tribunal for unfair dismissal.

4.4.1 What is an automatically unjust dismissal?

Definite dismissals are "automatically unjust" in which case the employee just has to be evidence for that the dismissal was for one of the following reasons:

Membership (or non membership) of a trade union or for trade union actions.

Something regarding to health and safety.

Bringing measures against the employer for breach certain statutory employment rights.

Illegal discrimination on basis of race, sex, disability, religion or belief, sexual orientation or age.

Pregnancy or any other reason related with the pregnancy.

looking for to enforce rights in the National Minimum Wage Act

creation a protected disclosure under the screech blowing legislation

Trying to acquire recognition of an independent trade union

Looking for to implement the right to be accompanied at a grievance or disciplinary hearing.

In relation with the employee's rights with refer to parental, paternity or espousal leave, time off for seek after dependants, maternity leave or the right to request to work flexibly.

Taking action in relation with part-time workers' or fixed term workers' rights.

Rejection by a shop worker to work on Sunday.

Related with an employee's purpose as a pension fund trustee.

In break of the Information and Consultation Regulations 2004.

In relation with retirement when the employer has not informed the employee of their right to ask for to continue working; or while the procedure is ongoing

4.5 When is a dismissal fair?

The law provides that is fair for employers to dismiss an employee for one of the subsequent reasons:

A statutory requirement

Misconduct at work

Lack of capability (or qualifications) to do the job

Retirement

Redundancy

Some other substantial reason

Denco v Joinson Ltd (1991):

Mr. Denco was employed as a temporary supervisor on the nightshift at Joinson Ltd. He was also a sop steward. He was summarily dismissed when his employer realised that he had, without authorization accessed the company's computer system. He had gained access to confidential information, including amongst other things, customer lists and salary accounts.

Court held that his dismissal was lawful; he had deliberately used an unauthorized password in order to gain access to information that he knew was confidential. His actions amounted to gross misconduct and Joinson was entitled to summarily dismiss him.

On the other hand, even if the employer convinces a Tribunal that they dismissed their employee for one of those reasons, they still have to be evidence for that they followed a reasonable process as set out in the (Advisory, Conciliation and Arbitration Service) code of conduct. They ought to also show that the decision to dismiss consider as the reasonable responses open to an employer.

Jeffrey v Laurence Scott & Electromotor (1984) :

Mr. Jeffery waited 3 months after his employer's breach before resigning and calming constructive dismissal.

Court held that there had been no constructive dismissal; Jeffrey had resigned. Having waited so long, he was taken to have acquiesced to his employer's actions.

4.6 Unfair dismissal in Malaysia:

The term dismissal in Malaysia legal perspective is in fact creates from termination of employment contract. This is what Ayadurai (1998) make clear; the term 'Termination' in Malaysian Industrial Law regard to the termination of employment relationship, but as this connection is a contractual one, it is recognized with the termination of the employment contract. Where the contract is terminated by the employer because of perceived misconduct of the employee, subsequently the termination is termed as dismissal.

The statutory provisions concerning termination and dismissal stated that it's the management prerogatives. Means that it is the right of the organization to exercise its right, nevertheless it ought to in fulfil with due valid reasons of punitive cases or misconduct and poor work performance.

S. Ahmad (1997) explained that there is no doubt dismissal is the severest punishment which can be awarded to offending employee by his employer for some act of misconduct, however if there is no misconduct, there be able to be no punishment.

5. The ethics of job discrimination:

discrimination.jpg

To discriminate in employment – to make an adverse decision against employees who belong to a certain class because of ethically unfair prejudice towards members of that class.

5.1 Effects of discrimination in the workplace:

Discrimination in the workplace harmfully affects businesses in that discriminatory policies are capable of harm a company's reputation. A business self-limits itself when it confines advancement to certain groups or sorts of employees. Talking negatively regarding a former employee can be harmful for a potential customer. There is also a direct connection between faithfulness, retention, and discrimination. Employees are more likely to be seeking

for new jobs when they sense they have been mistreated. Referring to a report on discrimination at the workplace by the International Labour Organization, “workplace discrimination remains a constant universal problem, with fresh more subtle forms rising.”[1] Sending wrong pointers to potential customers can also cause argument because clients can sense when employees aren’t enthusiastic or don’t trust in their company. This is one reason that it is significant for a job applicant to examine the attitudes of people they hope to work with. Transfer positive signals to employees create a center of attention future potential employees.

Inequality suffers by discriminated groups increase. Outstanding to assenting action policies, a new focal point class has been created that consists of previously discriminated people in some countries but in others, people who are from discriminated groups are normally concerned in the worst jobs, without benefits, public protection, preparation, or credit. Discrimination at a workplace can guide to poverty. “Discrimination creates a web of poverty, forced and child labor and social exclusion.

5.2 Gender discrimination and the workplace:

Albeit there are regulations that are used to encourage fairness within the workplace, discrimination is still out of control. Women still do not determine up to men when it comes to income, employment charge and occupational variety. Women’s average salary is 75 to 87 percent of men’s, also when variables such as education, situation point and job possession are considered. In most countries, the glass maximum is ever present for women and the salary differences are important compared to men. “Discrimination can occur at every stage of employment, from recruitment to education and remuneration, occupational segregation, and at time of layoffs.

R v Birmingham City Council, ex parte Equal Opportunities commission (1989) :

The City Council allocated 390 of 600 available school places to boys and only 210 to girls.

Court held that, this was an example of direct discrimination as the girls would not have received the same treatment had they been boys.

5.3 Unintentional discrimination:

Unintentional discrimination happens when impartial selection practices produce a considerable disparity of conclusion between one group and another. Such perform engage the use of standardized tests in the hiring procedure.

James v Eastleigh Borough Council (1990):

Mr. and Mrs. James both went swimming at their local pool. They were both 61 years of age. Mrs. James was allowed a free swim because she was a pensioner but her husband was

asked to pay 75p because he was not. The council hand not intended to discriminate against male pensioners; it was merely observing the ages at which people received their pension.

Court held that; although the council did not intend to discriminate on the grounds of sex, its actions amounted to direct discrimination. As a man Mr. James had been treated less favourably than he would have been had he been a woman.

Some laws forbid unintentional in addition to intentional discrimination, but might have different principles for deciding what is acceptable. Significant disparities in outcome are not essentially unlawful, if the practices that produce them are necessary.

5.4 Laws on Employment Discrimination in Malaysia:

Until lately, Malaysia had no legislation ruling employment discrimination; even though the Federal Constitution does state that there shall be no discrimination against citizens on the ground of race, religion, place of birth or descent. On September 29, 2002, Article 9(2) of the Federal Constitution was amended to disallow gender discrimination through the Constitution Act 2001.This, nevertheless, has yet to be encapsulated in any exact legislation.

In 2001, the Labor Department of the Malaysian Ministry of Human Resources issued the Code of Practice for the Employment of the Disabled in the Private Sector ("Disability Code").The objectives of the Disability Code are to:

(i) set up guidelines for the registration and job post of the disabled with the private sector;

(ii) Increase the consciousness of private sector employers on the significance of offering employment opportunities to the disabled; and

(iii) Maintain the disabled to arrange themselves in terms of ability, qualifications and skill sets to contribute in the improvement of Malaysia as employees.

While the Disability Code sets out the confident responsibilities of both the employer and the disabled employee, like other similar Codes relating to employment, there are no legal sanctions for non-compliance.

6. Occupational safety and health:

safety.jpg

Occupational health and safety is a cross-disciplinary region referring with protecting the safety, health and interests of people according in work or employment. The aim of all occupational health and safety programs is to promote a safe work environment. As a minor effect, it might also protect family members, co-workers, customers, employers, nearby communities, suppliers and other members of the community who are impacted by the workplace environment. It might engage interactions amongst many subject areas, as well as

occupational medicine, safety engineering, occupational (or industrial) hygiene, public health, health physics, chemistry.

6.1 Reasons for Occupational health and safety:

The occurrence of an incident at work (such as, fines, compensatory damages, lost production, investigation time, legal fees, lost goodwill from the workforce, from the wider community and from customers).

Occupational health and safety officers promote health and safety procedures in an organisation. They recognize hazards and measure health and safety risks, set suitable safety controls in place, and give recommendations on avoiding accidents to management and employees in an organisation.

Baker v Clarke (1992):

An experienced electrician was injured when he did not lock the wheels of mobile scaffolding. He claimed that his employer had not taken care for his safety.

Held the employer was not liable; the employer did not have to provide constant reminders of the risks involved in putting up scaffolding, or the likelihood of harm if it was not accurately.

6.2 OCCUPATIONAL SAFETY AND HEALTH MALAYSIAN ACT:

The Occupational Safety and Health Act is an Act which provides the legislative framework to secure the safety, health and welfare among all Malaysian workforces and to protect others against hazards to safety or health in relation with the activities of persons at work.

This Act was issued on 13th February 1994 and might be cited as the Occupational Safety and Health Act 1994. This Act is a sensible instrument superimposed on existing safety and health legislation.

6.2.1 The aims of this Act are:

to secure the health, welfare and safety of persons at work against risks to safety or health occur out of the activities of persons at work

to care for person at a place of work other than persons at work against risks to safety or health occurring out of the activities of persons at work

to encourage an occupational environment for persons at work which is adapted to their psychological and physiological needs.

Johnstone v Bloomsbury Health Authority (1991):

Johnston, a junior doctor, was employed by the Authority to work 40 hours per week. His contract also stated that he would make himself available to work a further 48 hours each week. He sued the Authority alleging that by requiring him to work an unrealistic number of hours

Topic 4 ▸ Ethics and Business Practice

By the end of this topic, you will be able to:

1. describes the connection between ethics and business;
2. explains the relationship between law and morality;
3. explains morals and ethics;
4. outlines the main theories of ethics;
5. relates how ethics operate in the business context; and
6. outlines some of the issues concerning ethics in corporations.

4.1 ETHICS AND BUSINESS

- acting ethically involves acting in a morally correct and honourable way
- the belief that 'making profits is all that matters' and 'as long as it is legal it is all right' are gradually being forced aside
- ethical business conduct may impose a cost on business, that cost may be offset by an increase in public confidence
- the community is now well aware of business matters and their consequences, especially those consequences which have an impact on individual members of the community – e.g. American subprime mortgage crisis in September 2008 has now resulted in a global financial crisis
- if businesses do not adopt acceptable ethical standards then Parliament will need to step in to impose standards

4.2 LAW AND MORALITY

- laws are relative to their time and their society
- what is perceived as appropriate in one time period may not be appropriate to another
- likewise, the law reflects the attitudes of the society in which it exists and, therefore, what is deemed acceptable in one society may not be acceptable in another
- moreover, social attitudes may change over time resulting in a corresponding change in the law

What is 'Law'?

- a set of rules, developed over a long period of time to regulate interactions between people; it sets standards of conduct between one group of individuals and another as well as between individuals and the government, which are enforceable through sanction
- law sets standards of conduct
- ethics cannot be enforced though sanction unless the ethical standards have become part of the law or the rules of an organization such as a professional body

'Justice' and the 'Law'

- justice – that which is right or fair

The Rule of Law

- every person and organization, including the government, is subject to the same laws
- its most basic principle – no one is above the law
- governmental authority is legitimately exercised only in accordance with written, publicly disclosed laws adopted and enforced in accordance with established procedural steps that are referred to as due process
- according to Dicey, 3 principles which together establish the rule of law are:
    - The absolute supremacy or predominance of regular law as opposed to the influence of arbitrary power
    - Equality before the law or the equal subjection of all classes to the ordinary law of the land administered by the ordinary courts
    - The law of the constitution is a consequence of the rights of individuals as defined and enforced by the courts
- the legal basis of government gives rise to the principle of legality, with the rule of law being expressed as follows:
    - Existence or non-existence of a power or duty is a matter of law and not of fact, and so must be determined by reference either to the nature of the legal personality of the body in question and the capacities that go with it, or to some enactment or reported case
    - The argument of state necessity is not sufficient to establish the existence of a power or duty which would entitle a public body to act in a way that interferes with the rights or liberties of individuals
    - If effect is to be given to the doctrine that the existence or non-existence of a power or duty is a matter of law, it should be possible for the courts to determine whether or not a particular power or duty exists, to define its ambit and provide an effective remedy for unlawful action
    - Since the principal elements of the structure of the machinery of government, and the powers and duties which belong to its several parts, are defined by law, its form and course can be altered only by a change of law
- the concept “rule of law” is associated with other concepts:

- *Nullum crimen, nulla poena sine praevia lege poenali* There should be no *ex post facto* laws.
- Presumption of innocence
  All individuals are "presumed innocent until proven otherwise."
- Legal equality
  All individuals are given the same rights without distinction to their social stature, religion, political opinions, etc.
- *Habeas corpus ad subjiciendum*
  "You must have *the* body to be subjected (to examination)".

- in examining the concept of the rule of law, one should consider:
  - whether judges are entitled to make law
  - whether that is the exclusive prerogative of parliament
- for the rule of law to thrive, the legal system needs the following characteristics:
  - Laws are relatively clear, accessible and prospective in their operation
  - Laws are seen to be legitimate and enjoy a broad measure of community support
    1. This legitimacy and support usually derives from the laws being considered to be generally just
    2. Laws are interpreted and applied openly by an independent judiciary which itself enjoys a broad measure of community acceptance
- Professor A.V. Dicey – rule of law comprised 3 inter-linked ideas:
  1. The supremacy of regular law rather than arbitrary power
  2. Government under the law and equality before the law
  3. The protection of individual liberties by the common law
- our efforts to strengthen legal systems should fall under 3 inter-connected priority areas:
  1. Supporting legal reform
  2. Improving the administration of justice
  3. Increasing citizens' access to justice

The Development of Equity

- concept of equity arose as a result of the growing inflexibility and rigidity of the common law
- strict rules of common law be modified in appropriate circumstances

Letter of the Law and Spirit of the Law

- the strict wording of a law (the letter of the law) may allow an individual to do something which is not really in accordance with the intentions (spirit) of the law
- the distinction between the letter and the spirit of the law is largely a moral or ethical problem

4.3 MORALS AND ETHICS

- morals – to deal with the distinction between right and wrong
- ethics – relate to morals, the treatment of moral questions and acting in a morally correct and honourable way
- ethical considerations involve going beyond self-interest in reaching a decision

4.4 THEORIES OF ETHICS

Consequentialism and Utilitarianism

- Consequentialism
  - concerned with the consequences
  - an approach to morals which evaluates behaviour according to the consequences of that behaviour
- Utilitarianism
  - a form of consequentialism
  - ethically right behaviour is to perform the action which results in a greater number of utilities than could be achieved by any other action

Deontological Ethics

- requires a person to do the right thing regardless of the consequences

- at odds with consequentialism ethics in that it considers that the consequences can never be an appropriate justification for the act
  - the end does not in itself justify the means

Virtue Ethics

- personal qualities that provide the basis for an individual to lead a good and noble life
- stresses on the type of moral qualities that put us in a position to act morally

Relativism

- moral values are relative to a particular environment
- moral values can differ from one culture to another, from one society to another, from one time to another, and even from one individual to another

4.5 ETHICS IN THE BUSINESS CONTEXT

Insider Trading

- an example of a white-collar crime
- part V, Division 1 subdivision 2 (sections 183 to 198), Capital Markets & Services Act 2007 prohibits insider trading

Giving and Receiving Gifts

- unethical and illegal if the nature of the gift is not nominal in value and where the gift is given as an inducement or in return for a favour, or if it is given under illegal circumstances
  - see: section 115, Banking and Financial Institutions Act 1989; sections 10–18, Anti-Corruption Act 1997; section 118, Development Financial Institutions Act 2002; section 49, Islamic Banking Act 1983; sections 161–165, Penal Code

Conflict between Commercial Interests and Social Utility

  - banks, telecommunications suppliers, private hospitals and other health service providers and the media are business organizations which are not only profit-oriented but also provide a social utility and must bear in mind the community's needs

Conflict of Interest

- arises when an individual is in a position where they cannot act fairly and properly in the interests of one party without prejudicing the rights and interests of another party for whom they also act

Unconscionable Contracts

- relative bargaining power may be very unequal – one party may be virtually helpless and unable to negotiate anything, and the extent of their negotiating position may be a 'take it or leave it' situation, as is often the case where standard form contracts are involved

Misuse of Limited Liability of a Company

- under the doctrine of separate legal entity, a company is regarded as a legal person, separate and distinct from its shareholders and directors
- the doctrine has often been abused with the result that creditors and employees have lost considerable amounts of money while the principals of the company have effectively lost nothing

Tax Evasion and Tax Havens

- try to eliminate tax totally by using certain tax-avoidance schemes and overseas tax havens
- many methods of tax avoidance are both ethically wrong and even illegal
- certain ways employed to minimize tax is legal when done so in compliance with the law

4.6 CORPORATIONS AND ETHICS

- companies are required to be ethical in their dealings
- company directors have a fiduciary duty to act in the interests of their company and the best interests of the company's shareholders
- businesses require good corporate governance by their directors and generally, directors must be 'fit and proper' persons to act as directors

Institutionalized Wrongdoing

- social forces within an organization may result in unethical behaviour or even illegal actions by an individual – fraud

Organizational Integrity

- organizational integrity is based on self-regulation in accordance with a formal set of guiding principles
- ethical values will be involved in the establishment of organizational systems, the decision-making process and the search for business opportunities
- integrity programmes often comprise:
  - a code of conduct
  - training in compliance with legal and regulatory obligations of the organization
  - systems for the reporting and investigation of possible breaches
  - a system of controls and audits to ensure that the integrity programme is being complied with
- Corporate Codes of Conduct
  - to fight corporate fraud and abuse by:
    a) exposing and punishing acts of corruption
    b) holding corporate officers and directors accountable
    c) protecting small investors, pension holders and workers
    d) moving corporate accounting out of the shadows
    e) developing a stronger, more independent corporate audit system
    f) providing better information to investors

4.7 ETHICAL INVESTING

- means investing in companies that operate ethically, provide social benefits and are sensitive to the environment
- a socially-responsible investor considers whether or not the investment is ethical aside from adequate returns and security
- this means judging or analysing a company or institution primarily on its products and/or services as well as socially responsible governance practices
- to determine which company to invest in, or not invest in, investors must consider whether the company is associated with, or linked to:

- Positive factors:
  - Environment protection
  - Pollution control
  - Conservation of resources
  - Health and safety of the workplace and the community
  - Ethical employment policies
- Negative factors:
  - Armaments
  - Terrorism
  - Money laundering
  - Oppressive regimes
  - Environmentally damaging practices
  - Unethical employment practices
  - Animal exploitation
  - Tobacco or alcohol
  - Gambling
  - Pornography and other vices

4.8 ETHICAL PROFESSIONAL ADVICE

- professional advisers sometimes stretch the legal system to the limit to avoid culpability for their unethical activities – see *McCabe* v *British American Tobacco Australia Services Ltd*
- 'just because it is legal does not make it right'
- during the global financial crisis of 2008:
  - many investors and employees have suffered the consequences of numerous financial scandals
  - a more widespread erosion of standards throughout our markets, with questionable practices becoming accepted

- there has been a global recognition of the need for reforms. Through multilateral co-operation, standards can be raised throughout our markets, and investors everywhere have the protections they need and deserve