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Assignment and Negotiability

Assignment and negotiable instruments

THE benefit of a contract may, in certain circumstances, be transferred to a third party. In this chapter we shall consider the subject of assignment, that is to say, the transfer of contractual rights to a third party without the concurrence of the other party to the contract, and the transfer of contractual liabilities. We shall also consider the nature of negotiable instruments.

I. Assignment of Contractual Rights[1]

Assignment of rights

A PARTY to a contract (the assignor) may, as a general rule, assign its rights under the contract to a third party (the assignee) without the consent of the party (the debtor) against whom those rights are held.

(a) No Assignment at Common Law

No assignment of benefit at common law

At common law the benefit of a contract could not be assigned so as to enable the assignee to bring an action upon it in its own name. This rule was sometimes expressed by the phrase 'a chose in action is not assignable'.

' "Choses in action" is a known legal expression used to describe all personal rights of property which can only be claimed or enforced by action, and not by taking physical possession.'[2] The contrasted term is 'chose in possession'. The definition of a chose in action thus includes not only contractual rights but many rights which are not contractual, e.g. patent rights, copyrights, rights of action in tort. We are concerned here, however, only with the assignment of contractual rights.

Exceptions and some transfer possible

The only exceptions allowed by the common law were assignments by or to the Crown[3] and assignments by holders of negotiable instruments permitted by the law merchant. The reason for the non-recognition of assignments of choses in action seems to have been that the common law judges feared that to permit assignments would both undermine the doctrine of privity of contract and encourage maintenance and unnecessary litigation.[4] But even at common law it

[1] For a more detailed study, see Marshall's *Assignment of Choses in Action* (1950).
[2] *Torkington* v. *Magee* [1902] 2 K.B. 427, *per* Channell J. at p. 430; rev'd. [1903] 1 K.B. 644.
[3] *Master* v. *Miller* (1791) 4 Term Rep. 320, at p. 340.
[4] *Lampert's Case* (1612) 10 Co. Rep. 46b, at 48a; *Fitzroy* v. *Cave* [1905] 2 K.B. 364, at p. 372.

was (and still is) possible for the right to sue on a contract to be conferred on a third party by other means.

In the first place, the contracting party could give to the third party a power of attorney and thus enable the third party to sue the debtor as the contracting party's representative.[5]

Secondly, the contracting party could allow the third party to sue the debtor in the contracting party's name, taking from the third party an indemnity against costs; but he could not be compelled to do this.

Thirdly, with the consent and co-operation of the debtor, the contracting party could effect a transfer by means of a substituted agreement, or 'novation', as follows:

> If A plc owes M Ltd £100, and M owes X £100, it may be agreed between all three that A shall pay X instead of M, which thus terminates its legal relationship with either party. In such a case the consideration for A's promise to pay X is the discharge by X of M's debt; for M's discharge of A, the promise of A to pay X; for X's discharge of M, the discharge by M of A's debt to M.

But a mere written authority from the creditor to the debtor (i.e. from M to A) to pay the amount of the debt over to a third party, even though the debtor acknowledged in writing the authority given, did not entitle the third party to sue for the amount unless the third party had furnished consideration by an express promise to release the creditor from the debt.[6]

These methods were, however, cumbrous and unsatisfactory, and from a fairly early period equity was prepared to recognize an assignment of a chose in action and to allow an assignee to invoke its aid.[7]

(b) Assignment in Equity

Benefit assignable in equity

Equity would permit the assignment of a chose in action, including debts and other contractual rights, whether such chose was equitable or legal.

(i) Equitable choses

An *equitable* chose is one which, before 1875, could only be enforced in the Court of Chancery, such as a share in a trust fund, a legacy, or a reversionary interest under a will. Where there was an assignment of an equitable chose, the assignee was allowed to proceed in its own name, and only an assignor who had an interest in the action had to be made a party to it.[8] The reason for this was that since there was no claim that might be asserted by an action at law, the Court of Chancery had exclusive jurisdiction over the whole transaction; there was therefore no risk that the trustees of the fund (i.e. the debtors) would be exposed to a second action at law by the assignor.

[5] *Re Bowden* [1936] Ch. 71, at p. 74.

[6] *Liversidge* v. *Broadbent* (1859) 4 H. & N. 603. But cf. *Walker* v. *Rostron* (1842) 9 M. & W. 411 and *Shamia* v. *Joory* [1958] 1 Q.B. 448.

[7] For a history of assignment, see Bailey (1931) 47 L.Q.R. 516; (1932) 48 L.Q.R. 248, 547.

[8] *Goodson* v. *Ellisson* (1827) 3 Russ. 583; *Cator* v. *Croydon Canal Co.* (1841) 4 Y. & C. Ex. 593; *Donaldson* v. *Donaldson* (1854) Kay 711.

(ii) Legal choses

A *legal* chose in action is one which, before 1875, could be enforced by an action at law, for example, a right under a contract, a debt, or a claim under a policy of insurance. Equity would recognize the assignment of a legal chose in action, but had here to proceed more carefully. If equity itself enforced the claim of the assignee, that would not prevent the assignor from bringing an action at law; and the debtor would have been put to the inconvenience of resorting to equity to restrain the assignor from enforcing the judgment on the ground that the assignee had already recovered in equity. Consequently the Court of Chancery did not in the ordinary case enforce the assignee's claim. What it did was to infer from the assignment a duty on the assignor to exercise the right for the benefit of the assignee. On receiving a proper indemnity against costs, the assignor's duty was to permit the assignee to use the assignor's name so that the assignee might bring an action at law. If necessary, it would enforce this duty.[9] So whenever a legal chose in action was assigned in equity—and it could not be assigned otherwise—the action in a Court of law was brought in the assignor's name.[10] This was primarily in the interests of the party liable, so that one action should bind both the legal and equitable title to the chose; and partly in the interests of the assignor, who might dispute the assignment if he thought fit.

Since the Judicature Act 1873 an assignment in equity will be recognized by all divisions of the High Courts of Justice, whether it be of a legal or equitable chose in action. But the rules relating to such assignments (including the use of the assignor's name) are based on those in operation before the passing of the Act. We shall examine these rules in detail later, but it is first necessary to note that section 25(6) of the Judicature Act (now replaced by section 136 of the Law of Property Act 1925) has introduced a form of statutory assignment which takes effect *at law*.

(c) Statutory Assignments

Law of Property Act 1925, s. 136

By section 136 of the Law of Property Act 1925:

> Any absolute assignment by writing under the hand of the assignor (not purporting to be by way of charge only) of any debt or other legal thing in action, of which express notice in writing has been given to the debtor, trustee or other person from whom the assignor would have been able to claim such debt or thing in action, is effectual in law (subject to equities having priority over the right of the assignee) to pass and transfer from the date of such notice—
>
> (a) the legal right to such debt or thing in action;
> (b) all legal and other remedies for the same; and
> (c) the power to give a good discharge for the same without the concurrence of the assignor.

[9] *Hammond* v. *Messenger* (1838) 9 Sim. 327.

[10] See, however, the statement of practice by Buller J. in *Master* v. *Miller* (1791) 4 Term Rep. 320, at p. 341, which shows that a Court of law did not always insist on the rule.

Words of section

The effect of this section, provided the conditions laid down in it are fulfilled, is to give to the assignee a legal title to the debt or right assigned.[11] The assignee is thus enabled to sue in its own name.[12] It is necessary to examine the words of the section in some detail.

(i) 'Assignment'

Equitable assignments unimpaired

The section does not touch the rules of assignment in equity so that equitable assignments remain unimpaired,[13] nor does it make assignable contracts which were not assignable in equity before:

> This sub-section is merely machinery; it enables an action to be brought by the assignee in his own name in cases where previously he would have sued in the assignor's name, but only where he could so sue.[14]

(ii) 'Absolute'

Statutory assignments must be absolute

The Act requires the assignment to be 'absolute' and not 'by way of charge'. This means that it must be an assignment of a sum due or about to become due, not of an amount which is dependent on any question as to the state of accounts between assignor and assignee.

and not conditional

The assignment must not be subject to any condition. So, if it is to take effect or to cease upon the happening of a future uncertain event, so that the original debtor is uncertain as to the person in whom the right to receive the money is vested, it is not absolute. Thus in *Durham Brothers* v. *Robertson*:[15]

> A building contractor wrote to the plaintiffs in the following terms: '*Re* Building Contract, South Lambert Road. In consideration of money advanced from time to time we hereby charge the sum of £1,080, being the price . . . due to us from [the defendant] on the completion of the above buildings as security for advances, and we hereby assign our interest in the above-mentioned sum until the money with added interest be repaid to you'.

It was held that the assignment was not within the section. It did not transfer the whole debt to the plaintiffs unconditionally, but only until the advances were repaid. The defendant could not be sure that he was paying his debt to the right person without knowing the state of accounts between the assignor and assignee. But an assignment which passes the entire interest of the assignor in the debt may still be absolute despite the fact that it contains a proviso for redemption and reassignment on repayment.[16] The assignment is subject to a condition, but it cannot prejudice the debtor, who will receive notice first of the assignment, and then of the reassignment, if one is made. The debtor will always know to whom the debt

[11] *Warner Bros. Records Inc.* v. *Rollgreen Ltd.* [1976] Q.B. 430.

[12] Subject to the right of a debtor who receives notice of a disputed assignment to call upon the persons giving notice to interplead.

[13] *Brandt's Sons & Co.* v. *Dunlop Rubber Co. Ltd.* [1905] A.C. 454, at p. 461.

[14] *Torkington* v. *Magee* [1902] 2 K.B. 427, *per* Channell J. at p. 435; *Marchant* v. *Morton, Down & Co.* [1901] 2 K.B. 829, at p. 832.

[15] [1898] 1 Q.B. 765. See also *Herkules Piling Ltd.* v. *Tilbury Construction Ltd.* (1992) 61 B.L.R. 107, at p. 117.

[16] *Tancred* v. *Delagoa Bay and East Africa Ry.* (1889) 23 Q.B.D. 239.

is owed. There may, too, be an absolute assignment of a debt arising out of an existing contract, even though it does not become payable until a date later than the assignment.[17]

or by way of charge

The assignment must also not purport to be by way of charge. An assignment by way of charge is one which merely gives a right to payment out of a particular fund, and does not transfer the fund to the assignee. A good illustration is furnished by *Jones* v. *Humphreys*:[18]

> A schoolmaster, in consideration of a loan to him of £15, assigned to the plaintiff so much and such part of his income, salary and other emoluments from his employers as should be necessary and requisite for repayment of the sum borrowed (with interest) or of any further or other sums in which he might thereafter become indebted to the plaintiff.

It was held that this was not an absolute assignment, but was a mere security purporting to be by way of a charge. Even the assignment of a definite part of an existing debt, for example part of a sum deposited in a bank account,[19] is not absolute, but merely a charge upon the whole debt;[20] for otherwise it would be in the power of the original creditor 'to split up the single legal cause of action for the debt into as many separate legal causes of action as he might think fit',[21] thus obviously prejudicing the position of the debtor. But any of these assignments, though not absolute, and therefore outside the section, may still be perfectly good as equitable assignments.

(iii) 'Writing'

Assignment must be in writing

The assignment must be in writing and signed by the assignor; signature by an agent may be insufficient.

(iv) 'Notice'

Need for express notice

The Act requires that express notice in writing should be given to the debtor or trustee. This requirement is peremptory, so that in a case where the debtor was unable to read and it was therefore thought useless to give him written notice, though the assignment was read over to him and understood by him, there was held to be no legal assignment.[22] The written notice, however, need not be in any particular form, provided that it sufficiently indicates the fact of the assignment.[23] The notice takes effect when it is received by the debtor.[24]

[17] *G. & T. Earle Ltd.* v. *Hemsworth R.D.C.* (1928) 44 T.L.R. 758; *Care S.S. Cpn.* v. *Latin American S.S. Cpn.* [1983] Q.B. 1005.
[18] [1902] 1 K.B. 10. See also *Court Line Ltd.* v. *Akt. Gotaverken* [1984] 1 Lloyd's Rep. 283.
[19] *Deposit Protection Board* v. *Dalia* [1994] 2 A.C. 367.
[20] *Williams* v. *Atlantic Assurance Co.* [1933] 1 K.B. 81.
[21] *Durham Brothers* v. *Robertson* [1898] 1 Q.B. 765, *per* Chitty L.J. at p. 774; *Forster* v. *Baker* [1910] 2 K.B. 636. See Hall [1959] C.L.J. 99.
[22] *Hockley* v. *Goldstein* (1922) 90 L.K.J.B. 111.
[23] *Denny, Gasquet & Metcalfe* v. *Conklin* [1913] 3 K.B. 177.
[24] *Holt* v. *Heatherfield Trust Ltd.* [1942] 2 K.B. 1.

(v) Consideration

Consideration not required

An assignment under the Act does not require the assignee to have furnished consideration in order to make it valid as between assignor and assignee or to enable the assignee to sue in its own name.[25]

(vi) Rights assignable

Extent of statute

The Act refers to 'any debt or other legal thing in action'. The meaning of this expression has been considered in several cases.[26] It is not, as might appear at first sight, confined to legal choses in action, which were enforceable only in a Court of Common Law, but extends to choses in equity as well.[27] In *Torkington* v. *Magee*,[28] Channell J. said:

> I think the words 'debt or other legal chose in action' mean 'debt or right which the common law looks on as not assignable by reason of its being a chose in action, but which a Court of Equity deals with as being assignable'.

A 'legal thing in action' may therefore be defined as any right the assignment of which a Court of law or equity would, before the Judicature Act, have recognized or enforced.

Further statutory exceptions

Statute has also created further exceptions to the rule that there can be no assignment at law. For example, by the Policies of Assurance Act 1867[29] and by the Marine Insurance Act 1906,[30] policies of life and marine insurance can be assigned, but the former Act requires notice to be given by the assignee to the insurance company. Stock and shares in a company are transferable under the provisions of the Companies Act 1985[31] and the Stock Transfer Act 1963, and assignments of patents and copyright are regulated by the Patents Act 1977[32] and the Copyright, Designs and Patents Act 1988.[33]

(d) Equitable Assignments

Assignment in Equity

An assignment which does not comply with one or more of the requirements of section 136 of the Law of Property Act 1925 may still be a perfectly good and valid equitable assignment. 'The statute does not forbid or destroy equitable assignments or impair their efficacy in the slightest degree.'[34] But whereas a statutory assignee acquires a legal title to the chose assigned, an assignee in equity does not do so.[35] Thus a statutory assignee is entitled to bring an action without the necessity of joining the assignor as a party to the action, but an assignee in equity will not always enjoy this right.

[25] *Re Westerton* [1919] 2 Ch. 104.
[26] *King* v. *Victoria Insurance Co. Ltd.* [1896] A.C. 250; *Re Pain* [1919] 1 Ch. 38; *Investors Compensation Scheme* v. *West Bromwich B.S., The Times*, 24 June 1997 (H.L.).
[27] *Re Pain* (*supra*, n. 26).
[28] [1902] 2 K.B. 427, at p. 430; reversed on other grounds [1903] 1 K.B. 644.
[29] s. 1.
[30] s. 50(2).
[31] s. 182.
[32] ss. 90, Sched. 1, paras. 25–9.
[33] ss. 90, 94.
[34] *Brandt's Sons & Co.* v. *Dunlop Rubber Co. Ltd.* [1905] A.C. 454, *per* Lord Macnaghten at p. 461.
[35] *Warner Bros. Records Inc.* v. *Rollgreen Ltd.* [1976] Q.B. 430.

(i) Joinder of the assignor

Can assignee sue in own name?

If the chose in action is *equitable*, the assignee is normally entitled to sue without joining the assignor as a party. The exception is where the assignor still has some interest in the suit. This may arise where there is still some question of accounts outstanding between the assignor and the assignee, or where the assignment consists of a charge upon a trust fund. In such a case the parties interested must be made parties to the action so that the court may make a final adjudication binding them all.

If the chose in action is *legal*, the assignee cannot recover damages or other relief without joining the assignor as a party to the action, if the assignor is willing as co-plaintiff, if not, as co-defendant.[36] Moreover the *assignor* of part of a debt cannot recover the balance in excess of the sum assigned without joining the assignee.[37] Attempts have been made to justify these requirements on the ground that they serve to protect the debtor who might otherwise pay the debt to the wrong person,[38] and that they allow an assignor who wishes to dispute the assignment to do so.[39] But the first of these reasons is only relevant where the assignor retains an interest in the chose, and the second would apply even in the case of a statutory assignment, where the assignee is entitled to sue alone. The rule that an assignor of a legal chose must always be joined as a party seems to be a procedural consequence of the fact that the legal title to the chose assigned does not pass to the assignee, but only an equitable right, the legal title remaining vested in the assignor.[40]

(ii) Form

Informal nature of equitable assignments

No particular form is necessary for an equitable assignment, and, except where the interest assigned is an equitable interest or trust within section 53 of the Law of Property Act 1925,[41] it need not even be in writing. It may be addressed to the debtor or to the assignee. If it is addressed to the debtor:

> It may be couched in the language of command. It may be a courteous request. It may assume the form of mere permission. The language is immaterial if the meaning is plain. All that is necessary is that the debtor should be given to understand that the debt has been made over by the creditor to some third person.[42]

[36] *Durham Brothers* v. *Robertson* [1898] 1 Q.B. 765, at p. 769; *Performing Right Society Ltd.* v. *London Theatre of Varieties Ltd.* [1924] A.C. 1; *Williams* v. *Atlantic Assurance Co.* [1933] 1 K.B. 81; *Central Insurance Co. Ltd.* v. *Seacalf S.S. Cpn.* [1983] 2 Lloyd's Rep. 25; *Weddell* v. *J. A. Pearce & Major* [1988] Ch. 26; *Three Rivers D.C.* v. *Bank of England* [1996] Q.B. 292. Cf. *Brandt's Sons & Co.* v. *Dunlop Rubber Co. Ltd.* (*supra*, n. 34), at p. 464.

[37] *Walter & Sullivan Ltd.* v. *J. Murphy & Sons Ltd.* [1955] 1 Q.B. 584.

[38] *Ibid.*, *per* Parker L.J. at p. 588.

[39] *Durham Brothers* v. *Robertson* (*supra*, n. 36), *per* Chitty L.J. at p. 770.

[40] *Warner Bros. Records Inc.* v. *Rollgreen Ltd.* [1976] Q.B. 430; *Three Rivers D.C.* v. *Bank of England* [1996] Q.B. 292.

[41] *Grey* v. *I.R.C.* [1960] A.C. 1; *Oughtred* v. *I.R.C.* [1960] A.C. 206; *Neville* v. *Wilson* [1997] Ch. 144. Cf. *Vandervell* v. *I.R.C.* [1967] 2 A.C. 291.

[42] *Brandt's Sons & Co.* v. *Dunlop Rubber Co. Ltd.* [1905] A.C. 454, *per* Lord Macnaghten at p. 462. But the assignment must either have been made by prior arrangement with, or be communicated to, the assignee: *Re Hamilton* (1921) 124 L.T. 737.

In *Thomas* v. *Harris*,[43] it was addressed to the assignee:

A father handed to his son certain insurance policies on his life with the request that the son should erect a tombstone in his memory, using the policy monies for this purpose. No notice was given to the insurance company.

It was held that, by this informal act, the father had assigned the policies to his son by way of charge for the cost of the tombstone. There was a valid equitable assignment.

(iii) Notice

Advisability of notice

No notice to the debtor is necessary; the assignment is effective as between assignor and assignee from the moment it is made.[44] Notice is nevertheless *advisable* for several reasons. In the first place, the assignment will not bind the debtor until notice has been received, not necessarily in writing, of the assignment. So, if, before notice, the debtor pays the assignor, that is a good discharge of the debt[45] but if the debtor pays the assignor after notice that is no answer to a claim by the assignee.[46] Accordingly, to constitute notice a communication to the debtor should make it clear that thereafter payment should not be made to the assignor and should generally be by the assignee.[47] Secondly, notice to the debtor or trustee is necessary to establish priority under the rule in *Dearle* v. *Hall*, which we shall deal with later.[48] Thirdly, notice to the debtor will prevent the debtor from setting up new equities which may mature after the receipt of the notice.

(iv) Consideration

Is consideration necessary?

The question whether, as between assignor and assignee, consideration is necessary in an equitable assignment is a difficult one.[49] Equity will not assist a volunteer, and it has been said that 'for every equitable assignment . . . there must be consideration. If there be no consideration, there can be no equitable assignment'.[50] This statement is, however, much too wide, and it is by no means true to say that value is required in every case.

Valuable consideration for this purpose may consist in any consideration sufficient to support a simple contract, or an antecedent debt or liability.[51] Thus if A assigns to B the benefit of a contract in satisfaction of a debt owed by A to B, this is good consideration for the assignment. Similarly if the assignment is by way of security for an existing debt in such circumstances that a forbearance to sue will

[43] [1947] 1 All E.R. 444.

[44] *Brandt's Sons & Co.* v. *Dunlop Rubber Co. Ltd.* (*supra*, n. 42), at p. 462.

[45] *Stocks* v. *Dobson* (1853) 4 De G.M. & G. 15.

[46] *Deposit Protection Board* v. *Dalia* [1994] 2 A.C. 367, at p. 387 (C.A.), rev'd. on other grounds, *ibid.*

[47] *Herkules Piling Ltd.* v. *Tilbury Construction Ltd.* (1992) 61 B.L.R. 107, at p. 119 (or possibly by the assignor, if acting on the assignee's behalf).

[48] *Post*, p. 458.

[49] For a discussion of this subject see Megarry (1943) 59 L.Q.R. 58; Hollond (1943) 59 L.Q.R. 129; Sheridan (1955) 33 Can. Bar Rev. 284; Hall [1959] C.L.J. 99; Marshall, *The Assignment of Choses in Action* (1950), p. 109.

[50] *Glegg* v. *Bromley* [1912] 3 K.B. 474, *per* Parker J. at p. 491.

[51] *Currie* v. *Misa* (1875) L.R. 10 Ex. 153; *Leask* v. *Scott* (1877) 2 Q.B.D. 376; (1943) 59 L.Q.R. 208.

be implied on the part of the assignee, this is sufficient to give the assignee a right to sue the debtor.[52] If consideration has been furnished by the assignee, no problem will arise; it is where the assignment is voluntary that some doubt exists.

Agreements to assign

It is well established that a mere *agreement* to assign a chose in action must, like other contracts, have consideration to support it; if it is voluntary, it is unenforceable.[53] An assignment of a future chose in action also requires consideration.[54] A future chose in action is a mere expectancy which may or may not materialize, such as a share of a trust fund, which will be received only if an uncertain event occurs,[55] damages in an action which is still pending,[56] or the right to payments falling due under contracts not yet made.[57] Such an assignment can only operate as a contract to assign when the subject-matter comes into existence, for 'nothing passes even in equity until the property comes into present existence';[58] it is therefore unenforceable unless value has been given.

Gratuitous assignment

But just as it is possible to make a gift of a chattel, so also it is possible to make a gift of (i.e. to transfer without consideration) a chose in action, provided that the transfer is effected in whatever manner is necessary for a transfer of that particular chose. Such a transfer, however, must, as it is said, be 'complete and perfect', for if anything remains to be done by the donor in order to give effect to the donor's intention, the gift will fail. Equity will not intervene to perfect an imperfect gift. This principle is similar to that enunciated by Turner L.J. in *Milroy* v. *Lord*[59] in relation to voluntary settlements:

> In order to render a voluntary settlement valid and effectual, the settlor must have done everything, which according to the nature of the property comprised in the settlement, was necessary to be done in order to transfer the property and render the settlement binding upon him.

The question of consideration in equitable assignments turns, therefore, on whether any act remains to be done by the assignor in order to perfect the assignment; the assignor must have made every effort to complete the transaction.[60]

of an equitable chose

If the subject-matter assigned is an equitable chose in action, the assignment is complete when the assignor has unequivocally, even though informally, expressed an intention that the chose should henceforth belong to the assignee.[61] The assignee is then, as we have seen, in a position to enforce the right to the chose without more ado: 'such an assignment without any valuable consideration is not

[52] *Glegg* v. *Bromley* (*supra*, n. 50).
[53] *Re McArdle* [1951] Ch. 669.
[54] *Tailby* v. *Official Receiver* (1888) 13 App. Cas. 523.
[55] *Re Ellenborough* [1903] 1 Ch. 697. See also *Norman* v. *Federal Commissioner of Taxation* (1963) 109 C.L.R. 9 (future interest and dividends).
[56] *Glegg* v. *Bromley* (*supra*, n. 50).
[57] *E. Pfeiffer Weinkellerei-Weineinkauf GmbH & Co.* v. *Arbuthnot Factors Ltd.* [1988] 1 W.L.R. 150; *Annangel Glory Comp. Nav. S.A.* v. *M. Golodetz, Middle East Marketing Cpn. Ltd.* [1988] 1 Lloyd's Rep. 45.
[58] *Ibid.*, *per* Parker J. at p. 490.
[59] (1862) 4 De G.F. & J. 264, at p. 274.
[60] *Fortescue* v. *Barnett* (1834) 3 My. & K. 36; (1943) 59 L.Q.R. 58, at pp. 61, 129; [1959] C.L.J. 99.
[61] *Voyle* v. *Hughes* (1954) 2 Sm. & G. 18; *Re Wale* [1956] 1 W.L.R. 1346; cf. *Re Lucan (Earl of)* (1890) 45 Ch. D. 470 where an assignment which failed to create a complete and perfect charge on a reversionary interest was held to be unenforceable for want of consideration.

of a legal chose

a mere agreement but is an actual transfer of the equitable right'.[62] But if the subject of the assignment is a legal chose in action, can a merely equitable assignment of it be said to be complete and perfect? That is the question on which the law is still not altogether clear.

One difficulty of so regarding the transaction is that it leaves the legal title to the chose transferred still outstanding in the assignor. In Australia it has now been settled that, even if the assignment is one which is capable of being a statutory assignment, it does not have to be made in the statutory form, and that the assignor has done everything which is necessary to transfer the legal title to the assignee when the assignor has done those things which it and only it could do.[63] Although the matter has not been settled, it is submitted that this would also be the position in England: the law does not require the assignment of a chose in action to be made only in the statutory form[64] since it continues to recognize the validity of equitable assignments. Furthermore, as we have seen,[65] it is not now necessary for the assignee to ask the Court to compel the assignor to join as co-plaintiff, for an unwilling assignor can be made a defendant. In the result, an equitable assignee of a legal chose in action is now able to enforce the rights under the contract against the debtor without seeking the aid either of the assignor or of the Court, and there seems no reason why the assignment should not be regarded as complete and perfect without consideration.[66] There may, of course, be other reasons why a particular equitable assignment is not complete and perfect, e.g. because the assignor fails to complete the transfer of shares or stock in the sole recognized form,[67] or because the necessary consent of a third party to the transfer has not been obtained.[68] But the better view is that, as between assignor and assignee, an equitable assignment of an existing chose in action, whether legal or equitable, is not rendered ineffective merely because it is voluntary.

(e) Title of Assignee

Assignee takes subject to equities

Whether the assignment of a chose in action is legal or equitable, the assignee takes 'subject to equities', that is, subject to all such defences as might have prevailed against the assignor. 'The general rule, both at Law and in Equity, is that no person can acquire title to a chose in action . . . from one who has himself no title to it.'[69] An assignee of contractual rights must therefore take care to ascertain the exact nature and extent of those rights; for no more than the assignor has to

[62] *Voyle* v. *Hughes* (*supra*, n. 61), at p. 30; *Letts* v. *I.R.C.* [1957] 1 W.L.R. 201.

[63] *Corin* v. *Patton* (1990) 169 C.L.R. 540 (High Court of Australia). Cf. *Olsson* v. *Dyson* (1969) 120 C.L.R. 365.

[64] Cf. *Milroy* v. *Lord* (*infra*, n. 67).

[65] *Ante*, p. 453.

[66] *Holt* v. *Heatherfield Trust Ltd.* [1942] 2 K.B. 1; *Harding* v. *Harding* (1886) 17 Q.B.D. 442; *Re Patrick* [1891] 1 Ch. 82; *Re Griffin* [1899] 1 Ch. 408; *German* v. *Yates* (1915) 32 T.L.R. 52; *Re Rose* [1952] Ch. 499; *Pulley* v. *Public Trustee* [1956] N.Z.L.R. 771; *Mascall* v. *Mascall* (1984) 50 P. & C.R. 119.

[67] *Milroy* v. *Lord* (1862) 4 De G. F. & J. 264. But such an 'assignment' could nevertheless take effect as a declaration of trust.

[68] *Re Fry* [1946] Ch. 312.

[69] *Crouch* v. *Crédit Foncier of England* (1873) L.R. 8 Q.B. 374, at p. 380.

give can be taken and an assignee cannot be exempt from the effect of transactions by which the assignor may have lessened or invalidated the rights assigned.

Claims arising out of contract assigned

The debtor is entitled to raise, by way of defence to an action brought by the assignee, all claims that directly arise out of the contract or transaction which forms the subject-matter of the assignment, whether such claims accrue before or after notice of the assignment is received. So, for example, despite the fact that the assignee is wholly innocent and has given value for the contractual rights assigned, the debtor can rescind the contract on the ground that it was induced to enter into it by the fraud of the assignor[70] or set off a claim for unliquidated damages for breach of the contract by the assignor.[71]

But a debtor with a claim of a strictly personal nature against the assignor cannot set that claim up against an innocent assignee. The debtor is restricted to claims which arise out of the contract itself and do not exist independently of it. The line between the two may be fine. For instance, while, as we have seen, the debtor can assert a right to rescind a contract because of the fraud of the assignor, a claim for damages for fraud cannot be asserted by the debtor in proceedings by the assignee. Thus in *Stoddart* v. *Union Trust*:[72]

> The Union Trust were fraudulently induced by one Price to buy a newspaper called 'Football Chat' for the sum of £1,000, of which £200 was to be paid immediately, and the balance of £800 by instalments. Price assigned this £800 to the plaintiff, Stoddart, who took in good faith without knowledge of the fraud. When sued by Stoddart, the Union Trust pleaded that they had sustained damage exceeding £800 and that therefore no money was owed by them.

The Court of Appeal rejected this contention and held that the Union Trust could not set off their claim for damages against the assignee. Kennedy L.J. said:[73]

> The defendants are claiming damages for the fraud which induced them to enter into the contract on the footing that they are liable under it, and at the same time seeking to repudiate their obligation under it. The claim for damages is a personal claim against the wrong-doer; it is something dehors the contract.

The debtor may also not recover money paid to the assignee, even where a subsequent breach of contract has given rise to an obligation on the part of the assignor to repay the money.[74]

Claims arising out of other transactions

On the other hand, where a claim arises out of a contract or transaction other than the one which forms the subject-matter of the assignment (as where money on deposit with a bank is assigned, but the bank has a claim against the assignor for taking up and paying bills of exchange),[75] the debtor can set off such a claim

[70] *Graham* v. *Johnson* (1869) L.R. 8 Eq. 36.

[71] *Young* v. *Kitchin* (1878) 3 Ex. D. 127; *Newfoundland Government* v. *Newfoundland Ry.* (1888) 13 App. Cas. 199. See also *Bank of Boston Connecticut* v. *European Grain and Shipping Ltd.* [1989] A.C. 1056 (if debtor's claim against assignor could not be set off against debt, it cannot be set off against assignee).

[72] [1912] 1 K.B. 181.

[73] At p. 194.

[74] *Pan Ocean Shipping Co. Ltd.* v. *Creditcorp Ltd.* [1994] 1 W.L.R. 161.

[75] *Re Pinto Leite and Nephews* [1929] 1 Ch. 221.

against the assignee if but only if the claim accrues[76] *before the debtor has notice of the assignment*. The effect of notice is, therefore, in this case to prevent the debtor from setting up against the assignee any fresh equities which may mature. 'After notice of assignment of a chose in action the debtor cannot by payment or otherwise do anything to take away or diminish the rights of the assignee as they stood at the time of the notice.'[77]

(f) Priorities

Priority of two assignments of same debt

It may happen that an assignor makes two or more assignments of the same chose in action to different assignees. If the fund is insufficient to meet all the claims, a problem of their respective priorities will arise. The rule is that *equitable titles have priority according to the priority of notice*.[78] The successive assignees of an obligation rank as to their title, not according to the dates at which the creditor assigned the contractual rights to them respectively, but according to the dates at which notice was given to the party to be charged. This rule is generally known as the rule in *Dearle* v. *Hall*.[79] The reason lying behind it seems to be that, by failing to give notice to the debtor, the first assignee has enabled the assignor to make a second, and possibly fraudulent, assignment to the subsequent assignee. Accordingly, even though the first assignee's assignment was first in time, it ought to be postponed to the later assignment.

But the first assignee will only be postponed to a subsequent assignment of which prior notice has been given, if, at the time of the first assignment, the second assignee had no knowledge of the previous assignment.[80] A second assignee who had such knowledge, could scarcely claim to have been misled.

Except where the interest assigned is an equitable interest in land or in personalty, when the notice must be in writing,[81] no special form is required for a notice to gain priority. Provided it is clear and unequivocal, and brought home to the party charged, oral notice is sufficient. Even a notice in a newspaper read by the debtor has been held to suffice.[82] If the interest assigned is an equitable interest in a trust fund, it is advisable to give notice to all the trustees in order to be perfectly safe; otherwise notice given to one trustee alone may determine with his death or resignation.[83]

(g) Rights not Assignable

Limits to assignability (i) Assignment prohibited

Some choses in action are not assignable, and not every right which arises under or out of a contract can be assigned.

In the first place, the contract itself may expressly provide that the rights arising under it shall not be assignable. In such a case, a purported assignment of

[76] *Business Computers Ltd.* v. *Anglo-African Leasing Ltd.* [1977] 1 W.L.R. 578.
[77] *Roxburghe* v. *Cox* (1881) 17 Ch. D. 520, *per* James L.J. at p. 526.
[78] *Marchant* v. *Morton, Down & Co.* [1901] 2 K.B. 829.
[79] (1823) 3 Russ. 1.
[80] *Re Holmes* (1885) 29 Ch. D. 786.
[81] Law of Property Act 1925, s. 137(3).
[82] *Lloyd* v. *Banks* (1868) L.R. 3 Ch. App. 488.
[83] *Re Phillips' Trusts* [1903] 1 Ch. 183.

those rights will be invalid as against the debtor,[84] although it may be effective as between assignor and assignee.[85]

(ii) Bare right of action

Secondly, it is said that by reason of the rules against champerty and maintenance[86] a mere right to sue for damages (a 'bare right of action') cannot be assigned.[87] However, rights of action arising out of or incidental to rights of property can be assigned with the property transferred. Thus the purchaser of an estate was permitted to sue for damages for breaches of covenant committed by the vendor's tenants before the sale,[88] and the purchaser of land injuriously affected by a railway to claim compensation in respect of damages already sustained.[89] Again, a debt, as opposed to a mere right to sue for damages, is a species of property and is assignable at law.[90] Further, in *Trendtex Trading Corporation* v. *Crédit Suisse*,[91] the House of Lords made it clear that even an assignment of a bare right of action may be upheld if the assignee has a genuine commercial or financial interest in taking the assignment. An assignment to an insurer, who has indemnified the insured under a policy of insurance, of the insured's right of action has been held valid on the ground that the insurer has a legitimate interest in recouping the loss sustained by paying out on the policy.[92] Likewise, an assignee who has financed the transaction giving rise to the right of action assigned will have a legitimate commercial interest in taking the assignment if its sole object is to enable the assignee to recoup its loss on the transaction.[93] On the other hand, in the *Trendtex* case, the purchase with a view to profit of a right of action arising out of the breach and repudiation of a letter of credit was held to be invalid in English law as 'savouring of maintenance', since it involved trafficking in litigation.[94] But where the assignee has a genuine commercial or financial interest an assignment by a party not entitled to legal aid to a party so entitled, where the object and effect of the assignment is to enable the assignee to obtain legal aid, is not contrary to public policy or unlawful.[95]

[84] *United Dominions Trust Ltd.* v. *Parkway Motors* [1955] 1 W.L.R. 719; *Helstan Securities Ltd.* v. *Hertfordshire C.C.* [1978] 3 All E.R. 262; *Linden Gardens Trust Ltd.* v. *Lenesta Sludge Disposals Ltd.* [1994] 1 A.C. 85, at p. 103; Goode (1979) 42 M.L.R. 553; Allcock [1983] C.L.J. 328.

[85] *Re Turcan* (1888) 40 Ch. D. 5; *Re Westerton* [1919] 2 Ch. 104. Contrast *Spellman* v. *Spellman* [1961] 1 W.L.R. 921, at p. 928, but cf. at p. 925.

[86] See *ante*, p. 354. This principle is unaffected by the abolition of the torts and crimes of champerty and maintenance: see Criminal Law Act 1967, s. 14(2).

[87] *De Hoghton* v. *Money* (1866) L.R. 2 Ch. App. 164; *May* v. *Lane* (1894) 64 L.J.Q.B. 236; *Torkington* v. *McGee* [1902] 2 K.B. 427, at p. 433 (decision reversed [1903] 1 K.B. 644); *Defries* v. *Milne* [1913] 1 Ch. 98. Cf. *Glegg* v. *Bromley* [1912] 3 K.B. 474 (fruits of action).

[88] *Defries* v. *Milne* (*supra*, n. 87); *Ellis* v. *Torrington* [1920] 1 K.B. 399.

[89] *Dawson* v. *G.N. & City Ry.* [1905] 1 K.B. 260.

[90] *Ellis* v. *Torrington* (*supra*, n. 88) at p. 411; *Camdex International Ltd.* v. *Bank of Zambia* [1996] 3 W.L.R. 759.

[91] [1982] A.C. 679, at pp. 694, 696, 697, 703.

[92] *Compania Colombiana de Seguros* v. *Pacific Steam Navigation Co.* [1965] 1 Q.B. 101.

[93] *Trendtex Trading Cpn.* v. *Crédit Suisse* (*supra*, n. 91), at pp. 694, 696, 697, 703 (but not if the object is to sell on to and divide the 'spoils' with a subsequent assignee).

[94] See also *Re Trepca Mines Ltd. (No. 2)* [1963] Ch. 199; *Laurent* v. *Sale & Co.* [1963] 1 W.L.R. 829; *Re Oasis Merchandising Services Ltd.* [1997] 2 W.L.R. 764.

[95] *Norglen Ltd.* v. *Reeds Rains Prudential Ltd* [1996] 1 W.L.R. 864, aff'd [1997] 3 W.L.R. 1177; *Circuit Systems Ltd.* v. *Zuken-Redac (U.K.) Ltd.* [1997] 1 W.L.R. 721.

(iii) Personal contracts

Thirdly, where some relation of personal confidence between the parties or their personal qualifications are of the essence of a contract, one party cannot assign the right to the performance of the obligations of the other, since to do so would be to alter the nature of the contract without the other's consent.

So, for example, a cake manufacturer was held not to be able to assign the right to be supplied with 'all the eggs he should require for manufacturing purposes for one year' to a new company on the amalgamation of the business.[96] What the supplier had undertaken to do was to supply all the eggs that the manufacturer, and not all that any other person or company, should require. Moreover, the manufacturer had undertaken not to buy eggs elsewhere and this introduced a personal element which was most material to the contract. This undertaking would not be binding on the assignee, so that the supplier would be deprived of its benefit. For a similar reason, a motor insurance policy cannot be assigned to the purchaser if the car is sold, unless the insurance company consents to the assignment, for that would be to 'thrust a new assured upon a company against its will'.[97] On the other hand, where it appears from the nature of the contract that no special personal considerations are involved, so that it can make no difference to the party on whom an obligation rests whether the performance is rendered for the original contracting party or another, then the right to the performance of an obligation may be assigned.[98]

(iv) Contracts of employment

The paradigm example of a personal contract is a contract of employment but, although at common law an employer could not assign its rights under contracts of employment with employees if it transferred the business without consent,[99] the position has been altered by legislation. On transfers of a business by sale, other disposition or by operation of law (e.g. on insolvency), there is a statutory novation by which all rights, powers, duties, and liabilities under a contract of employment operate between the employee and the transferee[100] unless the employee gives notice that he or she objects to being employed by the transferee.

(v) Salaries of public officers, etc.

Finally, for reasons of public policy, no assignment may be made of the salary of a public officer paid out of national funds (for example of a civil servant's pay),[101] of maintenance granted to a wife,[102] or of benefits under social security legislation.[103]

[96] *Kemp* v. *Baerselman* [1906] 2 K.B. 604.

[97] *Peters* v. *General Accident and Life Assurance Corporation Ltd.* [1937] 4 All E.R. 628, *per* Goddard J. at p. 633.

[98] *Tolhurst* v. *Associated Portland Cement Manufacturers (1900) Ltd.* [1903] A.C. 414; *Shayler* v. *Woolf* [1946] Ch. 320.

[99] *Nokes* v. *Doncaster Amalgamated Collieries Ltd.* [1940] A.C. 1014, at p. 1026; *Newns* v. *British Airways* (1992) 21 I.R.L.R. 575, at p. 576.

[100] Transfer of Undertakings (Protection of Employment) Regulations 1981 (S.I. 1981 No. 1794), reg. 5(1); Trade Union Reform and Employment Rights Act 1993, s. 33. See *Secretary of State for Employment* v. *Spence* (1986) 15 I.R.L.R. 248, at p. 251; *Litster* v. *Forth Dry Dock & Engineering Co. Ltd.* (1989) 18 I.R.L.R. 161.

[101] See *ante*, p. 353.

[102] *Re Robinson* (1884) 27 Ch. D. 160.

[103] e.g. Social Security Act 1975, s. 87; Supplementary Benefits Act 1976, s. 16.

II. Assignment of Contractual Liabilities

Liabilities cannot be assigned

THE burden of a contract can never be assigned without the consent of the other party to the contract.[104] A promisor cannot assign its liabilities under a contract without the consent of the promisee; or, conversely, a promisee cannot be compelled, by the promisor or by a third party, to accept any but the promisor as the person liable on the promise.

The rule is based on sense and convenience, for a contracting party ought not to be permitted to shift the burden of a contract onto the shoulders of a third party without the consent of the other party to the contract. It is illustrated by the case of *Robson and Sharpe* v. *Drummond*:[105]

S hired a carriage to D for 5 years, undertaking to paint it every year and to keep it in repair. R was the partner of S, but the contract was made with S alone. After 3 years S retired from business, and D was informed that R was thenceforth answerable for the painting and repair of the carriage and would receive the payments. D refused to deal with R, and returned the carriage.

It was held that he was entitled to do so. Lord Tenterden stated:[106]

[T]he defendant may have been induced to enter into this contract by reason of the personal confidence which he reposed in [S], and therefore have agreed to pay money in advance. The . . . defendant had a right to object to its being performed by any other person, and to say that he contracted with [S] alone, and not with any other person.

Parke J. stated that D 'had a right to have the benefit of the judgment and taste of [S] to the end of the contract'.[107]

Apparent exceptions (i) vicarious performance

There are certain limitations to this rule. In the first place, there may be circumstances which make it permissible for a contracting party to perform its side of the contract by getting someone else to do in a satisfactory fashion the work for which the contract provides. If A undertakes to do work for B which needs no special skill, and it does not appear that A has been selected with reference to any personal qualification, B cannot complain if A sub-contracts the work to an equally competent sub-contractor. Such cases are sometimes loosely referred to as assignments of a contractual liability, but they are really instances of the *vicarious performance* of a contract. The original contracting party remains liable on the contract and, as a rule, is the only person entitled to sue for payment. This is clearly stated by Lord Greene M.R. in *Davies* v. *Collins*:[108]

In many contracts all that is stipulated for is that the work shall be done and the actual hand to do it need not be that of the contracting party himself; the other party will be bound to accept performance carried out by somebody else. The contracting party, of course, is the only party who remains liable. He cannot assign his liability to a sub-contractor, but his liability in those cases is to see that the work is done, and if it is not

[104] *Linden Gardens Trust Ltd.* v. *Lenesta Sludge Disposals Ltd.* [1994] 1 A.C. 85, at p. 103.
[105] (1831) 2 B. & Ad. 303. [106] At p. 307. [107] At p. 308.
[108] [1945] 1 All E.R. 247, at p. 249. See also *Stewart* v. *Reavell's Garage* [1952] 2 Q.B. 545.

properly done he is liable. It is quite a mistake to regard that as an assignment of the contract; it is not.

The circumstances in which a contract may be vicariously performed, which are similar to those which determine whether a contractual right is assignable, are discussed in Chapter 11.

(ii) Novation

Another way by which the burden of a contract may be 'assigned' to third party is with the co-operation of the party entitled to performance. A liability may be transferred with the consent of the party entitled; but this is in effect the rescission of one contract and the substitution of a new one in which the same acts are to be performed by different parties. This is called a novation and it can only take place by an agreement supported by consideration[109] between the parties; novation cannot be compulsory.[110] It is therefore not properly to be regarded as an assignment.

(iii) Mutual rights and obligations

As a general rule, where the benefit of a contract, involving mutual rights and obligations, is the subject of a valid assignment, the assignee does not acquire the assignor's contractual obligations. But the circumstances may be such as to show that the assignee agreed to accept, not merely the rights, but also the obligations of the contract;[111] alternatively the rights assigned may themselves be qualified or conditional, the condition being that certain restrictions be observed or certain obligations assumed.[112] In such situations, an assignee who takes the benefit of the contract must also bear the burden.

III. Negotiable Instruments[113]

Negotiability

So far we have dealt with the assignment of contractual rights by the rules of common law, equity, and statute, and it appears that under the most favourable circumstances the assignment of a contract binds the party chargeable to the assignee only when notice is given, and subject always to the rule that a better title than the assignor possesses cannot be given to the assignee.

We now come to deal with a class of promises in writing, the benefit of which can be transferred in such a way that the promise may be enforced by the transferee of the benefit without previous notice to the debtor, and without the risk of being met by defences which would have been good against the transferor of the promise. In other words, we come to consider that special class of contracts known

[109] *Commissioners of Customs and Excise* v. *Diners Club Ltd.* [1988] 2 All E.R. 1016, at p. 1023, aff'd. [1989] 1 W.L.R. 1196.

[110] Approved in *Re United Railways of the Havana and Regla Warehouses Ltd.* [1960] Ch. 52, at p. 84, reversed in part on other grounds *sub nom. Tomkinson* v. *First Pennsylvania Banking and Trust Co.* [1961] A.C. 1007. See also *ante*, p. 448.

[111] *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at pp. 290–307. See also *Rother Iron Works Ltd.* v. *Canterbury Precision Engineers Ltd.* [1974] Q.B. 1.

[112] *Tolhurst* v. *Associated Portland Cement Manufacturers Ltd.* [1903] A.C. 414.

[113] See generally Chalmers and Guest, *Bills of Exchange*, 14th edn. (1991).

as 'negotiable instruments', in which the process of transfer is termed 'negotiation'.[114]

Features of negotiability

For an instrument to be negotiable these features seem to be essential:

In the first place, the title to it passes by delivery, or, if it is made to order (that is to say, either expressed to be so payable, or expressed to be payable to a particular person) then by the indorsement of the payee completed by delivery.

Secondly, the written promise which it contains gives a right of action to the holder of the document for the time being, though the holder and the fact of the holding may be alike unknown to the promisor.

Thirdly, a *bona fide* holder for value is not prejudiced by defects in the title of the assignor; the holder does not hold 'subject to equities'.

Fourthly, the instrument is of a type recognized by the law as negotiable. The parties cannot confer negotiability upon a contract which is not recognized by the law to possess this quality.

(a) Types of Negotiable Instrument

Examples of negotiable instruments

Certain instruments are negotiable by the custom of merchants recognized by the Courts; others are negotiable by statute. The operation of negotiability can best be illustrated by reference to some of these.

(i) Cheques

Cheques

Although, since the Cheques Act 1992, a large number of cheques are not negotiable,[115] the cheque remains the type of negotiable instrument which will be most familiar to readers of this textbook. A cheque is an unconditional order, addressed by the drawer of the cheque to a banker, directing him to pay on demand a certain sum to the person named on the face of the cheque or the bearer. If the cheque is made payable to 'Bearer' or to 'A or Bearer', the mere delivery of it by one holder to another suffices as negotiation and the holder for the time being is entitled to present the cheque for payment without any further formality. But if it is made payable to 'A or Order', it must first be indorsed. Until it is indorsed, a simple delivery does not suffice.[116] For the cheque to be negotiated, A must indorse it, and this is done by A signing on the back.

Indorsement in blank

If the indorsement consists in the mere signature of A, the cheque is said to be indorsed 'in blank'. It then becomes a cheque payable to bearer, that is, negotiable by mere delivery, for A has given his order, though it is an order not mentioning any particular person. The cheque is in fact indorsed over to anyone who becomes possessed of it.

Special indorsement

If the indorsement takes the form of an order in favour of B, written on the cheque and signed by A, i.e. 'B or Order', it is called a 'special' indorsement. Its effect is to transfer to B the right to demand payment of the cheque. Once again, B must now indorse the cheque, and may do so specially or in blank. Thus the

[114] See *post*, pp. 466–7 for the separate legal notion of 'transferability'.

[115] *Post*, p. 463.

[116] The Cheques Act 1957 removes the necessity for the indorsement of cheques paid into the account of the payee, but this does not apply where it is sought to negotiate the instrument.

cheque may pass through several hands before it is ultimately presented for payment.

(ii) Bills of exchange

Bills of exchange

A bill of exchange is an unconditional order in writing, addressed by A to B, requiring B to pay a sum of money to or to the order of a specified person or to bearer. Usually this specified person is a third person, C, but it need not be. A may draw a bill upon B in favour of A. We may assume, for example, that the order is addressed to B because B is buying goods from A and it has been arranged that 'payment' for the goods is to be made to C (a bank) or directly to A by means of a bill instead of cash; and since we are here dealing with bills of exchange merely as illustrative of negotiability, we will adopt the most usual, as it is the most convenient, form of illustration.

How drawn

A directs B to pay a sum of money 'to the Order of C', or to 'Bearer'. A is then called the drawer of the bill, and by drawing it promises to pay the sum specified in it either to C or to any subsequent holder into whose hands it may come if B does not 'accept' the bill or, having accepted it, fails to pay.

How accepted

B, upon whom the bill has been drawn, is called the drawee; but on assenting to pay the sum specified, B is said to become the 'acceptor'. Such assent (or 'acceptance') must be expressed by writing on the bill and signed by B. The payee of the bill, in our example C, may transfer it to another person before it has been accepted, and in that case it is for the transferee to present it to B for acceptance. Acceptance may be general or qualified. A general acceptance assents without qualification to the order of the drawer; but the person presenting the bill may be willing to take one qualified by conditions as to amount, time, or place,[117] though this releases the drawer or any previous indorser from liability unless they assent to the qualification.

Indorsement

The rules relating to payment, indorsement, and transfer by delivery are similar to those concerning cheques, and given above. If the bill has been accepted, the holder may demand payment from the acceptor. But in the event of default in acceptance or payment, the holder may also demand compensation either from the original drawer, or from any indorser; for an indorser is to all intents and purposes a new drawer, and becomes therefore an additional security for payment to the holder for the time being.

(iii) Promissory notes

Promissory notes

A promissory note is an unconditional promise in writing made by one person to another signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money, to, or to the order of, a specified person or to bearer.[118] A Bank of England note is a promissory note which by statute is made legal tender.[119]

[117] But by the Bills of Exchange Act 1882, s. 19(2) a condition as to payment at a particular place is not a qualified acceptance 'unless it expressly states that the bill is to be paid there only, and not elsewhere'. Hence the common form 'accepted payable at X Bank' is not a qualified acceptance.

[118] Bills of Exchange Act 1882, s. 83(1).

[119] Currency and Bank Notes Act 1954, s. 1.

Bills of exchange were negotiable by the law merchant; promissory notes were originally made so by the Promissory Notes Act 1704; both classes of instrument are now governed by the Bills of Exchange Act 1882.[120] A cheque is in fact a species of bill of exchange, but it possesses certain features of its own not common to all bills of exchange.

(iv) Other negotiable instruments

Instruments negotiable by custom

Certain other instruments are negotiable by the custom of merchants recognized by the Courts; such are foreign bonds expressed to be transferable by delivery,[121] and scrip certificates which entitle the bearer to become holder of such bonds or shares in a company,[122] and, perhaps we may say, other instruments to which the character of negotiability may from time to time be attached by the custom of merchants proved to the satisfaction of the Courts; i.e. notorious, certain, reasonable, and general.[123] The categories of negotiable instruments are never closed.

In *Goodwin* v. *Robarts*[124] the Court of Exchequer Chamber rejected the view that a mercantile custom of recent origin was insufficient to attach to an instrument the character of negotiability:

The plaintiff purchased scrip issued by the agent of a foreign government from a broker, but allowed the broker to remain in possession of it. The broker fraudulently pledged the scrip to the defendants in order to secure a loan. The defendants took the scrip in good faith and, upon the default of the broker, sold it. If the scrip was negotiable, the defendants acquired a good title; if not, they would be liable to the plaintiff as true owner.

It was held that the scrip was negotiable according to the custom of merchants. Dealing with the argument that this was a new and unrecognized type of negotiable instrument, Cockburn C.J. said:[125]

We are of the opinion that [this argument] cannot prevail. It is founded on the view that the law merchant thus referred to is fixed and stereotyped, and incapable of being expanded and enlarged so as to meet the wants and requirements of trade in the varying circumstances of commerce. It is true that the law merchant is sometimes spoken of as a fixed body of law, forming part of the common law, and as it were coeval with it. But as a matter of legal history, this view is altogether incorrect. The law merchant thus spoken of with reference to bills of exchange and other negotiable securities, though forming part of the general body of the lex mercatoria, is of comparatively recent origin. It is neither more nor less than the usages of merchants and traders in the different departments of trade, ratified by the decisions of Courts of law, which, upon such usages being proved before them, have adopted them as settled law with a view to the interests of trade and the public convenience.

Negotiability emphasizes the interest which merchants have in dynamic security, in speedy transactions, and the protection of the *bona fide* purchaser, as opposed

[120] As amended.
[121] *London Joint Stock Bank* v. *Simmons* [1892] A.C. 201.
[122] *Goodwin* v. *Robarts* (1875) 1 App. Cas. 476; *Rumball* v. *Metropolitan Bank* (1877) 2 Q.B.D. 194.
[123] See *ante*, p. 148.
[124] (1875) L.R. 10 Ex. 337, affirmed (1875) 1 App. Cas. 476. See also *Bechuanaland Exploration Co. Ltd.* v. *London Trading Bank Ltd.* [1898] 2 Q.B. 658 and *Edelstein* v. *Schuler & Co.* [1902] 2 K.B. 144; Bosanquet and Palmer (1899) 15 L.Q.R. 130, 245.
[125] (1875) L.R. 10 Ex. 337, at p. 346.

to static security which is designed to safeguard the title of the true owner.[126] The decision in *Goodwin* v. *Robarts* enables the Courts to give effect to that interest.

(b) Assignability and Negotiability

Assignability and negotiability distinguished

We may now endeavour to isolate the characteristics of a negotiable instrument, and to distinguish between assignability and negotiability.

(i) Notice

In the first place, notice to the debtor is never required in the case of a negotiable instrument, whereas in the case of an assigned contract, notice is necessary to perfect a statutory assignment, and is advisable in equitable assignments so as to prevent the debtor paying the assignor. Since the benefit of the promise to pay is transferable by the mere delivery of a negotiable instrument, the right of action vests in the holder for the time being, and he need give no notice to the promisor.

(ii) Title

Secondly, the holder for the time being, provided that he is a *bona fide* holder for value without notice,[127] obtains a good title to a negotiable instrument; whereas in assignment, the assignee takes 'subject to equities'. So, for example, if the instrument has been stolen, or obtained by fraud, a holder who took the instrument in good faith and for value, and without notice of any defect in the title of the person who negotiated it will still be entitled to demand payment. Thus in *London Joint Stock Bank* v. *Simmons*:[128]

> Negotiable bonds belonging to X were pledged to a bank by X's broker without authority, to secure a loan to the broker. The bank had no notice of these facts. On the broker's insolvency, the bank sold the bonds in satisfaction of the debt due, and the broker's clients sued the bank.

It was held by the House of Lords that the bank was entitled to retain and realize the securities, as it had taken the bonds for value and in good faith. 'It is', said Lord Herschell,[129] 'surely of the very essence of a negotiable instrument that you may treat the person in possession of it as having authority to deal with it, be he agent or otherwise, unless you know to the contrary, and are not compelled, in order to secure a good title to yourself, to inquire into the nature of his title, or the extent of his authority'.

(iii) Consideration

Thirdly, the doctrine of consideration does not always apply to negotiable instruments in the same way as to ordinary contracts. The rule in ordinary contracts (including some contracts of assignment) is that consideration must move from the promisee.[130] But in the case of bills of exchange, for example, no consideration need necessarily have been given by the holder of the bill. Section 27(2) of the Bills of Exchange Act 1882 provides that, where value has *at any time* been given for a bill, the holder is deemed to be a holder for value as regards the acceptor and all parties to the bill who became parties prior to such time.[131] Once value

[126] Demogue, *Modern French Legal Philosophy*, p. 418.
[127] A 'holder in due course': Bills of Exchange Act 1882, s. 29(1).
[128] [1892] A.C. 201.
[129] At p. 217.
[130] See *ante*, p. 95.
[131] See *Scott* v. *Lifford* (1808) 1 Camp. 246; *Diamond* v. *Graham* [1968] 1 W.L.R. 1061.

has been given by a party to the bill, the holder can enforce the bill whether he or she personally gave value or not.[132]

(iv) Holder in due course

Finally we may note that in the case of bills of exchange certain presumptions greatly assist the holder to establish a right to sue on the bill. Every holder of a completed bill of exchange is *prima facie* deemed to be 'a holder in due course'—that is, is presumed to have given value for it in good faith, without notice of any defect in title of the person who negotiated it.[133] The holder will therefore have to do no more than prove the signature of the person sued, everything else being presumed in the holder's favour. The burden will be on the person sued to prove that the holder's title is in some way defective or that no consideration has been given.

But to this rule there is an important exception. If in an action on the bill it is admitted or proved that the acceptance, issue, or subsequent negotiation of the bill is tainted with fraud or illegality of some kind, then this presumption no longer holds good. The burden of proof is shifted, and it is now the holder of the bill who must prove affirmatively that, subsequent to the alleged fraud or illegality, value has in good faith been given for the bill, though not necessary by itself.[134] A holder who can do so will still win the action whatever the earlier history of the bill may be, unless the holder was a party to the fraud or illegality alleged. A holder who has been a *party* to the fraud or illegality can never succeed, though mere knowledge of it will not invalidate the holder's title, if it is derived, not from a person whose own title is defective, but from one who is a holder in due course.[135]

Use of bills

In modern business practice, the primary function of a bill of exchange is to enable a seller or exporter to obtain cash as soon as possible after the despatch of the goods, and yet enable the buyer or importer to defer payment until the goods reach him, or later. Credit can be obtained if the bill is accepted by a bank, upon whom the parties can rely, and bills can be bought and sold on the discount market.[136]

(c) Limitation of Negotiability

Negotiability may be curtailed

We have spoken all the time of a bill of exchange or promissory note as if it must always be a negotiable instrument. But it is to be noted that a particular bill or note is only negotiable if it is in a condition of negotiability. It may, for example, contain words which prevent its transferability or negotiability. If so, it is valid as between the parties thereto, but is not negotiable.[137] For example, if a bill of exchange is drawn payable 'to P only' it is not transferable and only P can sue on

[132] *Sed quaere* whether this is so as between immediate parties whose relations regarding the bill arise out of their direct dealings: *Churchill & Sim* v. *Goddard* [1937] 1 K.B. 92, at p. 110; *Pollway Ltd.* v. *Abdullah* [1974] 1 W.L.R. 493; *Hasan* v. *Willson* [1977] 1 Lloyd's Rep. 431, at p. 441.

[133] Bills of Exchange Act 1882, s. 30(2).

[134] *Tatam* v. *Haslar* (1889) 23 Q.B.D. 345; *ante*, p. 344.

[135] Bills of Exchange Act 1882, s. 29(3).

[136] Gillett Bros., *The Bill on London* (1964), p. 16.

[137] Bills of Exchange Act 1882, s. 8(1).

it.[138] However, if a crossed cheque merely bears the words 'not negotiable', it still remains transferable, though the person to whom it is transferred takes it subject to any defect in the title of the transferor.[139] But, by the Cheques Act 1992 a crossed cheque with the words 'account payee' or 'a/c payee' with or without the words 'only' is not transferable. Cheque books issued by banks often contain these words. Crossing a cheque does not of itself hinder the negotiability of the cheque; it simply means that it cannot be presented for payment over the counter, but must be collected through a banker.

It is also possible for a bill to be restrictively indorsed, e.g. 'Pay Q only', in which case Q has the right to receive payment of the bill and to sue any party thereto that the indorser could have sued, but it gives Q no power to transfer its rights as indorsee unless the indorsement expressly authorized Q to do so.[140]

(d) Bills of Lading[141]

Bills of lading

Bills of lading, which are affected both by the law merchant and by statute, possess some characteristics which call for separate consideration. They are not, in fact, fully negotiable, but certain rights are transferred by indorsement and delivery of the bill.

Its several aspects

A bill of lading may be regarded in three several aspects: (i) it is a receipt given by the shipowners acknowledging that the goods specified in the bill have been put on board; (ii) it is a document which contains or evidences the terms of the contract for the carriage of the goods agreed upon between the shipper of the goods and the shipowners whose ship is to carry them; and (iii) it is a 'document of title' to the goods, of which it is the symbol. It is by means of this document of title that the goods themselves may be dealt with by the owner of them while they are still upon the high seas.

Three copies of the bill of lading are usually made, each signed either by the master of the ship or by the agents of the shipowner. One copy is kept by the consignor of the goods and one by the master of the ship, and the original is forwarded to the consignee, who (in the normal case) on receipt of it acquires a property in the goods which can only be defeated by the exercise of the right of the vendor of the goods to stop them in transit.[142] But if, before stoppage, the consignee lawfully transfers a bill of lading by indorsement and delivery to a holder in good faith and for value, that holder has a title to the goods which overrides the vendor's right of stoppage in transit. The holder of the bill can claim the goods in spite of the insolvency of the consignee, and the consequent loss of the price of the goods by the vendor.[143]

[138] *Hibernian Bank Ltd.* v. *Gysin and Hanson* [1939] 1 K.B. 483.

[139] Bills of Exchange Act 1882, s. 81 (crossed cheques only).

[140] *Ibid.*, s. 35(1) and (2).

[141] See generally *Scrutton on Charterparties and Bills of Lading*, 20th edn. (1996).

[142] Stoppage in transit is the right of the unpaid seller who has parted with possession of the goods sold to resume possession of them as long as they are in the course of transit, and to retain them until payment or tender of the price. It may be exercised when the buyer is insolvent. See Sale of Goods Act 1979, ss. 44–6.

[143] Sale of Goods Act 1979, s. 47.

At common law, the holder's right was a right of property only. The indorsement of a bill of lading gave a right to the goods alone; it did not give the holder any power to sue on the contract expressed in the bill. This proved very inconvenient and the Bills of Lading Act 1855 provided that an indorsee to whom the property in the goods passed by the indorsement acquired 'all rights of suit' and 'the same liabilities in respect of the goods'.[144] The position is now governed by the Carriage of Goods by Sea Act 1992 which provides that the lawful holder of a bill of lading is entitled to assert contractual rights irrespective of the passing of property and regardless of whether the holder has itself suffered loss.[145]

Distinguished from negotiable instruments proper

A bill of lading differs from the negotiable instruments with which we have just been dealing:

In the first place, its indorsement transfers a remedy *in rem*, the right to claim specific goods, whereas a negotiable instrument confers only a remedy *in personam*, the right to be paid a certain sum of money.

Secondly, although the indorsee is relieved from one of the liabilities to which the consignee of the goods is exposed, namely, the vendor's right of stoppage in transit, it does not acquire proprietary rights independent of the consignee's title: a bill of lading stolen, or transferred without the authority of the person really entitled, gives no such rights even to a *bona fide* indorsee.[146] Again the contractual rights transferred are, in effect, 'subject to equities' because, where the holder takes or demands delivery of the goods or otherwise claims under the contract of carriage against the shipowner, it becomes subject to any contractual liabilities as if it had been a party to the contract of carriage.[147]

IV. Assignment by Operation of Law

So far we have dealt with the voluntary assignment by parties to a contract of the benefit or the liabilities of the contract. But rules of law may also operate to transfer these rights or liabilities from one to another.

(a) The Effect of Death

The general rule is that rights and liabilities under a contract pass, on the death of a party to the contract, to his or her personal representatives.

But performance of such contracts as depend upon the personal service or skill of the deceased cannot be demanded of personal representatives, nor can they insist upon offering such performance, though they can sue for money earned by

[144] s. 1. For criticism, see Law Com. No. 196, *Rights of Suit in Respect of Carriage of Goods by Sea* (1991).

[145] s. 2(1). Where loss is suffered by another the holder's rights are exercised for the benefit of the person who sustained the loss: *ibid.*, s. 2(4).

[146] *Gurney* v. *Behrend* (1854) 3 E. & B. 622, at p. 634. See also Carriage of Goods by Sea Act 1992, ss. 2(1) and 5(2) ('lawful' holder).

[147] Carriage of Goods by Sea Act 1992, s. 3.

the deceased and unpaid at the time of the death.[148] Contracts of agency and of personal service expire with the death of either of the parties to them; thus an apprenticeship contract is terminated by the death of the master, and no claim to the services of the apprentice survives to the executor or administrator.[149]

(b) Bankruptcy

Trustees' powers: their extent, and limits

Bankruptcy is regulated by the Insolvency Act 1986. Proceedings commence with the filing of a petition for a bankruptcy order either by a creditor alleging acts of bankruptcy against the debtor or by the debtor alleging inability to pay the debts.[150] Where the grounds of the petition are established the Court may, in an appropriate case, appoint an insolvency practitioner to ascertain whether the debtor is willing to make a proposal for a voluntary arrangement and a meeting of the creditors should be summoned.[151]

If the creditors decide not to accept a composition or scheme of arrangement, the Court makes a bankruptcy order and a trustee is appointed. To the trustee passes 'all property belonging to or vested in the bankrupt at the commencement of the bankruptcy',[152] or may be acquired by or has devolved upon the bankrupt since the commencement of the bankruptcy.[153] The object of the laws of bankruptcy is that 'every beneficial interest which the bankrupt has shall be disposed of for the benefit of his creditors'.[154] It suffices to note that:

(1) Where any part of the property of the bankrupt consists of a chose in action, it is deemed to have been assigned to the trustee.[155]
(2) The trustee may disclaim, and so discharge, unprofitable contracts.[156]
(3) The trustee is excluded from suing for personal injuries arising out of breaches of contract, such as injuries to reputation or credit.[157]
(4) Executory contracts personal to the bankrupt do not pass.[158]

The trustee, as statutory assignee of the bankrupt's choses in action, is in one respect in a more favourable position than an ordinary assignee. If a chose in action has been assigned by the bankrupt *before* the bankruptcy took place, the

[148] *Stubbs* v. *Holywell Railway Co.* (1867) L.R. 2 Ex. 311.
[149] *Baxter* v. *Burfield* (1746) 2 Stra. 1266.
[150] Insolvency Act 1986, ss. 264–72.
[151] *Ibid.*, ss. 273–4.
[152] *Ibid.*, s. 283(1). 'Property' includes 'things in action': *ibid.*, s. 436. Between the date of the order and the appointment of the trustee the official receiver is under a duty to act as receiver and manager of the estate: *ibid.*, s. 287.
[153] *Ibid.*, s. 307.
[154] *Smith* v. *Coffin* (1795) 2 H. Bl. 444, at p. 461.
[155] Insolvency Act 1986, s. 311(4). Where there is a cross-claim what is assigned is a claim to the net balance: *ibid.*, s. 323; *Stein* v. *Blake* [1996] A.C. 243.
[156] *Ibid.*, s. 315. An administrative receiver of a company becomes liable on any contract of employment 'adopted' by him: *ibid.*, s. 44; *Powdrill* v. *Watson* [1995] 2 All E.R. 65.
[157] *Wilson* v. *United Counties Bank* [1920] A.C. 102 (credit); *Re Kavanagh* [1949] 2 All E.R. 264, affirmed [1950] 1 All E.R. 39n. (reputation). Cf. *Beckham* v. *Drake* (1849) 2 H.L.C. 579 (wrongful dismissal). See *Heath* v. *Tang* [1993] 1 W.L.R. 1421.
[158] *Gibson* v. *Carruthers* (1841) 8 M. & W. 321 (contract to marry); *Lucas* v. *Moncrieff* (1905) 21 T.L.R. 683 (contract to publish book).

assignment will be void as against the trustee if (i) it is of a future chose in action for which the consideration is not supplied until after the commencement of the bankruptcy[159] or (ii) it is a general assignment of book debts by a trader and has not been registered under the Bills of Sale Act.[160]

(c) Land

Land

If a person acquires an interest in land from another, either by purchase or lease, upon terms which bind that person to observe certain covenants respecting the land, the assignment by either party to the contract of his interest will, in certain circumstances, operate as a transfer to the assignee of the rights and obligations arising out of the covenants.[161] This subject is, however, best studied in the special works on the law of land, and is accordingly omitted here.

[159] *Wilmot* v. *Alton* [1897] 1 Q.B. 17; *Re Collins* [1925] Ch. 556; *Re de Marney* [1943] Ch. 126. Cf. *Re Davis & Co.* (1888) 22 Q.B.D. 193; *Re Trytel* [1952] 2 T.L.R. 32.

[160] Insolvency Act 1986, s. 344.

[161] See *ante*, pp. 423, 431.

PART 4

Performance and Discharge

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12

Performance

Performance must be precise and exact

THE general rule is that performance of a contract must be precise and exact. That is, a party performing an obligation under a contract must perform that obligation exactly within the time frame set by the contract and exactly to the standard required by the contract. Sometimes that standard will be strict. This is so in the case of many common law obligations[1] and the statutory implied terms of quality in contracts for the sale and supply of goods.[2] Sometimes, as in the case of contracts for services, it will only require the exercise of reasonable care[3] or due diligence.[4] Whether the alleged performance satisfies this criterion is a question to be answered by construing the contract, so as to see what the parties meant by performance, and then by applying the ascertained *facts* to that construction, to see whether that which has been done corresponds to that which was promised.

If there is the slightest deviation from the terms of the contract, the party not in default will be entitled to say that the contract has not been performed, will be entitled to sue for damages for breach, and, in certain cases, to elect to be discharged. Thus in *Re Moore & Co. and Landauer & Co.*:[5]

> The defendants agreed to buy from the plaintiffs 3,000 tins of canned fruit from Australia to be packed in cases containing 30 tins. When the goods were tendered it was found that a substantial part of the consignment was packed in cases containing 24 tins.

The defendants were entitled to reject the whole consignment. Even if the performance effected is commercially no less valuable than that which was promised, there is a default in performance. So a contract to ship goods direct from Singapore to New York was held not to have been performed by shipping them to the American Pacific Seaboard and thence to New York by train.[6]

[1] *Kurt A. Becher G.m.b.H & Co. K.G.* v. *Roplak Enterprises S.A. (The World Navigator)* [1991] 2 Lloyd's Rep. 23 (sellers obligation to load cargo); *The Anathanasia Cominos* [1990] 1 Lloyd's Rep. 277, at p. 282 (obligation not to ship dangerous cargo); *Pagnan SpA.* v. *Tradax Ocean Transportation SA.* [1987] 3 All E.R. 565 (obtaining export licence).

[2] Sale of Goods Act 1979, ss. 12, 14 (as amended), *ante*, p. 150; Supply of Goods and Services Act 1982, ss. 4 and 9. See also Supply of Goods Act (Implied Terms) Act 1973, s. 10 (hire purchase).

[3] e.g., *Lister* v. *Romford Ice and Cold Storage Co Ltd* [1957] A.C. 555 (driving lorry); *Thake* v. *Maurice* [1986] QB 644, at pp. 684–7, cf. pp. 677–8 (medical treatment); *Smith* v. *Eric S. Bush* [1990] 1 A.C. 831 at 843 (surveying house); *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145, at p. 176 (managing agents of Lloyds underwriters). See also Supply of Goods and Services Act 1982, s. 13. Cf. *Samuels* v. *Davis* [1943] 1 K.B. 526.

[4] Carriage of Goods by Sea Act 1971, s. 3 (seaworthiness); *Union of India* v. *N.V. Reederij Amsterdam* [1962] 2 Lloyd's Rep. 233 (H.L.).

[5] [1921] 2 K.B. 519.

[6] *Re L. Sutro & Co. and Heilbut Symons & Co.* [1917] 2 K.B. 348.

Only if the deviation is 'microscopic' will the contract be taken to have been correctly performed, for *de minimis non curat lex*.[7] We shall first discuss stipulations concerning the time and place of performance. We shall then consider payment, vicarious performance, alternative modes of performance, and when there is a right to cure bad or incomplete performance. Finally we shall consider tender and the partial performance of an entire obligation, two situations in which a party who does not render precise and exact performance of a contract is nevertheless treated as having performed to some extent.

I. Time and Place of Performance

(a) Time of Performance

Stipulations as to time at common law

Where a time was fixed for the performance of an undertaking by one of the parties to the contract, the common law as a general rule held this to be 'of the essence of the contract'.[8] If the condition as to time was not fulfilled, the other party might treat the contract as broken and elect to terminate it.[9] For instance, in a contract for the sale of a flat where time was stated to be of the essence, the vendor was entitled to terminate when the purchaser tendered the price 10 minutes late.[10]

Stipulations as to time in equity

Equity did not so regard a condition as to time. Where it could do so without injustice to the contracting parties it decreed specific performance notwithstanding failure to observe the time fixed by the contract for completion, and as an incident of specific performance relieved the party in default by restraining proceedings at law based on such failure.[11]

Law of Property Act 1925, s. 41

Since the passing of the Judicature Acts, the rules of common law and equity have been fused,[12] and section 41 of the Law of Property Act 1925[13] enacts:

> Stipulations in a contract, as to time or otherwise, which according to rules of equity are not deemed to be or to have become of the essence of the contract, are also construed and have effect at law in accordance with the same rules.

[7] *Arcos Ltd.* v. *E. A. Ronaasen & Son* [1933] A.C. 470, *per* Lord Atkin at pp. 479, 480.

[8] This phrase is often used but is capable of causing confusion because the question relates not to the contract as a whole but to the particular term which has been breached: *British and Commonwealth Holdings plc.* v. *Quadrex Holdings Inc.* [1989] 1 Q.B. 842, per Browne-Wilkinson V.-C. at p. 857.

[9] *United Scientific Holdings Ltd.* v. *Burnley B.C.* [1978] A.C. 904, *per* Lord Simon at pp. 940–1. Cf. *ibid.*, *per* Lord Diplock at pp. 927–8. See further, *ante*, pp. 133, 140 (conditions).

[10] *Union Eagle Ltd.* v. *Golden Achievement Ltd.* [1997] A.C. 514. See also *Comp. Commerciale Sucres et Denrees* v. *C.Czarnikow Ltd.* [1990] 1 W.L.R. 1337, at p. 1347. But cf. Sale of Goods Act 1979, s. 10(1), *post*, p. 477 (stipulations as to time of payment in contracts for the sale of goods presumptively not of the essence).

[11] *United Scientific Holdings Ltd.* v. *Burnley B.C.* [1978] A.C. 904, at p. 942. See also *Stickney* v. *Keeble* [1915] A.C. 386, at p. 415.

[12] *Ibid.* [1978] A.C. 904, at pp. 924–5, 926–7, 940, 956–7, 964.

[13] Re-enacting the Judicature Act 1873, s. 25(7). Cf. *Raineri* v. *Miles* [1981] A.C. 1050 (damages available).

But this relief is not available in three instances:

(1) where the agreement expressly states that time is of the essence of the contract;[14]

(2) where time was not originally of the essence of the contract, but has been made so by one party, upon a breach by the other party,[15] giving notice to the party in breach requiring performance of the contract within a reasonable time;[16]

(3) where from the nature of the contract, its subject-matter, or the circumstances of the transaction, time must be taken to be of the essence of the agreement. The most common examples of this are provided by mercantile contracts, considered *infra*, but, although time is *prima facie* not of the essence in sales of land,[17] or provisions in leases, such as rent review clauses,[18] in certain cases it will be. Thus, in the case of the sale of a public-house as a going concern,[19] or of a leasehold house required for immediate occupation,[20] or of an option to acquire property,[21] or the power under a 'break' clause in a lease to determine the lease prematurely,[22] time may well be of the essence and, if so, no relief is permitted.

Mercantile contracts

In mercantile contracts, time will readily be assumed to be of the essence of the contract. For example, if a contract to purchase shares provides for payment by a fixed date, payment must be made on or before that date, and in default the seller can treat the contract as discharged.[23] Similarly, time is of the essence for payment under a time charterparty of a ship if the owner is given the right to withdraw the vessel in default of 'punctual payment' of hire.[24] However, section 10(1) of the Sale of Goods Act 1979 provides that, unless a different intention appears from the terms of the contract, stipulations as to time of *payment* are not of the essence of a contract of sale of goods.[25] Whether or not any other stipulation as to

[14] *Steedman* v. *Drinkle* [1916] 1 A.C. 275.

[15] *Behzadi* v. *Shaftesbury Hotels Ltd.* [1992] Ch. 1; *British and Commonwealth Holdings plc.* v. *Quadrex Holdings Inc.* [1989] 1 Q.B. 842, at pp. 857–8.

[16] *Stickney* v. *Keeble* (*supra*, n. 11); *Behzadi* v. *Shaftesbury Hotels Ltd.* (*supra*, n. 15); *Finkielkraut* v. *Monohan* [1949] 2 All E.R. 234. On 'reasonableness', see also *Oakdown Ltd.* v. *Berstein and Co. (a firm)* (1985) 49 P. & C.R. 282.

[17] *Webb* v. *Hughes* (1870) L.R. 10 Eq. 281; *Chancery Lane Developments Ltd.* v. *Wade's Department Stores Ltd.* (1986) 53 P. & C.R. 306, at p. 312.

[18] *United Scientific Holdings Ltd.* v. *Burnley B.C.* (*supra*, n. 12).

[19] *Tadcaster Tower Brewery Co.* v. *Wilson* [1897] 1 Ch. 705.

[20] *Tilley* v. *Thomas* (1867) L.R. 3 Ch. App. 61.

[21] *Hare* v. *Nicoll* [1966] 2 Q.B. 130.

[22] *United Scientific Holdings Ltd.* v. *Burnley B.C.* (*supra*, n. 12) at p. 929; *Coventry City Council* v. *J. Hepworth & Sons Ltd.* (1982) 46 P. & C.R. 170. But cf. *Metrolands Investments Ltd.* v. *J. H. Dewhurst Ltd.* [1986] 3 All E.R. 659.

[23] *Hare* v. *Nicoll* (*supra*, n. 21). See also *Union Eagle Ltd.* v. *Golden Achievement Ltd.* [1997] A.C. 514, *ante*, p. 476.

[24] *Scandinavian Trading Tanker Co. A.B.* v. *Flota Petrolera Ecuatoriana* [1983] 2 A.C. 694.

[25] But the unpaid seller may give notice of his intention to re-sell perishable goods and, if payment is not tendered within a reasonable time thereafter, re-sell and recover damages for any loss: *ibid.*, s. 48(3).

time is of the essence of a contract of sale of goods depends upon the terms of the contract;[26] but it is very often held to be so.[27]

Where a person is required to perform on or before a particular date, the performance may normally be carried out during the whole of that day.[28] Thus if payment of hire under a time charterparty is due on 14 June, the charterer has (regardless of banking hours) until midnight on 14/15 June to make the payment, and the shipowner cannot withdraw the ship for non-payment before that time.[29] Where no time is fixed by the contract for performance, it must be performed within a reasonable time.[30]

(b) Place of Performance

The place of performance depends upon the express or implied intentions of the parties, judged from the nature of the contract and the surrounding circumstances. If no place of performance is specified even by implication, in a contract for the sale of goods it is basically the duty of the buyer to collect the goods rather than the seller to send them,[31] and in contracts to pay money it is basically the debtor's duty to pay the creditor at the creditor's place of business or residence.[32]

II. Performance

(a) Payment

One mode of complete performance of an obligation is by payment.

Mode of payment

Payment normally means payment in cash. The parties may, however, agree, expressly or impliedly, that payment may be made in some other manner, and, in the absence of any express stipulation, the method of payment may be determined by course of dealing between the parties or by trade custom. If the parties are dealing together on a regular basis, it may be agreed that, at periodic intervals, sums due from one party shall be set off against sums due to that party by the other, and such set-off is then equivalent to an actual cash payment.[33]

[26] Sale of Goods Act 1979, s. 10(2). But see *Hartley* v. *Hymans* [1920] 3 K.B. 475, at p. 483.

[27] *Reuter* v. *Sala* (1879) 4 C.P.D. 239, at pp. 246, 249; *Hartley* v. *Hymans* (*supra*, n. 26), at p. 484; *Finagrain S.A. Geneva* v. *P. Kruse Hamburg* [1976] 2 Lloyd's Rep. 508; *United Scientific Holdings Ltd.* v. *Burnley B.C.* [1978] A.C. 904, at pp. 924, 937, 944, 950, 958; *Bunge Cpn.* v. *Tradax Export S.A.* [1981] 1 W.L.R. 711 (*ante*, p. 141); *Comp. Commerciale Sucres et Denrees* v. *C.Czarnikow Ltd.* [1990] 1 W.L.R. 1337, at p. 1347.

[28] Contrast Sale of Goods Act 1979, s. 29(5) (demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour).

[29] *Afovos Shipping Co. S.A.* v. *R. Pagnan & Filii* [1983] 1 W.L.R. 195.

[30] *Postlethwaite* v. *Freeland* (1880) 5 App. Cas. 599; Sale of Goods Act 1979, s. 29(3).

[31] Sale of Goods Act 1979, ss. 29(1), (2).

[32] *Charles Duval & Co. Ltd.* v. *Gans* [1904] 2 K.B. 685; *Fowler* v. *Midland Electricity Corporation for Power Distribution Ltd.* [1917] 1 Ch. 656 (debenture). On payment through the banking system, see *post*, p. 479.

[33] *Larocque* v. *Beauchemin* [1897] A.C. 358, at pp. 365–6.

Interbank transfers

Nowadays payment is frequently made by use of the banking system. The debtor instructs its bank to pay a specified sum to the account of the creditor at another bank. The transfer may be effected by letter, telegram, or telex from the one bank to the other, or even electronically by computer. Such payment, when made, is 'the equivalent of cash, or as good as cash' for the purposes of a contract that requires payment in cash.[34] But difficulties can arise. If payment has to be made by a certain date, does the receipt of the payment order by the creditor's bank constitute payment? Or is payment only made when the order has been processed and the amount credited to the creditor's account? In *Mardorf Peach & Co. Ltd.* v. *Attica Sea Carriers Corporation of Liberia*,[35] where the evidence was that the system of processing might take up to 24 hours before the account was credited, members of the House of Lords expressed differing opinions. Lord Salmon[36] and Lord Russell[37] were inclined to the view that, since a payment order was as between banks the equivalent of cash, it should suffice for punctual payment that such cash equivalent was tendered in due time to the creditor's bank to be credited to its account.[38] But Lord Fraser[39] was of the opinion that payment would not take place until the creditor's bank acted on the request in the order and credited the amount to the creditor's account. However, in *A/S Awilco of Oslo* v. *Fulvia S.p.A. di Navigazione of Cagliari (The Chikuma)*:[40]

The respondents chartered the appellants' vessel *Chikuma*. Failing punctual payment of hire in cash in American currency monthly in advance, the appellants were entitled to withdraw the vessel from service. Payment of one instalment of hire fell due on 22 January. On 21 January the respondents instructed their Norwegian bank to make the required payment by credit transfer. By a telex message before noon on the 22nd there was a credit transfer to the appellants' bank in Italy of the sum due, which the bank credited on the same day to the appellants' account. By Italian banking law, however, although the appellants would have immediate access to the money, interest would not start to be paid by the bank until 26 January, and if the appellants had withdrawn the sum credited they would probably have incurred liability to the bank to pay interest for those 4 days. The appellants withdrew the vessel for default in punctual payment.

The House of Lords upheld their right to do so. The payment on 22 January was not equivalent to cash for it could not be used to earn interest, e.g. by immediate transfer to a deposit account. The fact that the appellants could withdraw the money, but subject to payment of interest, did not make the payment equivalent to cash, since the arrangement amounted in substance to an overdraft facility.

Negotiable instrument or documentary credit as payment

A negotiable instrument,[41] such as a bill of exchange, cheque, or promissory note may, by agreement, be given and accepted in payment. But the presumption

[34] *A/S Awilco of Oslo* v. *Fulvia S.p.A. di Navigazione of Cagliari (The Chikuma)* [1981] 1 W.L.R. 314, at p. 320.

[35] [1977] A.C. 850. [36] At p. 880. [37] At p. 889.

[38] In the case of a transfer between branches of the same bank, it was held in *Momm* v. *Barclays Bank International Ltd.* [1977] Q.B. 79 that payment was effected when the staff of the bank received the debtor's instructions and set in motion the bank's internal procedures for crediting the creditor's account.

[39] At p. 885. [40] [1981] 1 W.L.R. 314 (criticized by Mann (1981) 97 L.Q.R. 379).

[41] See *ante*, pp. 462–9.

where a negotiable instrument is taken in lieu of a money payment is that the parties intend it to be a conditional discharge only:[42]

Suppose that A, being owed a sum of money by B, agrees to take a cheque in payment of the sum due.

So far, B has satisfied the debt.[43] But if the cheque is dishonoured when presented for payment, A's right to sue on the debt revives and A's original rights are restored.[44] Exceptionally, however, a negotiable instrument may be given and accepted as absolute payment. In such a case, in the example given above, B's debt would then be wholly discharged. A would have to rely upon the rights conferred by the cheque, and, if the cheque is dishonoured, A must sue on it, and cannot revert to the original claim for the debt.[45] Similar principles apply to payment by documentary credit.[46]

Payment by credit or charge card

By contrast, payment by a credit or charge card is an unconditional and absolute payment unless the contract provides otherwise. So, the liability of a cardholder who has paid for goods or services in this way is discharged and the cardholder will not be liable to the seller or supplier if the credit or charge card company fails to pay the seller or supplier the amount charged to the card.[47]

Duty to pay

No request or demand for payment is normally necessary[48] unless the contract so provides.[49]

Receipts

There is a common, but mistaken, belief that payment of a debt can only be proved by the production of a written receipt. But payment may be proved by any evidence,[50] and a receipt is only *prima facie* evidence that a debt has been paid.[51]

(b) Vicarious Performance

There may be circumstances which make it permissible for a contracting party to perform his side of the contract by getting someone else to do in a satisfactory fashion the work for which the contract provides.[52] A contract may be vicariously

[42] *Re Romer and Haslam* [1893] 2 Q.B. 286, at pp. 296, 300, 303.
[43] *Sayer* v. *Wagstaff* (1844) 5 Beav. 415, at p. 423; *Hadley & Co. Ltd.* v. *Hadley* [1898] 2 Ch. 680; *Bolt & Nut Co. (Tipton) Ltd.* v. *Rowlands, Nicholls & Co. Ltd.* [1964] 2 Q.B. 10.
[44] *Sayer* v. *Wagstaff* (*supra*, n. 43); *Re Romer and Haslam* (*supra*, n. 42).
[45] *Sard* v. *Rhodes* (1836) 1 M. & W. 153; *Sibree* v. *Tripp* (1846) 15 M. & W. 23; *Re Romer and Haslam* (*supra*, n. 42), at pp. 296, 300.
[46] *W.J. Alan & Co. Ltd.* v. *El Nasr Export and Import Co.* [1972] 2 Q.B. 189, at pp. 209–12; *Re Charge Card Services Ltd.* [1989] Ch. 497, at p. 511. On documentary credits, see further, *ante*, p. 422.
[47] *Re Charge Card Services Ltd.* [1989] Ch 497; *Customs & Excise Commissioners* v. *Diners Club Ltd.* [1989] 1 W.L.R. 1196.
[48] *Bell & Co.* v. *Antwerp, London & Brazil Line* [1891] 1 Q.B. 103, *per* Lord Esher M.R. at p. 107; *Carne* v. *Debono* [1988] 1 W.L.R. 1107, at p. 1112.
[49] *Libyan Arab Foreign Bank Co.* v. *Bankers Trust Co.* [1989] 1 Q.B. 728, at pp. 748–49. On the need for notice by a tenant of want of repair before landlord's obligation to repair is due, see *Calebar Properties Ltd.* v. *Stitcher* [1984] 1 W.L.R. 287, at p. 298; *British Telecommunications plc.* v. *Sun Life Assurance Society plc.* [1996] Ch. 69.
[50] *Eyles* v. *Ellis* (1827) 4 Bing. 112. See also Cheques Act 1957, s. 3.
[51] *Wilson* v. *Keating* (1859) 27 Beav. 121.
[52] See *ante*, p. 461, for the distinction between vicarious performance and assignment.

performed where this is expressly permitted by the contract,[53] or, from the terms of the contract, its subject-matter, and surrounding circumstances, it may properly be inferred that it is a matter of indifference whether the performance is that of the contracting party or his nominee. Thus, it has been held that a contract to let out railway waggons and keep them in repair could be vicariously performed.[54] The repairs were 'a rough description of work which ordinary workmen conversant with the business would be perfectly able to execute'.[55] If, however, the person employed has been selected with reference to his individual skill, competency, or other personal qualification, he is not entitled to sub-contract the performance of the contract to another. Thus it has been held that personal care and skill is an ingredient in contracts by a warehouseman for the storage of furniture,[56] by a publishing firm for the publication of a book,[57] and by an architect in the design of a building.[58] Such contracts cannot be vicariously performed without the consent of the promisee. Contracts of service are normally personal to the contracting parties.[59] Furthermore, payment of a debt which is made by a person other than the debtor or the debtor's agent will not be effective to discharge the debt.[60]

Even where the contract may not in principle be vicariously performed, if the promisee in fact agrees to it being performed by a non-party and accepts such performance, the contract will be discharged.[61]

(c) Alternative Modes of Performance[62]

A contract can provide for alternative modes of performance in one of two ways. First, it may provide for performance in a particular way, for instance a shipper's obligation to load a cargo of wheat, but give that party the option to perform in an alternative way, for instance, to change to a cargo of barley. Secondly, it may permit one party to choose[63] between alternative modes of performance without specifying one as the primary mode, for instance, a shipper's obligation to load a full cargo in the months of September or October.

Contract option

In the first situation, once the option is exercised, the contractual obligation is varied; in the example above, the contract ceases to be one to load wheat and becomes one to load barley. The option must be exercised within a reasonable

[53] e.g. *Société Commerciale de Reassurance* v. *E.R.A.S. International Ltd.* [1992] 1 Lloyd's Rep. 570, at p. 596.

[54] *British Waggon Co. Ltd.* v. *Lea & Co.* (1880) 5 Q.B.D. 149.

[55] *Ibid.*, *per* Cockburn C.J. at p. 153.

[56] *Edwards* v. *Newland & Co.* [1950] 2 K.B. 534.

[57] *Griffith* v. *Tower Publishing Co. Ltd.* [1897] 1 Ch. 21.

[58] *Moresk Cleaners Ltd.* v. *Hicks* [1966] 2 Lloyd's Rep. 338.

[59] *Nokes* v. *Doncaster Amalgamated Collieries Ltd.* [1940] A.C. 1014 (rights). But note the Transfer of Undertakings Regulations 1981 (S.I. 1981 No. 1794), reg. 5(1), *ante*, p. 460.

[60] See *Belshaw* v. *Bush* (1851) 11 C.B. 191; *Walter* v. *James* (1871) L.R. 6 Ex. 124; *Owen* v. *Tate* [1976] 1 Q.B. 402. See generally Beatson and Birks (1976) 91 L.Q.R. 188; Beatson, *The Use and Abuse of Unjust Enrichment* (1991), ch. 7; Friedmann (1983) 99 L.Q.R. 534.

[61] *Belshaw* v. *Bush* (*supra*, n. 60); *Hirachand Punamchand* v. *Temple* [1911] 2 K.B. 483, *ante*, p. 110.

[62] See generally Treitel, *Frustration and Force Majeure* (1994), ch. 10.

[63] If the contract does not specify which party has the option, it will be the one who has to do the first act: *Reed* v. *Kilburn Co-op* (1875) L.R. 10 Q.B.D. 264.

time and this must be communicated to the other party;[64] if it is not exercised it is lost. But, in considering whether to exercise the option, the promisee is not generally bound to consider the interests of the other party.[65] For example, if the primary mode of performance becomes impossible, the option-holder is not obliged to exercise it in order to avoid the contract being frustrated.[66] But an attempt to rely on the exercise of such an option to render a contractual performance substantially different from that which was reasonably expected may be ineffective against a consumer or a party dealing on the other's written standard terms of business.[67]

Performance option

In the second situation there is a truly alternative obligation. The promisor is obliged to perform in any of the authorized modes. If, prior to a choice being made, one mode ceases to be available, that simply narrows the scope of contractually authorized performance.[68] So, in the example given above, if access to the loading port is impossible due to strikes or bad weather during September, that does not affect the obligation to ship a full cargo; the shipper remains liable to load a full cargo in October, even if the shipper had planned to do so in September. But once a party chooses the alternative to be performed, that choice binds.[69]

(d) Right to Cure Bad or Incomplete Performance

We have seen that the common law treats a serious misperformance, such as incomplete delivery or delivery of goods that are not of satisfactory quality, as the standard example of a breach entitling the innocent party to treat the contract as discharged.[70] But if a bad or incomplete performance is tendered before the time of performance has arrived, it does not generally prevent the promisor making another tender of performance within time that does comply. The promisee would have to accept this fresh tender unless the first amounted to a repudiation which the promisee had acted upon and terminated the contract.[71] One situation

[64] *Reardon Smith Line Ltd.* v. *Ministry of Agriculture, Fisheries & Food* [1963] A.C. 691, at p. 731.

[65] *Ibid.*, at pp. 719–20, 730. See also *Thompson* v. *ADSA-MFI Group Plc.* [1988] 1 Ch. 241, at pp. 251, 266–7 (no general principle that a party cannot take advantage of own acts to avoid obligations under the contract).

[66] On frustration, see further Chapter 14.

[67] Unfair Terms in Contracts Act 1977, s. 3(2)(b); Unfair Terms in Consumer Contracts Regulations 1994 (S.I. 1994 No. 3159), Sched. 3, para. 1(b), (c), (h), (l). See generally *ante*, pp. 189, 197.

[68] *Reardon Smith Line Ltd.* v. *Ministry of Agriculture, Fisheries & Food* [1963] A.C. 691, at p. 717, 720, 730; *Atlantic Lines & Navigation Co. Ltd.* v. *Didymi Corp., (The Didymi)* [1984] 1 Lloyd's Rep. 583, at p. 587; *Libyan Arab Foreign Bank* v. *Bankers Trust Co.* [1989] Q.B. 728, at p. 766; *Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep 1, at p. 9.

[69] *Schneider* v. *Foster* (1857) 2 H. & N. 4; *Gath* v. *Lees* (1865) 3 H. & C. 558. But authority (*Brown* v. *Royal Insurance Co.* (1859) 1 E. & E. 853) suggesting the party remains bound even where it is no longer possible to perform the contract in that way is doubtful since it predates the development of the doctrine of frustration, on which see *post*, Chapter 14.

[70] *Ante*, pp. 133, 138 (conditions and innominate terms). See further *post*, Chapter 15.

[71] *Borrowman, Phillips & Co.* v. *Free & Hollins* (1878) 4 Q.B.D. 500; *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corporation of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391 at p. 399.

in which the defective performance will be treated as a repudiation is where the defective performance has destroyed the confidence of the promisee.[72]

III. Attempted and Partial Performance

(a) Tender

Tender is of two kinds

Tender is attempted performance; and the word is applied to attempted performance of two kinds, dissimilar in their results. It is applied to a performance of a promise to do something, and of a promise to pay something. In each case the performance is prevented by the act of the party for whose benefit it is to take place.

Tender of acts

Where one party is obliged by the contract to perform a promise to do something, but the other party refuses to accept the performance when tendered, the promisor is discharged from performing that obligation and may sue for damages. In addition, if the promisee commences an action against the promisor for failure to perform the obligation, the promisor is entitled to set up the refusal to accept the tender as a defence. [73] The promisor will not, however, be treated as having performed the obligation. If the refusal to accept the tender amounts to a repudiation of the contract the promisor can elect to terminate the contract and sue for damages.[74] Although such a refusal does not always have this effect,[75] if it is absolute and unqualified it entitles the promisor to elect to be discharged. For example, the Sale of Goods Act 1979, section 37, provides that when the seller is ready and willing to deliver the goods and requests the buyer to take delivery, the buyer must do so within a reasonable time or become liable for any loss occasioned to the seller by the buyer's neglect. But this does not affect the rights of the seller where the non-acceptance amounts to a repudiation of the contract.

Tender of payment

Where, however, the performance due consists of the payment of a sum of money, a tender by the debtor, though refused by the creditor, does not discharge the debtor from the obligation to pay the debt. The debtor is bound in the first instance 'to find out the creditor and pay him the debt when due';[76] if the creditor will not take payment when tendered, the debtor must nevertheless continue to be ready and willing to pay the debt. Then, the debtor, if sued, can plead that a tender had been made, but must pay the money into Court.[77] If the debtor proves this plea, the creditor gets nothing but the money originally tendered, i.e. no interest or damages, while the debtor gets judgment for the costs of the action, and so is placed in as good a position as at the time of the tender.

[72] On repudiation, see further *post*, Chapter 15.
[73] *Startup* v. *Macdonald* (1843) 6 M. & G. 593.
[74] *Ibid.*
[75] See e.g. the Sale of Goods Act 1979, s. 31(2), *post*, p. 539.
[76] *Walton* v. *Mascall* (1844) 13 M. & W. 452, *per* Parke B. at p. 458.
[77] R.S.C., Ord. 18, r. 16; Ord. 22.

Tender of payment, to be a valid performance to this extent, must observe exactly any special terms which the contract may contain as to time,[78] place, and mode of payment. The nineteenth century authorities further prescribe extremely strict requirements for a valid tender: it must be unconditional and it must be in legal currency.[79] There must be an offer of money produced and accessible to the creditor, not necessarily of the exact sum, but of such a sum as will allow the creditor to take exactly what is due without being called upon to give change.[80] Finally, it was necessary for the cash to be produced to the creditor in person. 'Great importance', it was said,[81] 'was attached to the production of money, as the sight of it might tempt the creditor to yield'. But these requirements may be dispensed with expressly or impliedly by the creditor,[82] and the requirement of payment in cash must be interpreted against the background of modern commercial practice. In commercial transactions, it would appear that any commercially recognized method of transferring funds, the result of which is to give the transferee the immediate use of the funds transferred, will nowadays suffice.[83]

Early tender

A promisee need not, moreover, accept an early tender, but, as we have seen, if a bad tender is made before the time of performance has arrived, it does not generally prevent the promisor making another tender within time that does comply with the contract.[84]

(b) Partial Performance of an Entire Obligation[85]

Since the performance of a contractual obligation must be precise and exact, where one party's performance is made conditional on complete and entire performance by the other party, at common law[86] the general rule is that the other can recover nothing for incomplete performance. It is immaterial how the failure to effect complete performance comes about. It may be due to a deliberate abandonment of the contract, to a negligent act or omission, or to a simple misfortune occurring without any fault. In *Cutter* v. *Powell*,[87] for example:

[78] In the absence of such terms a tender of goods must be made at a reasonable hour: Sale of Goods Act 1979, s. 29(5).

[79] The Currency and Bank Notes Act 1954; the Coinage Act 1971 and the Currency Act 1983 define legal tender.

[80] *Betterbee* v. *Davis* (1811) 3 Camp. 70.

[81] *Finch* v. *Brook* (1834) 1 Bing. N.C. 253, *per* Vaughan J. at p. 257.

[82] *Farquharson* v. *Pearl Assurance Co. Ltd.* [1937] 3 All E.R. 124.

[83] *Tenax Steamship Co. Ltd.* v. *The Brimnes (Owners)* [1975] 1 Q.B. 929, at p. 963; *Mardorf Peach & Co. Ltd.* v. *Attica Sea Carriers Cpn. of Liberia* [1977] A.C. 850, at pp. 880, 885, 889; see *ante*, p. 479; *Libyan Arab Foreign Bank Co.* v. *Bankers Trust Co.* [1989] 1 Q.B. 728, at pp. 749–50.

[84] *Ante*, p. 482.

[85] See Williams (1941) 57 L.Q.R. 373; Treitel (1967) 30 M.L.R. 139, at p. 141 ff; Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), Mr Brian Davenport Q.C. dissented and the government rejected the report: 19th Annual Report (1983–84) Law Com. No. 140, § 2.11.

[86] For statutory exceptions, see Apportionment Act 1870 (rents, annuities, dividends, and other periodic payments in the nature of income *prima facie* considered as accruing from day to day); Law Reform (Frustrated Contracts) Act 1943, *post*, p. 528.

[87] (1795) 6 Term R. 320; Stoljar (1956) 34 Can. Bar Rev. 288. But the effect of this decision has been alleviated by statute: see the Law Reform (Frustrated Contracts) Act 1943; *post*, p. 529, and what is now the Merchant Shipping Act 1995, s. 38.

A seaman was engaged to act as second mate on a voyage from Jamaica to Liverpool. He was to be paid 30 guineas, almost four times the going rate, in a single payment upon completion of the voyage. Nineteen days out from Liverpool, when the voyage was nearly completed, he died. His widow sued to recover a proportion of the agreed sum.

Her action failed. The seaman's obligation was construed as an entire contract or, more accurately, an entire obligation, that is to say, if the voyage was completed he was to receive the stipulated sum, but, if it was not, he was to receive nothing. As Sir George Jessel M.R. said; 'if a shoemaker agrees to make a pair of shoes, he cannot offer you one shoe and ask you to pay half the price'.[88]

Entire & divisible obligations

The reason it is inaccurate to refer to 'entire' contracts, is that it is very unlikely indeed that complete performance of each and every obligation in a contract by one party is a condition precedent to the liability of the other. The contract may, for example, be a complex one, composed of a number of undertakings differing in character or importance; or it may be a promise to do a number of successive acts; or to do a single act which can be partly or defectively performed.[89] Very often a contract may be entire as to one aspect but 'divisible' or 'severable' (in the sense that the right to payment accrues incrementally as the performance is rendered) as to another. For example, in *Cutter* v. *Powell*, although the seaman's obligation to complete the voyage was entire, his obligation to exercise reasonable care in the performance of his duty was unlikely to be entire, so that, had he completed the voyage, but had performed his duty badly, it seems he would have been able to recover his wages, subject to a claim against him for poor work.[90] Again, in contracts for the carriage of goods by sea, whereas the obligation to deliver the cargo to the stipulated port is entire, so that no freight at all is payable if delivery is made at an intermediate port,[91] the obligations with respect to the quantity or condition of the cargo are not, so that, if half the cargo is delivered, half the freight is payable,[92] and if all the cargo arrives damaged (but still of the same commercial description), freight will be payable subject to a counterclaim against the carrier for damages.[93]

Because the consequences can be draconian, Courts are reluctant to construe an obligation as 'entire'.[94] But where the payment for the performance was to be a lump sum to be paid after completion they have generally done so, so that the

[88] *Re Hall & Barker* (1878) 9 Ch. D. 538, at p. 545.

[89] See the discusion in *Baltic Shiping Co.* v. *Dillon* (1992–93) 176 C.L.R. 344, at pp. 350, 384 (High Court of Australia).

[90] Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), § 2.12, citing Somervell L.J. in *Hoenig* v. *Isaacs* [1952] 2 All E.R. 176, at p. 178.

[91] *St. Enoch S.S. Co. Ltd.* v. *Phosphate Mining Co.* [1916] 2 K.B. 624; *Metcalfe* v. *Brittania Iron Works Co.* (1877) 2 Q.B.D. 423.

[92] *Ritchie* v. *Atkinson* (1808) 10 East 295, at 530. But where there is a stipulation for lump freight or freight to be computed on loading, the carrier will be entitled to full freight: *Aires Tanker Corp.* v. *Total Transport Ltd (The Aires)* [1977] 1 W.L.R. 185; *Colonial Bank* v. *European Grain & Shipping Ltd. (The Dominique)* [1989] A.C. 1056. See further *Scrutton on Charterparties*, 20th edn. (1996) art. 166.

[93] *Dakin* v. *Oxley* (1864) 15 C.B.(N.S.) 646, at p. 667. See further *Scrutton on Charterparties*, (*supra*, n. 92).

[94] *Button* v. *Thompson* (1869) L.R. 4 C.P. 330, at p. 342.

promisee cannot recover anything until the work is completely executed.[95] Thus, apart from *Cutter* v. *Powell*, this construction has been put on obligations by a builder to build two houses and stables for a client,[96] and by a plumber to supply and install a combined central heating and hot water system in a private house.[97]

Rationale

The general rule has been justified in a number of ways.[98] First, the recipient of the performance has not contracted to buy part of the performance for a proportionate part of the price and should not be compelled to pay for performance that is different to that agreed, and, in some cases, insisted upon.[99] Where, like the seaman in *Cutter* v. *Powell*, the performer is to be paid significantly more than the going rate for the job, it can also be said that he has accepted the risk of incomplete or defective performance. Secondly, the rule holds people to their contracts and gives them a strong incentive to complete.[100] It is particularly important where there is inequality of bargaining power or scope for opportunistic behaviour, as there often is in contracts for small building works on private houses. It is all too common for a builder not to complete one job before moving on to the next, and the rule enables the householder to withhold all payment unless the job is finished.[101] Thirdly, the losses the innocent party suffers may be ones for which the law finds it difficult to compensate.[102]

Critique

The principle precluding recovery, however, if rigorously applied, could be productive of great injustice. It is hard to contend, for example, that even the most trivial defect of workmanship in the decoration of a flat,[103] or some momentary slip or inefficiency on the part of an employee,[104] should entitle the 'injured' party to refuse all payment save where the injured party has made it absolutely clear that the trivial defect or breach will have this effect.[105] It should not, accordingly, be inferred, as it has been,[106] that such penal consequences follow from the mere postponement of payment of a lump sum by one party until after the other party has completely performed.[107] Such postponement may be prompted by a number

[95] *Appleby* v. *Myers* (1867) L.R. 2 C.P. 651 at pp. 660–1, *The Madras* [1898] P. 90, and *Sumpter* v. *Hedges* [1898] 1 Q.B. 190, *post*, p. 488, appear to adopt this as a general rule. For criticism, see *post*.

[96] *Sumpter* v. *Hedges* (*supra*, n. 95).

[97] *Bolton* v. *Mahadeva* [1972] 1 W.L.R. 1009.

[98] See generally, Waddams in Reiter and Swan, eds., *Studies in Contract Law* (1980) p. 163 ff; Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), §§ 2.24–2.26.

[99] *Wiluszynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493; *Miles* v. *Wakefield M.B.C.* [1987] A.C. 539, *post*, p. 489; *British Telecommunications plc* v. *Ticehurst* [1992] I.C.R. 383.

[100] *Munro* v. *Butt* (1858) 8 E. & B. 735, at p. 754; Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), § 2.25.

[101] *Ibid.*, p. 37 (Mr B. J. Davenport Q.C.'s dissent). A builder may protect itself by requiring payments before the completion of performance, which (*post*, pp. 605, 608) will generally be irrecoverable. Note that in contracts for the sale of goods, consumers have wider power of rejection than others: Sale of Goods Act 1979, s. 30(2A), *infra*, n. 116.

[102] As in the case of non-pecuniary loss (*Vigers* v. *Cook* [1919] 2 K.B. 475; and see *post*, p. 561) or loss to a third party (*ante*, p. 412).

[103] *Hoenig* v. *Isaacs* [1952] 2 All E.R. 176 (contract price £750, defects remedied for £55).

[104] *Ibid.*, at p. 178.

[105] *Miles* v. *Wakefield M.B.C.* [1987] A.C. 539 at pp. 551, 561, 568; *Wiluszynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493 at pp. 500, 503.

[106] *Supra*, n. 95.

[107] Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), §§ 2.11, 2.27 and 2.67; Williams (1941) 57 L.Q.R. 373, at pp. 389 ff.

of other reasons, including easing the 'cash-flow' of the party who will have to pay, and protecting that party from the risk that the other may become insolvent. Moreover, the application of the principle would often result in the unjust enrichment of the injured party if that party could retain the benefit of the incomplete performance without the necessity of paying for it. A general acceptance of the risk of incomplete performance by the part performer may not extend to a situation where the other party is incontrovertibly benefited, and a restitutionary remedy does not necessarily constitute a redistribution of risks allocated by the contract.[108]

The unpalatable consequences that can follow have led Courts to seek to avoid construing an obligation as entire. Broadly speaking this can properly be done in two situations; where the injured party has *accepted* the partial performance, and, although this is not so clearly established, where the part performer can establish that the services rendered or the work done has *incontrovertibly benefited* the other party so as to give rise to a claim in restitution. The underdevelopment of the law of restitution until recently and the tendency to construe an obligation as 'entire' simply because the contract provides for a lump sum has, however, also led to authority favouring a remedy in a third situation; where the part performer has *substantially performed* the 'entire' obligation.

Doctrine of 'substantial performance'

Where the contract is *substantially* performed, there is authority that the injured party is not discharged from the obligation to pay, but is protected by a counterclaim or set-off for any loss which may have been sustained by reason of the incomplete or defective performance.[109] A Court will hold a contract to have been substantially performed if the actual performance falls not far short of the required performance, and if the cost of remedying the defects is not too great in amount in comparison with the contract price.[110] In *Dakin (H.) & Co. Ltd.* v. *Lee*:[111]

The plaintiffs were builders who had contracted to execute certain repairs to the defendant's premises for £1,500. They carried out a substantial part of the contract, but failed to perform it exactly in three unimportant respects (which could have been rectified at a cost of £80). The official referee appointed by the parties held that the plaintiffs were consequently not entitled to recover any part of the contract price.

On appeal, it was held that this finding was erroneous. The contract had been substantially, if not precisely, performed. Pickford L.J. stated that the fact that the

[108] Although it *might* do so; see Beatson, *The Use and Abuse of Unjust Enrichment* (1991), ch. 4, and *Wiluszynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493, *post*, p. 489.

[109] *Boone* v. *Eyre* (1779) 1 H. Bl. 273; *Broom* v. *Davis* (1794) 7 East 480n; *Bolton* v. *Mahadeva* (*supra*, n. 97), at p. 1015; *Sim* v. *Rotherham Metropolitan Borough Council* [1987] Ch. 216, at p. 253; *Wiluszynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493, at p. 499; *Williams* v. *Roffey Bros. & Nicholls (Contractors) Ltd.* [1991] 1 Q.B. 1, at pp. 8–10, 17.

[110] Compare *Hoenig* v. *Isaacs* [1952] 2 All E.R. 176 (cost of remedying defects was 7.3% of contract price) and *Bolton* v. *Mahadeva* [1972] 1 W.L.R. 1009 (no substantial performance where cost of remedying defects was 31% of contract price).

[111] [1916] 1 K.B. 566, at p. 579. Note Greer L.J.'s criticism in *Eshelby* v. *Federated European Bank Ltd.* [1932] 1 K.B. 423, at p. 431 and cf. *Vigers* v. *Cook* [1919] 2 K.B. 475; *Bolton* v. *Mahadeva* [1972] 1 W.L.R. 1009.

work was done badly did not mean that it had not been performed at all.[112] The plaintiff was accordingly entitled to recover the price less a reduction for the breach. In the USA a more flexible approach has been taken whereby the Court may look at the quality of performance so that, even if the cost of compliance is great, there may still be substantial performance if the work that is done is of the same quality as that contracted for,[113] and there are indications that this approach may be taken in English law.[114]

Since the basis of the rules governing entire obligations is that the parties have made *complete* and *precise* performance by one party a condition to entitlement to performance by the other, it is submitted that it is logically difficult to justify applying a principle of substantial performance to such obligations. To do so is to set aside the contractual allocation of risks. But the cases which have construed an obligation as entire simply because the contract provided for a lump sum to be paid after the completion of performance provide some pragmatic justification, since this fact alone may not truly indicate that the risks of any trivial incompleteness in performance are to lie with the part performer. On principle, however, the correct approach is greater caution in the categorization of an obligation as entire, and development of the emerging restitutionary principles to which we now turn.

Injured party may accept partial performance

A party who renders incomplete performance of an entire contract may nevertheless claim remuneration where the other party has freely accepted such partial performance or otherwise waived the need for complete performance. So, if the customer of Sir George Jessel's shoemaker had accepted one shoe he would have been obliged to pay for the shoe he accepted.[115] In the case of the sale of goods, section 30(1) of the Sale of Goods Act 1979 provides:

> Where the seller delivers to the buyer a quantity of goods less than he contracted to sell, the buyer may reject them, but if the buyer accepts the goods so delivered he must pay for them at the contract rate.[116]

In most cases, such a claim will arise upon a *quantum meruit*, that is to say, for a reasonable sum in respect of the services rendered or the work done by the partial performance. But it will only do so if the party not in default has the option whether to accept or to refuse the partial performance. Thus in *Sumpter* v. *Hedges*:[117]

> The plaintiff agreed to erect two houses and stables on the defendant's land for £565. He failed to complete the contract. The defendant thereupon completed the buildings him-

[112] This suggests that on true analysis the obligation concerning the *quality* of the work may not have been entire. See Williams (1941) 57 L.Q.R. 373, at pp. 386–7, and see *ante*, p. 485.

[113] *Jacob & Youngs Inc* v. *Kent*, 129 NE 889 (1921). The New York Court of Appeals held that a builder who failed to use galvanised piping of 'Reading manufacture' for the plumbing in a building had substantially performed the contract; the pipes in fact used were of the same quality as those specified and the defect could only be remedied by demolishing a substantial part of the building.

[114] In *Ruxley Electronics Ltd.* v. *Forsyth* [1996] 1 A.C. 344, *post*, p. 566 (not involving an entire obligation, *ibid.*, p. 363), *Jacob & Youngs Inc* v. *Kent*, (*supra*, n. 113) was approved in a slightly different context.

[115] *Ante*, p. 37. See also *Baltic Shipping Co.* v. *Dillon* (1992–93) 176 C.L.R. 344, at p. 378.

[116] But a non-consumer may not reject where the shortfall is so slight that it would be unreasonable for him to do so: 1979 Act, s. 30(2A), inserted by the Sale and Supply of Goods Act 1994.

[117] [1898] 1 Q.B. 673. See also *Munro* v. *Butt* (1858) 8 E. & B. 738; *Forman & Co. Proprietary Ltd.* v. *Ship 'Liddesdale'* [1900] A.C. 190.

self, using the materials left on the site by the plaintiff. The plaintiff brought an action to recover the value of the work done before he abandoned the contract, and also claimed in respect of the building materials used.

It was held that he was entitled to recover the value of the materials left which the defendant used, for the defendant had the choice whether or not to use these to complete the building. But he could not recover for the work he had done, for the defendant had no option but to accept the partly-erected building which was on his land. Similarly, an employer who told employees working 'to rule' and not carrying out part of their contractual services not to come to work at all unless they were prepared to work normally, was not held to have 'accepted' the partial performance simply because it did not send them home; '[a] person is not treated by the law as having chosen to accept that which is forced down his throat despite his objections'.[118]

Originally the basis of this liability was said to be that acceptance of partial performance implies a fresh agreement between the parties to pay for the work already done or goods supplied[119] but the implication of such a contract can be fictional, and, in such cases, it is better to regard the obligation to pay as restitutionary arising from the operation of principles of unjust enrichment.[120]

Incontrovertible benefit

As the failure of the claim in respect of the partially-erected building in *Sumpter* v. *Hedges* shows, the mere fact that a person appears to have benefited from the part performance of an entire obligation, has not generally sufficed to ground a claim for recompense.[121] But, where it can be shown that the recipient of the part performance has gained a readily realizable financial benefit or has been saved expense which he must have incurred, there is some support for the view that the part performer would be entitled to reasonable remuneration[122] save where the parties have made it clear that the risk of non-completion is to be borne by the part performer even where there is such a benefit.[123]

[118] *Wiluszynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493, *per* Nicholls L.J. at p. 504, but see Mead (1990) 106 L.Q.R. 192. In *Miles* v. *Wakefield M.B.C.* [1987] A.C. 539, at pp. 553, 563, two of their Lordships suggested that, if the employer has not made it clear that reduced or inefficient work will not be accepted, the employee will be entitled to a reasonable sum for that reduced work. But, as the contract had not been discharged, there are formidable difficulties with any restitutionary claim: *post*, p. 612. Cf. Lord Bridge's doubts, *ibid.*, at p. 552. Lord Brandon and Lord Oliver reserved their opinions.

[119] *Sumpter* v. *Hedges* (*supra*, n. 95); *Steele* v. *Tardiani* (1946) 72 C.L.R. 386, at pp. 394, 402 (High Court of Australia).

[120] *Baltic Shipping Co.* v. *Dillon* (1992–93) 176 C.L.R. 344 at pp. 374, 385 (High Court of Australia). For the recognition of unjust enrichment in England, see *Lipkin Gorman* v. *Karpnale* [1991] A.C. 548, *ante*, p. 21.

[121] See also *Bolton* v. *Mahadeva* [1972] 1 W.L.R. 1009.

[122] *Hain S.S. Co. Ltd.* v. *Tate & Lyle Ltd.* (1936) 41 Com. Cas 350, *per* Lord Atkin, Lord Wright M.R., and Lord Maugham, at pp. 358, 367–8, 373; *Procter & Gamble Philippine Manufacturing Corp.* v. *Peter Cremer GmbH & Co. (The Manilla)* [1988] 3 All E.R. 843, at p. 855; *Miles* v. *Wakefield M.B.C.* (*supra*, n. 118) at pp. 553, 563. See also *Britton* v. *Turner* 6 N.H. 481; 26 Am. Dec 713 (1834) (New Hampshire); Goff and Jones, *The Law of Restitution* 4th edn. (1994), pp. 442–7; Burrows, *The Law of Restitution* (1993), pp. 279–80; Birks, *An Introduction to the Law of Restitution* (1985), pp. 239–41. Cf. Beatson (1981) 98 L.Q.R. 389 at pp. 411, 413.

[123] Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), §§ 2.66–2.69, 2.73, and see *supra*, n. 118.

13

Discharge by Agreement

I. Introduction

Forms of discharge by agreement

CONTRACT rests on the agreement of the parties: as it is their agreement which binds them, so by their agreement they may be discharged. And this mode of discharge may occur in one of four ways: by release under seal; by accord and satisfaction; by rescission of a contract which is still executory; or by the operation of some provision contained in the contract itself.

Difficulties

Two sources of difficulty, however, exist which render the topic of discharge by agreement one of considerable artificiality and refinement.

Consideration

The first is that the doctrine of consideration applies to the discharge as well as to the formation of a contract.[1] As a result, a distinction has to be drawn between those situations where the contract is still *executory* on both sides, and those where the contract has been *executed* on one side. In the case of an executory contract, the consideration for the discharge by agreement is found in the relinquishment by each promisee of its right to performance. Where, however, the contract has been wholly executed by one party, leaving the other party still to perform its side of the obligation, as, for example, where A has sold and delivered goods to B, but B has not yet paid for them, any release of B would be purely gratuitous since A would not receive any benefit, nor would B suffer any detriment, by this action. This distinction was emphasized by Parke B. in *Foster* v. *Dawber*, when he said:[2]

> It is competent for both parties to an executory contract, by mutual agreement, without any satisfaction, to discharge the obligation of that contract. But an executed contract cannot be discharged except by release under seal, or by performance of the obligation, as by payment, where the obligation is to be performed by payment.

The agreement to discharge must therefore be under seal, or be supported by some other consideration ('accord and satisfaction') on the part of the person seeking to be released.

Contracts evidenced by writing

The second source of difficulty is that certain contracts are required by law to be evidenced by writing,[3] and it has been held that any subsequent variation of such a contract must also be proved by writing. But writing is not required for the rescission by agreement of such a contract, nor for the waiver of a term contained in it. The distinction between rescission, variation, and waiver is, as we shall see, a fine one, and there is much artificiality in the lines to be drawn between almost

[1] See *ante*, p. 107. [2] (1851) 6 Exch. 839, at p. 851. [3] See *ante*, p. 79.

identical cases. The occasions on which this difficulty can arise have declined greatly since writing is a requirement for very few types of contract.[4] But writing is still required for contracts for the sale or other disposition of land and contracts of guarantee, so that it cannot be said that the difficulties have entirely disappeared.

II. Forms of Discharge by Agreement

(a) Release

Release

The right to performance of a contract can be abandoned by release under seal. If a sealed instrument is employed, it is immaterial that the contract has been executed on one side, for the seal dispenses with the need for consideration. A release not under seal requires consideration. The agreement is then discharged by accord and satisfaction.

An agreement not to sue in perpetuity amounts to a release,[5] but, at common law, an agreement not to sue for a limited period merely gave rise to a cross-action for damages.[6] Equity, however, would restrain the promisor from suing within that time,[7] and today the equitable rule prevails so that the agreement acts as a bar to the original action.[8]

(b) Accord and Satisfaction

Accord and satisfaction

Discharge of a contract in return for a consideration which consists in some satisfaction other than the performance of the original obligation is termed 'accord and satisfaction':

> Accord and satisfaction is the purchase of a release from an obligation, whether arising under contract or tort by means of any valuable consideration, not being the actual performance of the obligation itself. The accord is the agreement by which the obligation is discharged. The satisfaction is the consideration which makes the agreement operative.[9]

It is effective to discharge any contract, whether executory or executed, and even if it is under seal.[10]

Executory satisfaction

Formerly, a contractual obligation, or cause of action arising from the breach of a contract, was not discharged so long as the satisfaction remained executory, that is, so long as the agreement to furnish new consideration had not been

[4] See *ante*, p. 78.

[5] *Hodges* v. *Smith* (1599) Cro. Eliz. 623. See, however, *Cutler* v. *McPhail* [1962] 2 Q.B. 292, at p. 298.

[6] *Ford* v. *Beech* (1848) 11 Q.B. 852.

[7] *Beech* v. *Ford* (1848) 7 Hare 208.

[8] Supreme Court Act 1981, s. 49.

[9] *British Russian Gazette and Trade Outlook Ltd.* v. *Associated Newspapers Ltd.* [1933] 2 K.B. 616, *per* Scrutton L.J. at p. 643.

[10] *Steeds* v. *Steeds* (1889) 22 Q.B.D. 537.

carried out.[11] As it was said in an old case:[12] 'Accord executed is satisfaction; accord executory is only substituting one cause of action in the room of another, which might go on to any extent'. But the question is now regarded as one of the construction of the agreement; and the promise only, as distinct from the actual performance of it, may be a good satisfaction and discharge the original obligation, if it clearly appears that the parties so intended.[13] The original obligation or claim is then discharged from the date the promise is accepted. If the promisor fails to perform its promise, the promisee's only remedy is to sue for breach of the promise, and it cannot return to the original obligation or claim.[14]

Pinnel's Case

It must be remembered, however, that the rule in *Pinnel's Case*[15] prescribes that the payment of a smaller sum in satisfaction of a larger is not a good discharge of a debt. So if B owes A the sum of £50 for goods sold and delivered, and A agrees to excuse him £45 out of this amount, the debt is not discharged by the payment of £5. But the receipt by A of some satisfaction different in kind, or of a fixed instead of an uncertain sum, or of a lesser sum at an earlier date or in a different place than that required by the contract, is sufficient. Compromises of a disputed claim,[16] compositions with creditors,[17] and payments by a third party,[18] also afford exceptions to this rule.

Promissory estoppel

Accord without satisfaction is of no effect, and it is still a matter of some doubt whether the principle of promissory estoppel considered above in Chapter 3 could be successfully relied upon to obviate the necessity for consideration where the accord involves the permanent abandonment by one party of his right to performance by the other. It is questionable whether the principle extends this far. The view has been advanced that promissory estoppel serves only to suspend, and not totally to extinguish, existing rights,[19] although it is probable that this is not a necessary limitation on the doctrine.

Bills of exchange

One important exception does, however, exist. It was a rule of the law merchant, imported into the common law, that no satisfaction was required for the discharge of a bill of exchange or promissory note. The Bills of Exchange Act 1882, section 62, has given statutory force to this rule, but subject to the provision that the discharge must be in writing, or the bill delivered up to the acceptor.

(c) Rescission

Rescission by agreement

A contract which is executory on both sides may be discharged by agreement between the parties that it shall no longer bind them. This effects a rescission of

[11] *Peytoe's Case* (1612) 9 Co. Rep. 79b.

[12] *Lynn* v. *Bruce* (1794) 2 H. Bl. 317, *per* Eyre L.C.J. at p. 319.

[13] *Good* v. *Cheesman* (1831) 2 B. & Ad. 328; *Morris* v. *Baron & Co.* [1918] A.C. 1, at p. 35; *British Russian Gazette and Trade Outlook Ltd.* v. *Associated Newspapers Ltd.* (*supra*, n. 9), at pp. 650, 654–5. See also *Auriens Ltd.* v. *Haigh & Ringrose Ltd.* (1988) Const. L. J. 200.

[14] *British Russian Gazette and Trade Outlook Ltd.* v. *Associated Newspapers Ltd.* (*supra*, n. 9), at pp. 644, 654; *Green* v. *Rozen* [1955] 1 W.L.R. 741.

[15] (1602) 5 Co. Rep. 117a; *ante*, p. 107; *Ferguson* v. *Davis* [1997] 1 All E.R. 315.

[16] See *ante*, p. 100, and see *Kitchen Design & Advance Ltd.* v. *Lea Valley Water Co.* [1989] 2 Lloyd's Rep. 221.

[17] See *ante*, p. 109. [18] See *ante*, p. 110. [19] *Ante*, p. 117.

the contract, and it releases the parties from their obligations under it. Such an agreement is formed of mutual promises, and the consideration for each promise of each party is the abandonment by the other of its rights under the contract.

Abandonment

The court can infer from a long period of delay or inactivity that the parties have agreed to abandon their contract. In order to do this it must be shown that one party conducted itself in such a way that the other party reasonably assumed that it was agreed that the contract was abandoned.[20] Courts have come close to inferring an offer to abandon a contract from mere silence, although some overt act is almost always likely to be required.[21] In the case of arbitration, legislation now gives arbitrators the power to dismiss a claim for want of prosecution irrespective of whether the arbitration contract has been abandoned.[22]

Substituted contract

Rescission of a contract may also take place by such an alteration in its terms as substitutes a new contract for the old one. The old contract may be expressly discharged in the new one, or discharge may be implied by the introduction of new terms or new parties. This method of discharge is therefore a form of rescission with a new contract superadded.

New terms

An example of the discharge of a contract by the substitution of new terms is provided by *Morris* v. *Baron & Co.*:[23]

> A dispute had arisen out of a contract for the sale of cloth and an action had been begun. Before the case came on for trial the parties made an oral arrangement of which the chief terms were that the action and counterclaim were to be withdrawn, an extension of credit was to be given to the buyer for a sum admittedly due from him under the old contract, and, as regards the balance of goods contracted for but undelivered, there was to be substituted for a firm contract of sale an option for the buyer to take them if he pleased.

The House of Lords held that in these circumstances it must be concluded that the parties had agreed to abrogate the old contract and substitute a new one for it.

or new parties substituted

Similarly the introduction of new parties[24] may impliedly rescind an existing contract and substitute a new one for it:

> Suppose A has entered into a contract with B and C, and that B and C agree among themselves that C shall retire from the contract and cease to be liable upon it.

A may of course insist upon the continued liability of C; but if A continues to deal with B after becoming aware of the retirement of C, A's conduct will probably justify the inference that a new contract to accept the sole liability of B has been made, and A cannot then hold C to the original contract. 'If one partner goes out of a firm, and another comes in, the debts of the old firm may, by the consent of all three parties—the creditor, the old firm, and the new firm—be transferred to

[20] *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* [1983] 1 A.C. 854, at pp. 865, 885, 914, 916, 924.

[21] On arbitration, see *ante*, pp. 30–1. On landlord and tenant, see *Collin* v. *Duke of Westminster* [1985] 1 Q.B. 581.

[22] Now contained in the Arbitration Act, 1996 s. 41(3).

[23] [1918] A.C. 1.

[24] See also 'novation', *ante*, pp. 448, 462.

the new firm',[25] and this consent may be implied by conduct, if not expressed in words or writing.

Form of discharge by agreement

As regards the form needed for the expression of an agreement which purports to rescind an existing contract, the old rule of the common law was that a contract under seal could only be discharged by agreement expressed under seal. But, in equity, an agreement to rescind which was not under seal afforded an equitable defence to an action on the deed. Since the Judicature Acts the rule of equity prevails, and a contract under seal may be rescinded by a parol contract.[26]

A parol or simple contract, whether in writing or not, may be discharged by a subsequent agreement, either written or oral. Even when the original agreement is one required by statute to be in or evidenced by writing, as in the case of contracts for the sale or other disposition of land, or contracts of guarantee,[27] there is no need for a written discharge since there is no requirement that they shall be dissolved in writing. In *Morris* v. *Baron & Co.*,[28] for example, the original contract for the sale of cloth was one which was required by section 4 of the Sale of Goods Act 1893 (now repealed) to be evidenced by writing. The substituted contract was itself unenforceable because it did not comply with that section. Nevertheless, it operated as a discharge of the old contract with the result that the buyer, who claimed damages for non-delivery of the goods alternatively under the original and under the substituted agreement, was unable to succeed on either ground.

Rescission of an agreement by substitution of new terms must, however, be distinguished in form and in effect from (i) variation, and (ii) forbearance or waiver.

(i) Variation

Variation of contract

The parties to a contract may effect a variation of the contract by modifying or altering its terms by mutual agreement, but without intending to rescind it and to substitute a wholly new contract for it.[29] A contract may also give one of the parties the power unilaterally to vary the obligations, for example by a price variation clause, but in the case of consumer contracts, this power has been restricted by legislation.[30]

Form of variation

A contract under seal may be varied, as it may be rescinded, by a parol contract.[31] A simple contract, again, whether in writing or not, may be varied by a subsequent agreement either written or oral. This in no way conflicts with the rule that extrinsic evidence is not admissible to vary or add to the contents of a written document, for that principle merely refers to the ascertainment of the

[25] *Hart* v. *Alexander* (1837) 2 M. & W. 484, *per* Parke B. at p. 493. In the case of partnership, these rules are substantially embodied in the Partnership Act 1890, s. 17(3).

[26] *Berry* v. *Berry* [1929] 2 K.B. 316; Supreme Court Act 1981, s. 49.

[27] See *ante*, p. 79.

[28] [1918] A.C. 1; *ante*, p. 493.

[29] *British and Beningtons Ltd.* v. *North Western Cachar Tea Co. Ltd.* [1923] A.C. 48; Stoljar (1957) 35 Can. Bar. Rev. 485; Dugdale and Yates (1976) 39 M.L.R. 680.

[30] *Lombard Tricity Finance Ltd.* v. *Paton* [1989] 1 All E.R. 916; Unfair Terms in Consumer Contracts Regulations 1994 (S.I. 1994 No. 3159), *ante*, p. 198.

[31] *Berry* v. *Berry* [1929] 2 K.B. 316.

original intention of the parties. It has no application to the case of a *subsequent* variation.[32] But a contract required by law to be evidenced by writing must be varied in writing. In *Goss* v. *Lord Nugent*:[33]

> By an agreement in writing the plaintiff had contracted to sell to the defendant several lots of land and to make good title to them. It was afterwards discovered that a good title could not be made to one of the lots, and the defendant orally agreed not to insist on a good title to that lot. The defendant later, relying on the defective title, refused to pay the purchase money.

The contract being one for the sale of land, it was required to be evidenced in writing. The promise to accept the defect in title would operate to vary that contract. But the Court held that the plaintiff could not rely on this variation as it was merely oral, and the defendant was therefore entitled to succeed on the ground that a good title had not been made.

Whether there has been a mere variation of terms or a rescission must depend upon the intention of the parties in each particular case and the question is often not an easy one to determine; but the following test has been suggested by Lord Dunedin:[34]

> In the first case [variation] there are no such executory clauses in the second arrangement as would enable you to sue upon that alone if the first did not exist; in the second [rescission] you could sue on the second arrangement alone, and the first contract is got rid of either by express words to that effect, or because, the second dealing with the same subject-matter as the first but in a different way, it is impossible that the two should be both performed. When I say you could sue on the second alone, that does not exclude cases where the first is used for mere reference, in the same way as you may fix a price by a price list, but where the contractual force is to be found in the second by itself.

The changes must go to the 'very root' of the original agreement,[35] and 'there should have been made manifest the intention in any event of a complete extinction of the first contract, and not merely the desire of an alteration, however sweeping, in terms which leave it still subsisting'.[36]

Consideration for variation

A variation involves a definite alteration, *as a matter of contract*, of contractual obligations by the mutual agreement of both parties.[37] It must be supported by consideration. In most cases, consideration for the variation can be found in a mutual abandonment of existing rights or the conferment of new benefits by each party on the other.[38] Alternatively, consideration may be found in the assumption

[32] *Goss* v. *Lord Nugent* (*infra*, n. 33), at p. 64.

[33] (1833) 5 B. & Ad. 58. See also *Noble* v. *Ward* (1867) L.R. 2 Ex. 135; *United Dominions Trust (Jamaica) Ltd.* v. *Shoucair* [1969] 1 A.C. 340; *Richards* v. *Creighton Griffiths (Investments) Ltd.* (1972) 225 Est. Gaz. 2104; *New Hart Builders Ltd.* v. *Brindley* [1975] Ch. 342.

[34] *Morris* v. *Baron & Co.* [1918] A.C. 1, at p. 26. See also *United Dominions Corporation (Jamaica) Ltd.* v. *Shoucair* [1969] 1 A.C. 340.

[35] *British and Benningtons Ltd.* v. *North Western Cachar Tea Co. Ltd.* [1923] A.C. 48, *per* Lord Sumner at p. 68.

[36] *Morris* v. *Baron & Co.* (*supra*, n. 34), *per* Lord Haldane at p. 19.

[37] *Besseler Waechter Glover & Co.* v. *South Derwent Coal Co.* [1938] 1 K.B. 408, *per* Goddard J. at p. 416.

[38] *Re William, Porter & Co. Ltd.* [1937] 2 All E.R. 361; *W. J. Alan & Co. Ltd.* v. *El Nasr Export and Import Co.* [1972] 2 Q.B. 189.

of additional obligations or the incurring of liability to an increased detriment.[39] Although an agreement whereby one party undertakes an additional obligation, but the other party is merely bound to perform its existing obligations, will, as a general rule, not be effective to vary a contract, as no consideration is present,[40] it has been held that the contract may exceptionally be varied where the court can identify a 'practical' benefit to the party undertaking the additional obligation.[41] And if one party merely agrees not to enforce one of the terms of the contract to be performed by the other, this does not constitute a variation. Such an agreement may, however, be binding as a waiver[42] or in equity.[43]

(ii) Waiver[44]

Waiver

A party who voluntarily agrees to forbear from insisting on the mode of performance or time of performance fixed by the contract, or forbears from so insisting, will be held to have waived the right to require that the contract be performed by the other party in accordance with its terms. But 'waiver' is a term which bears many meanings, has been criticized as a 'slippery word worn smooth with overuse',[45] and, as we shall see, is also used to refer to an election between inconsistent rights. Waiver is relevant where difficulties of form or absence of consideration mean that there is no variation of the contract. Waiver was developed by the common law mainly as a device for evading the formal requirements of the Statute of Frauds, but because, as we have noted, formal requirements are much less important in the modern law, this aspect is now of less importance, although still relevant for certain types of contract, such as contracts for the sale of land and guarantees.[46]

Difficulties as to form

Where a contract has to be by deed, or in, or evidenced by, writing, an oral agreement to forbear, for example by acceding to a request to extend the time of performance, might be met by the plea that the contract had been discharged by an alteration of the time of performance, that a new contract was thereby created, and that the new contract was unenforceable for non-compliance with the statutory requirements as to form.[47] Alternatively, the party which agreed to extend the time for performance, if sued by the other party, might plead that the other party was never ready and willing to perform within the time originally fixed for performance. A party thus given more time for performance, could not rely on the assent of the other to this, as this constituted a variation of the contract which was nugatory since it was not in writing.[48]

[39] *North Ocean Shipping Co. Ltd.* v. *Hyundai Construction Co. Ltd.* [1979] Q.B. 705.

[40] *Stilk* v. *Myrick* (1809) 2 Camp. 317; *Syros Shipping Co. S.A.* v. *Elaghill Trading Co.* [1980] 2 Lloyd's Rep. 390; see *ante*, p. 104.

[41] *Williams* v. *Roffey Bros. & Nicholls (Contractors) Ltd.* [1991] 1 Q.B. 1; *Anangel Atlas Compania Naviera S.A.* v. *Ishikawajima-Harima Heavy Industries Co. Ltd. (No. 2)* [1990] 2 Lloyd's Rep 526, *ante*, p. 105. Cf. *Re Selectmove Ltd.* [1995] 1 W.L.R. 474, *ante*, p. 108.

[42] See *infra*.

[43] See *ante*, p. 110; *post*, p. 498.

[44] See Carter (1991) 4 J.C.L. 59.

[45] Roscoe Pound's forward to Ewart, *Waiver Distributed* (1917), vi.

[46] *Ante*, p. 494, and see generally *ante*, Chapter 3.

[47] *Stead* v. *Dawber* (1839) 10 A. & E. 58.

[48] *Plevins* v. *Downing* (1876) 1 C.P.D. 220, at p. 225.

Variation and waiver distinguished

In order to overcome these difficulties, and so that statutory requirements of formality might not become a cloak for fraud, the Courts showed themselves willing to draw a distinction between variation on the one hand and mere waiver or forbearance on the other. Whereas the former might, in the cases previously mentioned, be required to be in writing, an oral waiver would be efficacious although not in the statutory form. In *Levey & Co.* v. *Goldberg*,[49] for example:

> The defendant agreed in writing to buy from the plaintiffs certain cloth over £10 in value, delivery to be made within a specified time. At the request of the defendant, the plaintiffs orally consented to withhold delivery during that period. Subsequently, however, before delivery was made, the defendant sought to terminate the contract claiming that the plaintiffs had repudiated the contract by not being ready and willing to deliver the cloth within the contract time or within a reasonable time, and pleading the Sale of Goods Act, section 4, as a defence to the plaintiff's subsequent action for non-acceptance of the goods.

It was held that the forbearance by the plaintiffs at the request of the defendant to deliver within the defined period did not constitute a variation but was a valid and effective waiver although not in writing. The defendant was therefore liable for his failure to accept the cloth. The distinction between variation and waiver has been said to depend upon the intention of the parties;[50] for there to be a variation the parties must intend permanently to alter the contractual obligation, if the party forbearing wishes to preserve the possibility of reverting to the contract, it is at most, a waiver. The distinction is difficult to apply in practice,[51] and, although now much less important in respect of formal requirements, it is still important in commercial transactions.

Waiver does not require consideration

The reason for its importance is that waiver is an extremely common occurrence in commercial transactions, but it is open to the technical objection that it ought to have no binding force since it is gratuitous and made without consideration. As it benefits only the promisee, without any corresponding benefit to the promisor, the element of consideration is lacking. It should therefore be without legal effect. But the Courts have not hesitated to hold that the waiver of a contractual stipulation is valid and binding even though this element is not present. The party granting the indulgence cannot go back on the promise and require strict adherence to the contract.[52] However, in cases of postponement of performance, if no period of postponement is fixed, that party may give reasonable notice to the other party requiring the contract to be performed within a certain time, and the contract must then be performed within that time.[53] Similarly

[49] [1922] 1 K.B. 688.

[50] *Stead* v. *Dauber* (1839) 10 A. & E. 57; *Tallerman & Co. Pty. Co. Ltd.* v. *Nathan's Merchandise (Vic.) Pty. Ltd.* (1954) 91 C.L.R. 288, at p. 297 (High Court of Australia). Dugdale and Yates (1976) 39 M.L.R. 680 distinguish pre-breach statements which are likely to be variations from post-breach ones, which are not.

[51] Compare, for example, *Goss* v. *Lord Nugent* (1833) 5 B. & Ad. 58 with *Hickman* v. *Haynes* (1875) L.R. 10 C.P. 598.

[52] *Leather Cloth Co.* v. *Hieronimus* (1875) L.R. 10 Q.B. 140; *Bruner* v. *Moore* [1904] 1 Ch. 305; *Besseler Waechter Glover & Co.* v. *South Derwent Coal Co.* [1938] 1 K.B. 408; *Tankexpress A/S* v. *Compagnie Financière Belge des Petroles S.A.* [1949] A.C. 76.

[53] *Charles Rickards Ltd.* v. *Oppenhaim* [1950] 1 K.B. 616.

in cases of the waiver of other types of contractual term, the party granting the indulgence may as a general rule, upon reasonable notice, require the other party to comply with the original contractual stipulation; but cannot treat the forbearance as of no effect. In *Panoutsos* v. *Raymond Hadley Corporation of New York*:[54]

> P contracted to buy from RH 4,000 tons of flour which RH was to ship to Greece, by means of separate shipments. The contract required payment to be effected by P opening a bankers' confirmed letter of credit in RH's favour. P did open a letter of credit, but it was not 'confirmed'. RH made some shipments and received payment for these by this letter of credit. Subsequently, however, RH summarily terminated the remainder of the contract on the ground that the letter of credit was not in accordance with the contractual stipulation. P sued for breach.
>
> It was held that RH, by its acceptance of payment by means of the unconfirmed letter of credit, had impliedly waived this condition in the contract. This, however, did not mean that it was consequently bound to accept that letter of credit until the end of the contract; it might, by giving reasonable notice, insist on the strict contractual terms. But it was not entitled to cancel the contract in a summary manner.

Risk to be borne by party requesting postponement

The party to whom the forbearance is granted is also bound by its terms.[55] Moreover, if that party asks to have the performance of the contract postponed, it does so at its own risk. For if that party subsequently refuses to accept the goods, and the market value of the goods which it should have accepted at the earlier date has altered at the later date, the measure of damages may be increased as against it by the addition of damages consequent on the delay.[56]

Equitable estoppel

In developing waiver mainly as a common law device for evading the formalities required by the Statute of Frauds, little attempt was made to explain why a gratuitous promise should thus be binding. If it is to be justified analytically, it may be more satisfactory to regard waiver as a species of estoppel. It will be remembered that equity, by use of the principle of promissory estoppel,[57] is also prepared to give effect to a promise made in similar circumstances:

> If persons who have contractual rights against others induce by their conduct those against whom they have such rights to believe that such rights will either not be enforced or will be kept in suspense or abeyance for some particular time, those persons will not be allowed by a court of equity to enforce the rights until such time has elapsed, without at all events placing the parties in the same position as they were before.[58]

The party who has waived strict performance may be said to be estopped from going back on the promise or representation to do so, at any rate without giving fair and adequate notice to the promisee.[59]

[54] [1917] 2 K.B. 473.

[55] *Hickman* v. *Haynes* (1875) L.R. 10 C.P. 598; *Levey & Co.* v. *Goldberg* [1922] 1 K.B. 688.

[56] *Levey & Co.* v. *Goldberg* (*supra*, n. 55).

[57] See *ante*, p. 110.

[58] *Birmingham and District Land Co.* v. *L. & N.W. Ry.* (1888) 40 Ch. D. 268, *per* Bowen L.J. at p. 286.

[59] For recent discussion on waiver in the sense of estoppel see *Motor Oil Hellas (Corinth) Refineries S.A* v. *Shipping Corp. of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391; *Commonwealth of Australia* v. *Verwayen* (1990) 170 C.L.R. 394.

The similarity between waiver and estoppel was expressly noted by Denning L.J. in *Charles Rickards Ltd.* v. *Oppenhaim*:[60]

O ordered from CR a Rolls Royce car chassis, which was delivered to him. He wished to have a body built on the chassis, and CR accepted this order. The job was to be completed by 20 March 1948, at the latest. On that day it was still not completed, but O continued to press for delivery. On 29 June, however, he wrote to CR stating he would not take delivery after 25 July. CR still having failed to deliver the car, O treated the contract as repudiated.

The Court of Appeal held that he was entitled to do so. Although by his conduct he had impliedly waived the original stipulation as to time, he had given reasonable notice of his intention to reimpose a new time limit. CR having failed even then to perform, the contract was clearly discharged by its breach. Denning L.J. said of O's consent to postponement:[61]

Whether it be called waiver or forbearance on his part, or an agreed variation or substituted performance, does not matter. It is a kind of estoppel. By his conduct he evinced an intention to affect their legal relations. He made, in effect, a promise not to insist on his strict legal rights. That promise was intended to be acted on, and was in fact acted on. He cannot afterwards go back on it.

The analogy, however, is not completely exact. It may be that promissory estoppel is more limited than waiver. For an estoppel to become binding, the promisee must alter its position in reliance on the promise. In fact, when waiver is used in the sense of estoppel, the focus of the law is on whether the dealings between the parties and the prejudice to the party who has been told that strict performance is not required are such as to render it inequitable for the other party to go back on its promise or representation.[62] But the requirement of reliance has not been strictly enforced for waiver,[63] although it is true to say that in cases of waiver of a time fixed for performance (but not in the case of waiver of other types of stipulation) it will usually be found to have been satisfied.

Waiver may also be used in the sense of election, that is, where a party is entitled either under the terms of the contract or by the general law, to choose between alternative and inconsistent rights.[64] Here the law focuses on that party's words, conduct, and knowledge to determine whether an election has been made.[65] Once an election is made it can be said that the party has waived the alternative and inconsistent right. For example, waiver may apply to conditions precedent,[66] to the right of one party to treat itself as discharged by reason of a repudiatory breach by the other,[67] or to terminate a contract for breach under an

[60] [1950] 1 K.B. 616; cf. Stoljar (1957) 35 Can. Bar. Rev. 485.
[61] At p. 623.
[62] See *ante*, pp. 113–14.
[63] *W. J. Alan & Co. Ltd.* v. *El Nasr Export and Import Co. Ltd.* [1972] 2 Q.B. 189, at p. 213, but cf. *ibid.*, at p. 221; *Finagrain S.A. Geneva* v. *P. Kruse Hamburg* [1976] 2 Lloyd's Rep. 508. See *ante*, p. 497.
[64] *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corp. of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391, *per* Lord Goff at p. 398.
[65] See *United Australia Ltd.* v. *Barclays Bank Ltd.* [1941] A.C. 1, *per* Lord Atkin at p. 30.
[66] See *ante*, p. 133.
[67] See *post*, pp. 547, 548.

express contractual provision to that effect.[68] If a party elects to affirm the contract and thus waive its right to terminate, it will not be held to have waived (in the sense of an election) its right to damages for the breach unless the requirements of a waiver in the sense of estoppel are established to that effect.[69] Further, a party may, without the assent of the other party, waive compliance with a term of the contract which is inserted solely for its own benefit.[70] When used in the sense of an election, waiver is always permanent; it cannot be reversed by the service of a notice.[71] This is to be contrasted to what was said above in relation to waiver in the sense of estoppel which can (but not always) be negated by the service of a notice.[72] In addition, when used in the sense of election there is no requirement of reliance and detriment although there is still a focus on words and conduct. Moreover, when used in the sense of estoppel there is no requirement of knowledge whereas with election there is a requirement that the promisee has knowledge of the facts which give rise to the right to elect and arguably in some cases knowledge of the right itself.[73]

(d) Provisions for Discharge Contained in the Contract Itself

Provisions in contract itself

A contract may contain within itself the elements of its own discharge, in the form of provisions, express or implied, for its determination or termination in certain circumstances. Apart from the statutory protection given to those dealing on the other party's standard terms[74] and to consumers,[75] and the power of the court to give equitable relief against forfeiture,[76] there is no requirement that a party act reasonably when deciding to exercise a contractual power to terminate.

The parties may expressly provide that, upon the happening of a certain event, either the contract shall *ipso facto* determine,[77] or that, on the occurrence of that event, one party is to have the option to cancel the contract.[78]

Automatic termination

Where the event is one over which the parties have no control and cannot bring about themselves, then effect will generally be given to a provision that the con-

[68] See *infra*.

[69] *Hain S.S. Co. Ltd.* v. *Tate & Lyle Ltd.* (1936) 41 Com. Cas. 350, at p. 363; [1936] 2 All E.R. 597, at p. 608; *Suisse Atlantique Societe d'Armament Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale* [1967] 1 A.C. 361, at p. 395; *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corp. of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391, at p. 400.

[70] *Hawksley* v. *Outram* [1892] 3 Ch. 359. Cf. *Burgess* v. *Cox* [1951] Ch. 383 (term inserted for benefit of both parties).

[71] *Kammins Ballrooms Co. Ltd.* v. *Zenith Investments (Torquay) Ltd.* [1971] A.C. 850, at p. 883; *China National Foreign Trade Transportation Corporation* v. *Evologia Shipping Co. S.A. of Panama* [1979] 1 W.L.R. 1018, *per* Lord Scarman at p. 1034–5.

[72] *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corp. of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep 391, at p. 399. See *ante*, p. 498 on estoppel.

[73] See *Peyman* v. *Lanjani* [1985] Ch 457. See further *post*, p. 537.

[74] Unfair Contract Terms Act 1977, s. 3(2)(b)(ii).

[75] Unfair Terms in Consumer Contracts Regulations 1994 (S.I. 1994 No. 3159), Sched. 3, esp. para 1(f), (g), *ante*, p. 196; Consumer Credit Act 1974, ss. 76, 86, 87, 88, 98.

[76] This is considered *post*, p. 609. See also Law of Property Act 1925, s. 146 (forfeiture of lease).

[77] *Continental Grain Export Corpn.* v. *S.T.M. Grain Ltd.* [1979] 2 Lloyd's Rep. 460.

[78] *Head* v. *Tattersall* (1871) L.R. 7 Ex. 7; *Brown* v. *Knowlsey B.C.* [1986] I.R.L.R. 102, *ante*, p. 135.

tract is *ipso facto* to cease to bind.[79] But if the relevant event is a breach of contract the courts are likely to interpret the contract as nevertheless requiring an election by the innocent party before holding that the contract is terminated. This is an application of the principle that a party may not rely on its own breach to bring the contract to an end;[80] i.e a party may not take advantage of his or her own wrong.[81] The better view is that this is not an independent rule of law,[82] but a principle of construction reflecting the presumed intention of the parties, and which may be rebutted by the express terms of the contract.[83] Moreover, even if the event triggering the automatic termination provision is not a breach of contract, a party will not be able to take advantage of that provision if their wrongful action gave rise to the event upon which the automatic termination provision is based.[84]

Termination on notice

More often, a provision is inserted making the contract terminable at the option of one or both of the parties upon notice. This right of termination may be exercisable upon a breach of the contract by one party (whether or not the breach would amount to a repudiation of the contract), or upon the occurrence or non-occurrence of a specified event other than breach,[85] or simply at the will of the party upon whom the right is conferred. For example, the contract may be terminable 'by 3 months' notice in writing on either side'. A similar provision may be incorporated by implication, or by the usage of trade. At common law,[86] for instance, a contract of employment may be terminated by reasonable notice by either party, the length of the notice depending upon the nature of the employment and the intervals at which remuneration is to be paid. Moreover, even where the duration of a written contract is on the face of the instrument indefinite and unlimited, such a provision may sometimes be implied from the nature of the

[79] *New Zealand Shipping Co.* v. *Societe des Ateliers et Chantiers* [1919] A.C. 1, *per* Lord Wrenbury at p. 15; *Gyllenhammar & Partners International Ltd.* v. *Sour Brodogradevna Industrija* [1989] 2 Lloyd's Rep 403, *per* Hirst J. at p. 413.

[80] The principle does not apply if breach is of a duty owed to a person who is not a party to the contract: *Cheall* v. *Association of Professional Executive Clerical and Computer Staff* [1983] 2 A.C. 180, *per* Lord Diplock at p. 189 and *Thompson* v. *ASDA-MFI Group plc.* [1988] 1 Ch. 241, at p. 266.

[81] *Alghussein Establishment* v. *Eton College* [1988] 1 W.L.R. 587; *Cheall* v. *Association of Professional Executive Clerical and Computer Staff* (*supra*, n. 80); *Brown* v. *Knowsley B.C.* [1986] I.R.L.R. 102; *Cerium Investments Ltd.* v. *Evans*, *The Times*, 14 February 1991.

[82] *New Zealand Shipping Co.* v. *Societe des Ateliers et Chantiers* (*supra*, n. 79); *Alghussein Establishment* v. *Eton College* (*supra*, n. 81); *Cheall* v. *Association of Professional Executive Clerical and Computer Staff* (*supra*, n. 80).

[83] See e.g., *Gyllenhammar & Partners International Ltd.* v. *Sour Brodogradevna Industrija* [1989] 2 Lloyd's Rep 403, *per* Hirst J. at p. 416 and *Thornton* v. *Abbey National plc.*, *The Times*, 3 March 1993.

[84] See *Cheall* v. *Association of Professional Executive Clerical and Computer Staff* (*supra*, n. 80), *per* Lord Diplock at p. 189. This principle means that even where such a provision declares that the contract is to be 'void', it is not absolutely so: *New Zealand Shipping Co.* v. *Societe des Ateliers et Chantiers* (*supra*, n. 79) per Lord Wrenbury at p. 15. See also *post*, p. 521 (self-induced frustration).

[85] *Mannai Investment Co. Ltd.* v. *Eagle Star Life Assurance Co. Ltd.* [1997] 2 W.L.R. 945 ('break' clause in lease). See also *Head* v. *Tattersall* (1871) L.R. 7 Ex. 7 and, *ante*, p. 135 (condition subsequent).

[86] But see now the Employment Rights Act 1996, s. 86 (minimum periods of notice by employer).

contract,[87] particularly where the contract is for a fixed price[88] or is a commercial contract.[89] Thus a partnership for no fixed time is terminable by notice.[90]

Any notice given must be clear and unambiguous in its terms, and if it is to be given in a certain form, e.g. in writing, or within a certain time, or if a specified period of notice must be given, these requirements must normally be strictly complied with, otherwise the notice will be of no effect.[91]

[87] *Crediton Gas Co.* v. *Crediton U.D.C.* [1928] 1 Ch. 447; *Winter Garden Theatre (London) Ltd.* v. *Millennium Productions Ltd.* [1948] A.C. 173; *Re Spenborough U.D.C.'s Agreement* [1968] Ch. 139; Cf. *Kirklees Metropolitan B.C.* v. *Yorkshire Woollen District Transport Co.* (1978) 77 L.G.R. 448 (fixed term agreement could not be terminated by notice). See also Carnegie (1969) 85 L.Q.R. 392.

[88] *Staffordshire Area Health Authority* v. *South Staffs. Waterworks Co.* [1978] 1 W.L.R. 1387, on which see *post*, p. 521. Where there are price variation provisions, such an implied term is unlikely: *The Queensland Electricity Generating Board* v. *New Hope Collieries Pty Ltd.* [1989] 1 Lloyd's Rep. 205; *Watford Borough Council* v. *Watford Rural Parish* (1987) 86 L.G.R. 524 at p. 58.

[89] *Martin-Baker Aircraft Co. Ltd.* v. *Canada Flight Equipment Ltd.* [1955] 2 Q.B. 556, at p. 577; *Re Spenborough U.D.C.'s Agreement* [1968] Ch. 139; *Watford Borough Council* v. *Watford Rural Parish* (*supra*, n. 88) at p. 532.

[90] Partnership Act 1890, s. 26.

[91] *Avofos Shipping Co. S.A.* v. *R. Pagnan & Filii* [1983] 1 W.L.R. 195. Cf. *Bremer Handelsgesellschaft mbH* v. *Vanden Avenne-Izegem P.V.B.A.* [1978] 2 Lloyd's Rep. 109; *ante*, p. 140. But cf. *Mannai Investment Co. Ltd.* v. *Eagle Star Life Assurance Co. Ltd.* [1997] 2 W.L.R. 945 (minor misdescription did not preclude notice from being effective where, construed in its contractual setting, it would unambiguously inform a reasonable recipient how and when it was to operate).

14

Discharge by Frustration[1]

I. History and Scope of the Doctrine

Impossibility and frustration

MOST legal systems make provision for the discharge of a contract where, after its formation, a change of circumstances makes contractual performance illegal or impossible. In English law, such a situation is provided for by the doctrine of frustration.[2] Originally, this term was confined to the discharge of maritime contracts by the 'frustration of the adventure', but it has now been extended to cover all cases where an agreement has been terminated by supervening events beyond the control of either party. But the doctrine is not one of supervening impossibility; some kinds of impossibility may in some circumstances not discharge the contract at all, while impossibility does not accurately describe the cases of frustration of a commercial purpose where the fundamentally different situation which has unexpectedly occurred means that performance would be, as a matter of business, radically different from the contractually stipulated performance.[3] In these cases the contract is discharged although performance is not literally impossible.

The defining characteristics of the doctrine of frustration that have emerged from the case law have been summarized by Bingham L.J.[4] in the following terms:

> The doctrine of frustration was evolved to mitigate the rigour of the common law's insistence on literal performance of absolute promises . . . The object of the doctrine was to give effect to the demands of justice, to achieve a just and reasonable result, to do what is reasonable and fair, as an expedient to escape from injustice where such would result from enforcement of a contract in its literal terms after a significant change in circumstances . . . Since the effect of frustration is to kill the contract and discharge the parties from further liability under it, the doctrine is not to be lightly invoked, must be kept within narrow limits and ought not to be extended . . . Frustration brings the contract to an end forthwith, without more and automatically . . . The essence of frustration is that it should not be due

[1] See generally, Treitel, *Frustration and Force Majeure* (1994).

[2] Initial impossibility and misunderstandings that exist at the time of the formation of the contract, sometimes referred to as 'pre-contractual frustration', are considered *ante*, in Chapter 8. See esp. p. 299, n. 27, and note that care should be taken not to treat such cases as frustration, cf. *Gamerco S.A.* v. *I.C.M./Fair Warning (Agency) Ltd.* [1995] 1 W.L.R. 1226, *quaere* wrongly so treated, see Carter and Tolhurst (1996) 10 J.C.L. 264, at pp 265–6. See also *post*, p. 526.

[3] *Joseph Constantine Steamship Line Ltd.* v. *Imperial Smelting Corporation Ltd.* [1942] A.C. 154, *per* Viscount Simon, at p. 164. See also *Jackson* v. *Union Marine Insurance Co. Ltd.* (*post*, p. 505) and *Krell* v. *Henry* (*post*, p. 507).

[4] *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep. 1 at p. 8. For the facts, see *post*, p. 522.

to the act or election of the party seeking to rely on it . . . A frustrating event must be some outside event or extraneous change of situation . . . A frustrating event must take place without blame or fault on the side of the party seeking to rely on it.

In this chapter we trace the history of the doctrine and examine the scope of its present application. It should, however, be noted that as the doctrine has developed, so too has the use, particularly in standard form contracts, of *force majeure* clauses, which entitle one or both of the parties to be excused (in whole or in part) from performance of the contract. Such clauses may cover non-frustrating events and may provide for more flexible remedies than total discharge. For instance they may entitle a party to suspend performance, to claim an extension of time for performance, or to be compensated for performance which will be more onerous.[5]

(a) Emergence of the Doctrine

Formerly obligations regarded as absolute

Before 1863 it was a general rule of the law of contract that a person was absolutely bound to perform any obligation which had been undertaken, and could not claim to be excused by the mere fact that performance had subsequently become impossible; for 'where there is a positive contract to do a thing, not in itself unlawful, the contractor must perform it or pay damages for not doing it, although in consequence of unforeseen accidents, the performance of his contract has become unexpectedly burdensome or even impossible'.[6] So in *Paradine* v. *Jane* in 1647:[7]

Paradine sued Jane for rent due upon a lease. Jane pleaded 'that a certain German Prince, by name Prince Rupert, an alien born, enemy to the king and kingdom, had invaded the realm with an hostile army of men; and with the same force did enter upon the defendant's possession, and him expelled, and held out of possession . . . whereby he could not take the profits'. This plea was in substance a plea that the rent was not due because the lessee had been deprived, by events beyond his control, of the profits from which the rent should have come.

The Court held that this was no excuse:[8]

When the party by his own contract creates a duty or charge upon himself, he is bound to make it good, if he may, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract. And therefore if the lessee covenant to repair a house, though it be burnt by lightning, or thrown down by enemies, yet he ought to repair it.

unless subject to express or implied provision excluding performance

It has always, however, been open to the parties to introduce an express provision into their agreement that the fulfilment of a condition or the occurrence of an event should discharge one or both of them from some or all of their obligations

[5] On such clauses, which fall outside the scope of this book, see generally, *Channel Island Ferries Ltd.* v. *Sealink U.K. Ltd.* [1988] 1 Lloyd's Rep 323; Treitel, *Frustration and Force Majeure* (1994), §12–012 ff; McKendrick, *Force Majeure and Frustration of Contract*, 2nd edn. (1994), esp. chs. 1 and 3. For one other advantage, see *post*, p. 523.

[6] *Taylor* v. *Caldwell* (1863) 3 B. & S. 826, *per* Blackburn J. at p. 833.

[7] (1647) Aleyn 26 and Style 47. On the antecedents of this decision, see Ibbetson, ch. 1 in Rose, ed., *Consensus ad Idem* (1996).

[8] *Ibid.*, at p. 27.

under it;[9] and just as the parties may expressly discharge their obligation to perform a contract, so there are cases in which a contract, though containing no express provision, will be interpreted by the Courts as containing such a provision by implication. An implication of this nature would, it might be thought, readily be made where, without the fault of either party, an event occurs which renders the contract not merely more onerous, but completely impossible of performance.

Taylor v. *Caldwell*

This was the device[10] used by the Court of Queen's Bench in 1863 in the case of *Taylor* v. *Caldwell*[11] in order to introduce an exception into the existing law:

> The defendant agreed with the plaintiff to hire to him a music-hall and gardens for the purpose of entertainment. Before the day of performance arrived, the music-hall was destroyed by fire. The plaintiff sued the defendant for damages for breach of the contract which the defendant, through no fault of his own, was unable to perform.

The defendant was held not liable to pay, for 'the contract is not to be construed as a positive contract, but as subject to an implied condition that the parties shall be excused in case, before breach, performance becomes impossible from the perishing of the thing without default of the contractor'.[12] Blackburn J. said:[13]

> 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. In none of these cases is the promise in words other than positive, nor is there any express stipulation that the destruction of the person or thing shall excuse the performance; but that excuse is by law implied, because from the nature of the contract it is apparent that the parties contracted on the basis of the continued existence of the particular person or chattel.

From this time onwards the Courts showed themselves prepared to hold that, unless a contrary intention appears, the continuance of a contract was conditional upon the possibility of its performance.

'Frustration of the adventure'

It was not long, however, before the new doctrine was extended outside the sphere of literal impossibility to situations where there had been a 'frustration of the adventure'. Most of the early frustration cases arose out of delay, attributable to the fault of neither party, in the carrying out of charterparties; and they seem at first to have been treated as raising a question which was regarded as connected, rather than identical, with that raised by the cases of impossibility.

In *Jackson* v. *Union Marine Insurance Co. Ltd.*:[14]

> The plaintiffs' ship had been chartered to proceed in January to Newport to load a cargo of iron rails for San Francisco. On the way to Newport she ran aground and it took over a month to refloat her. She was then taken into Liverpool and underwent lengthy repairs lasting until August. In the meantime the charterers had chartered another ship. The plaintiffs claimed from the defendant insurance company for a total loss, by perils of the sea, of the freight to be earned under the charterparty.

[9] See *ante*, p. 135.
[10] See Trakman (1983) 46 M.L.R. 39.
[11] (1863) 3 B. & S. 826.
[12] At p. 833.
[13] At p. 839.
[14] (1874) L.R. 10 C.P. 125.

The question whether or not there had been such a loss depended for the answer on the question whether or not the charterers had been justified in throwing up their contract with the plaintiffs instead of waiting until the ship was repaired and then loading her. The jury found that the time necessary to get the ship off, and to repair her so that she might become a cargo-carrying ship, had been so long as to put an end in a commercial sense to the speculation entered into by the plaintiffs and the charterers; and on this finding the Court held that a voyage undertaken after the ship had been repaired would have been an adventure different from that which both parties had contemplated at the time of the contract. It was, they said, an implied term of the contract that the ship should arrive at Newport within a reasonable time, and her inability to arrive put an end to it. 'The adventure', said Bramwell B.,[15] 'was frustrated by perils of the seas, both parties were discharged, and a loading of cargo in August would have been a new adventure, a new agreement'.

Principles the me as in case of impossibility

The dislocation of business caused by the war with Germany from 1914 to 1918 brought a large number of frustration cases into the Courts, and it soon became clear that they raised the same questions as those raised by cases previously considered under the head of impossibility. 'When this question arises in regard to commercial contracts', said Lord Loreburn,[16] 'the principle is the same, and the language as to 'frustration of the adventure' merely adapts it to the class of cases in hand'. 'The doctrine of frustration is only a special case of the discharge of contract by an impossibility of performance arising after the contract was made.'[17] The modern practice is to use the term 'frustration' to cover cases of both classes.

(b) Instances of Frustration

Before turning to the theoretical basis of the doctrine of frustration, we consider examples of fact situations in which the Courts have been ready to infer, from the nature of the contract and from the circumstances surrounding it, that it has been frustrated by the happening of a subsequent event. While the reasoning in some of these examples is based on the 'implied term' theory of frustration, which, as we shall see, is now discredited, they remain useful illustrations of situations in which a contract may be frustrated.

) Destruction of ubject-matter of contract

The first and most simple case is probably that where the performance of the contract is made impossible by the destruction of a specific thing *essential* to that performance, for example, the destruction of the music-hall in *Taylor* v. *Caldwell*. So if A agrees with B to supply and install certain machinery in B's factory premises, and the premises are destroyed by fire, the contract will be frustrated.[18] But if the machinery only is destroyed, leaving the premises untouched, then it is

[15] At p. 148.

[16] *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Ltd.* [1916] 2 A.C. 397, at p. 404.

[17] *Joseph Constantine Steamship Line Ltd.* v. *Imperial Smelting Corporation Ltd.* [1942] A.C. 154, *per* Viscount Maugham at p. 168.

[18] *Appleby* v. *Myers* (1867) L.R. 2 C.P. 651; *post*, p. 527.

still possible to obtain other machinery and A must do the work over again: the contract will not be discharged.[19] Where an agreement for the sale of specific goods has been made and, before the risk passes to the buyer, without any fault on the part of the seller or buyer, the goods perish, the agreement is avoided.[20]

(ii) Non-occurrence of a particular event

Secondly, the principle of frustration has been held to apply to cases concerning the cancellation of an expected event. In the so-called 'Coronation cases', which arose out of the postponement of the coronation of King Edward VII owing to his sudden illness, it was applied to contracts the performance of which depended on the existence or occurrence of a particular state of things forming the basis on which the contract had been made. In *Krell* v. *Henry*,[21] for instance:

The defendant agreed to hire a flat from the plaintiff for 26 and 27 June 1902; the contract contained no reference to the coronation processions, but they were to take place on those days and to pass the flat. The processions were cancelled.

Two-thirds of the rent had not been paid when the processions were abandoned and the Court of Appeal held that the plaintiff could not recover it. The Court considered that the processions and the relative position of the flat lay at the foundation of the agreement. The contract was therefore discharged.

It should not be imagined, however, that failure before performance of the factor which induced the parties to enter into the agreement will necessarily discharge the contract; for 'it may be that the parties contracted in the expectation that a particular event would happen, each taking his chance, but that the actual happening of the event was not made the basis of the contract'.[22] In *Herne Bay Steamboat Co.* v. *Hutton*:[23]

The defendant chartered from the plaintiff the S.S. *Cynthia* for 28 and 29 June 1902, for the express purpose of taking paying passengers to see the Coronation naval review at Spithead and to tour the fleet. The review was cancelled, but the fleet remained.

The Court of Appeal refused to hold the defendant discharged. They did so, partly on the ground that a tour of the fleet was still possible, but mainly because they considered that it was the defendant's own venture and it was at his risk. The Court pointed out that if the existence of a particular state of things is merely the motive or inducement to one party to enter into the contract, as distinct from the basis on which both contract, the principle cannot be applied. And the example was given of the hire of a vehicle to take the hirer and a party to Epsom to view the races on Derby day; the hirer will not be discharged if the races are cancelled, for the hirer's purpose is not the common foundation of the contract to hire the vehicle.

[19] *Ibid.*, at p. 660.

[20] Sale of Goods Act 1979, s. 7. See further *post*, pp. 533–4 (effect of frustration and partial perishing of goods).

[21] [1903] 2 K.B. 740. See also *Chandler* v. *Webster* [1904] 1 K.B. 493 (*post*, p. 527). Cf. *Griffith* v. *Brymer* (1903) 19 T.L.R. 434 (*ante*, p. 305).

[22] *Larrinaga & Co. Ltd.* v. *Société Franco-Americaine des Phosphates de Medulla, Paris* (1923) 39 T.L.R. 316, *per* Lord Finlay at p. 318.

[23] [1903] 2 K.B. 683.

(iii) Death, or incapacity for personal service

Thirdly, where performance of obligations under a contract for personal services is rendered impossible or radically different by the death or incapacitating illness of the promisor, the contract will be frustrated. In *Stubbs* v. *Holywell Railway Co.*[24] it was held that a contract for personal services was put an end to by the death of the party by whom the services were to be rendered. And in *Robinson* v. *Davison*:[25]

The defendant's wife, an eminent piano player, promised to perform at a concert, but was prevented from doing so by a dangerous illness. An action was brought against the defendant claiming damages for breach of contract.

It was held that the contract was discharged by the defendant's wife's illness, and it was not therefore broken by her failure to perform, nor, on the other hand, could she have insisted on performing when she was unfit to do so as frustration is not brought about by an act of election.[26] These are examples of cases where performance by the relevant party is personal and cannot be carried out by anyone else so that death or illness gives rise to frustration.[27] Similar decisions have been reached in the case of the discharge of a seaman's contract of service by his internment,[28] and of that of a music-hall artist, 'Cheerful Charlie Chester', by his call-up for service in the army.[29] However, absence—even prolonged absence—through illness will not necessarily determine a contract of employment. A number of factors must be considered: the terms of the contract (including any sick pay provisions), the nature and the expected duration of the employment, the period of past employment, and the nature and duration of the illness and the prospects for recovery.[30] In *Marshall* v. *Harland & Wolff Ltd.*[31] the test for frustration of a contract of employment was formulated as follows, 'Was the employee's incapacity . . . of such a nature, or did it appear likely to continue for such a period, that further performance of his obligations in the future would either be impossible or would be a thing radically different from that undertaken by him and accepted by the employer under the agreed terms of his employment?'. The application of the doctrine of frustration to employment contracts can give rise to results that may appear harsh. In *Notcutt* v. *Universal Equipment Co. (London) Ltd.*[32] frustration was held to have occurred when it became apparent to the parties that an employee who had suffered a heart attack would never work again. This had the effect of automatically terminating the contract of

[24] (1867) L.R. 2 Ex. 311. [25] (1871) L.R. 6 Ex. 269. [26] *Post*, p. 521 ff.

[27] If performance is not of a personal character then the contract is not necessarily frustrated by death or incapacity: *Phillips* v. *Alhambra Palace Co. Ltd.* [1901] 1 Q.B. 59.

[28] *Horlock* v. *Beal* [1916] 1 A.C. 486.

[29] *Morgan* v. *Manser* [1948] 1 K.B. 184.

[30] *Marshall* v. *Harland & Wolff Ltd.* [1972] 1 W.L.R. 899, at pp. 903–5. Note that an employee who is suspended from work on medical grounds is entitled to be paid by the employer for up to 26 weeks: Employment Rights Act 1996, s. 64.

[31] [1972] 1 W.L.R. 899, at p. 905 *per* Donaldson J. But see *Hart* v. *A. R. Marshall & Sons (Bulwell) Ltd.* [1977] 1 W.L.R. 1067 ('key' worker replaced); *Egg Stores (Stamford Hill) Ltd.* v. *Leibovici* [1977] I.C.R. 260, at p. 264. See also *F.C. Shepherd & Co. Ltd.* v. *Jerrom* [1987] 1 Q.B. 301 (imprisonment of employee).

[32] [1986] 1 W.L.R. 641.

employment and thereby releasing the employer from the contractual provisions which required that notice be given before terminating the contract and the statutory obligation to pay the employee during the period of notice.

(iv) Charterparties

Fourthly, a number of cases have arisen concerning charterparties, and these provide some of the most important instances of the application of the doctrine.

Requisitioning of ships

In war-time, ships are often requisitioned for such time and for such purposes as the Government may require them. If the ship is under charterparty the question will arise whether or not the requisitioning operates so as to frustrate the rights of the shipowners and charterers under the agreement. In *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Co. Ltd.*:[33]

The steamship *F. A. Tamplin* was chartered by a time charterparty for 5 years from 4 December 1912, to 4 December 1917. In February 1915 the Government requisitioned the ship for use as a troopship and made certain structural alterations to her for this purpose. The charterers were willing to go on paying the agreed freight under the charterparty, but the owners claimed that the contract had been frustrated by the requisition as they wished to obtain a larger amount of compensation from the Crown.

The House of Lords, by a bare majority, held that the contract still continued. The interruption was not of sufficient duration to make it unreasonable for the parties to go on. There might be many months during which the ship would be available for commercial purposes before the 5 years expired.

In *Bank Line Ltd.* v. *Capel (A.) & Co.*,[34] on the other hand:

In February 1915, the appellants chartered the steamship *Quito* to the respondents for a period of 12 months from the time the vessel should be delivered. It was provided in the charterparty that (i) if the steamer had not been delivered by 30 April 1915, the charterers were to have the option to cancel the contract or to proceed with it, and (ii) 'Charterers to have option of cancelling this charterparty should steamer be commandeered by Government during this Charter'. The steamer was not delivered by 30 April, and, on 11 May, before delivery, she was commandeered by the Government and not released until September. She was then sold by the appellants, and the respondents sued for non-delivery, having never exercised their options to cancel.

The House of Lords held that the contract had been frustrated. The clauses in the charterparty were not intended to place the shipowners indefinitely at the charterers' mercy, to oblige them to deliver however long the delay. They merely gave to the charterers the option to cancel the contract without the necessity of proving frustration:

A contingency may be provided for, but not in such terms as to show that the provision is meant to be all the provision for it. A contingency may be provided for, but in such a way as shows that it is provided for only for the purpose of dealing with one of its effects and not with all.[35]

Lord Haldane, who dissented, was of the opinion that there was no frustration: the requisition was not of such a permanent character as to make the terms of the charterparty wholly inapplicable.

[33] [1916] 2 A.C. 397. [34] [1919] A.C. 435.
[35] [1919] A.C. 435, *per* Lord Sumner at p. 456.

These differences of opinion within the highest tribunal show that cases of frustration raise most difficult questions of fact and principle. In the *Bank Line* case Lord Loreburn stated[36] that 'the main thing to be considered is the probable length of the total deprivation of the use of the chartered ship compared with the unexpired duration of the charterparty'. On this basis, the two decisions can perhaps be reconciled without undue difficulty, since the *Bank Line* charter was of one year's duration only, whereas that in the *Tamplin* case had still nearly 3 years to run at the time the requisitioning took place. But it is by no means certain that Lord Loreburn's test is the correct one to apply.[37]

and other events

Events other than the seizure or requisitioning of the ship may also frustrate a charterparty. It has already been seen that, in *Jackson* v. *Union Marine Insurance Co. Ltd.*,[38] the charterparty was frustrated by the stranding of and damage to the ship. In a number of cases a charterparty has been held to have been frustrated by the inability of the ship to leave port, due, for example, to the refusal of a foreign government to allow the ship to depart,[39] or to the outbreak of hostilities, as happened in 1980 when some sixty ships were trapped in the Shatt-el-Arab river upon the outbreak of war between Iran and Iraq,[40] or to the arrest of the ship.[41] More difficulty, however, arises where strikes prevent the loading or unloading of the ship. The charterer of a ship usually undertakes in the contract to load and unload the cargo within a specified number of days, and, in default, to pay a certain sum of money to the shipowner by way of 'demurrage'. If strikes occur at the port of loading or discharge, this does not (in the absence of any express provision to the contrary) absolve the charterer from his liability to pay demurrage in respect of the delay.[42] However, a prolonged strike may in exceptional circumstances frustrate a charterparty, that is if the delay is such as to make further performance something radically different from that which was undertaken in the contract.[43] Prolongation of a voyage by interruption of the contemplated route might also bring about frustration, but did not do so, for example, where the blocking of the Suez Canal necessitated a voyage round the Cape, since the alternative route was not fundamentally different, but merely longer and more expensive.[44]

[36] [1919] A.C. 435, at p. 454. See also the *Tamplin* case (*supra*, n. 33), at p. 405.

[37] *International Sea Tankers Inc.* v. *Hemisphere Shipping Co. Ltd.* [1982] 1 Lloyd's Rep. 128, at pp. 131, 133, 135. The alternative tests were discussed by Diplock J. in *Port Line Ltd.* v. *Ben Line Steamers Ltd.* [1958] 2 Q.B. 146. See also *post*, pp. 517–18.

[38] (1874) L.R. 10 C.P. 125, *ante*, p. 505.

[39] *Embiricos* v. *Reid (Sydney) & Co.* [1914] 3 K.B. 45; *Scottish Navigation Co.* v. *Souter* [1917] 1 K.B. 222; *Lloyd Royal Belge* v. *Stathatos* (1917) 34 T.L.R. 70.

[40] *International Sea Tankers Inc.* v. *Hemisphere Shipping Co. Ltd.* [1983] 1 Lloyd's Rep. 400; *Kodros Shipping Cpn. of Monrovia* v. *Empresa Cubana de Fletes* [1983] 1 A.C. 736; *Finelvet A.G.* v. *Vinava Shipping Co. Ltd.* [1983] 1 W.L.R. 1469.

[41] See *Adelfamar S.A.* v. *Silos E. Mangimi Martini S.p.A. (The Adelfa)* [1988] 2 Lloyd's Rep. 466.

[42] *Budgett & Co.* v. *Binnington & Co.* [1891] 1 Q.B. 35.

[43] *The Penelope* [1982] P. 180; *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.* [1982] A.C. 724.

[44] *Ocean Tramp Tankers Cpn.* v. *V/O Sovfracht (The Eugenia)* [1964] 2 Q.B. 226, overruling *Société Franco Tunisienne D'Armement* v. *Sidermar S.p.A.* [1961] 2 Q.B. 278. See also *Palmco Shipping Inc.* v. *Continental Ore Cpn* [1970] 2 Lloyd's Rep. 21.

(v) Sale and carriage of goods

Similar principles have been applied to contracts for the sale of goods to be carried by sea. In *Nickoll* v. *Ashton Edridge & Co.*,[45] for example, a cargo sold by the defendants to the plaintiffs was to be shipped 'per steamship *Orlando* . . . during the month of January'. Without default on the defendant's part the ship was so damaged by stranding as to be unable to load in January. It was held that in these circumstances the contract must be treated as at an end.

The Anglo-French invasion of Egypt in 1956 and the consequent closure of the Suez Canal led to a number of cases concerning the frustration of c.i.f. contracts[46] for the sale of goods. Among these was the case of *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.*:[47]

The appellants agreed to sell to the respondents a quantity of groundnuts to be shipped from the Sudan to Hamburg during November or December 1956. On 2 November, the Suez Canal was closed and remained closed for the next 5 months. The price of the groundnuts c.i.f. Hamburg was clearly calculated on the basis of shipment *via* the canal, but the contract contained no term to this effect. The appellants refused to perform the contract, claiming that it had been frustrated by the closure of the canal.

The House of Lords held there was no frustration, since it would still be possible to ship the nuts to Hamburg around the Cape of Good Hope. Such a journey would not be commercially or fundamentally different from that by the canal, but merely more expensive. Their Lordships also pointed out that the contract was one of sale of goods, the transport of which is normally of no direct concern to the buyer. Nevertheless, they indicated that, if the goods had been perishable or if a definite date had been fixed for delivery, the contract might possibly have then been frustrated by the necessity for the longer Cape route.

(vi) Building contract

Further instances of the doctrine of frustration are provided by a group of cases concerning building or construction contracts. Events may occur which hold up completion of the works. Such delays inevitably increase the contractor's costs. If the contract is a fixed-price contract, the contractor may lose the profit which it expected to gain, or even be forced into loss. In *Davis Contractors Ltd.* v. *Fareham U.D.C.*:[48]

In July 1946, the appellants entered into a contract with the respondents to build seventy-eight houses for a fixed sum of £94,424. Owing to the unexpected shortage of skilled labour and of certain materials the contract took 22 months to complete instead of the 8 months expected, and cost some £115,000. The appellants contended that the contract had been frustrated and that they were entitled to claim on a *quantum meruit* for the cost actually incurred.

The House of Lords refused to accept this contention. The mere fact that unforeseen circumstances had delayed the performance of the contract, and rendered it

[45] [1901] 2 K.B. 126.

[46] 'C.i.f.' stands for cost, insurance, and freight. In a c.i.f. contract the price will be agreed on the basis that it includes insurance of the goods while in transit and the expenses of carriage (freight) to the port of destination.

[47] [1962] A.C. 93, overruling *Carapanayoti & Co. Ltd.* v. *E. T. Green Ltd.* [1959] 1 Q.B. 131.

[48] [1956] A.C. 696.

more onerous to the appellants, did not discharge the agreement. The ultimate situation was still within the scope of the contract; the thing undertaken was not, when performed, different from that contracted for.

These strict requirements were, however, fulfilled in the case of *Metropolitan Water Board* v. *Dick, Kerr & Co. Ltd.*:[49]

Messrs. Dick, Kerr & Co. contracted with the Metropolitan Water Board to construct a reservoir within 6 years. Two years elapsed when the Minister of Munitions, acting under statutory powers, required them to cease work on their contract and to remove and sell their plant. The Board brought an action claiming that the contract still continued.

The House of Lords held that the interruption created by the prohibition was of such a character and duration as to make the contract, if resumed, in effect a different contract, and that the original contract was therefore discharged.

(vii) Change in the law

Finally, the performance of a contract is sometimes made legally impossible either by a change in the law or by a change in the operation of the law by reason of new facts supervening. The law may actually forbid the doing of some act undertaken in the contract;[50] or it may take from the control of the promisor something in respect of which it has contracted to act or not to act in a certain way, as, for example, where a piece of land subject to a restrictive covenant against building is compulsorily acquired and built upon by Act of Parliament.[51] Such cases are explained by policy and 'the elementary proposition that if further performance of a contract becomes impossible by legislation having that effect the contract is discharged'.[52]

For there to be frustration, the change in the law must be such as to strike at the root of the agreement, and not merely to suspend or hinder its operation in part. So it has been held that a 99 year building lease was not frustrated by Government restrictions on building for only a small part of the term,[53] and that the rights of a payee of a cheque drawn on a bank in Holland were not discharged by an enemy invasion and occupation of that country rendering presentation for payment there illegal, but not elsewhere.[54] Lesser interruptions may, however, be covered by provisions in the contract, for instance clauses providing a seller with an excuse for non-performance in the event of 'prohibition of export . . . preventing fulfilment',[55] although, as will be seen, the presence of such a clause may preclude the application of the doctrine of frustration.

[49] [1918] A.C. 119.

[50] *Denny, Mott & Dickson Ltd.* v. *Fraser (James B.) & Co. Ltd.* [1944] A.C. 265.

[51] *Baily* v. *De Crespigny* (1869) L.R. 4 Q.B. 180. See also *Brown* v. *London Cpn.* (1862) 13 C.B.N.S. 828; *Studholme* v. *South Western Gas Board* [1954] 1 W.L.R. 313.

[52] *Reilly* v. *The King* [1934] A.C. 176, *per* Lord Atkin at p. 180. On the implications for the theoretical basis of the doctrine, see *post*, pp. 513–14.

[53] *Cricklewood Property and Investment Trust Ltd.* v. *Leighton's Investment Trust Ltd.* [1945] A.C. 221; *post*, p. 524. See also, *Libyan Arab Foreign Bank* v. *Bankers Trust Co.* [1989] 1 Q.B. 728, *per* Staughton J., at p. 772.

[54] *Cornelius* v. *Banque Franco-Serbe* [1942] 1 K.B. 29. See also *Arab Bank Ltd.* v. *Barclays Bank* [1954] A.C. 495 (accrued rights not destroyed).

[55] On such clauses, see *Bremer Handelgesellschaft mbH* v. *Vanden Avenne-Izegem P.V.B.A.* [1978] 2 Lloyd's Rep. 109; *Bremer Handelgesellschaft mbH* v. *C. Mackprang Jr.* [1979] 1 Lloyd's Rep. 221; *Bremer Handelgesellschaft mbH* v. *Westzucker GmbH (No. 3)* [1989] 1 Lloyd's Rep. 198, and Treitel, *Frustration and Force Majeure* (1994) §12-025 ff.

Effect of war

The outbreak of war is another event which, by changing the operation of the law, may have the effect of abrogating obligations outstanding under a contract by reason of supervening illegality, if one of the parties resides in this country and the other in enemy or enemy-occupied territory, and the contract is one which involves commercial dealings with the enemy.[56] So strong are the public policy considerations in this situation that the contract will be wholly frustrated, even though the parties themselves provide that their obligations shall be merely postponed.[57]

Performance of only one party affected

The illustrations above show that, save in cases of supervening illegality, a frustrating event often only affects the ability of one of the parties to perform, while the other party, who usually has to pay money, is still capable of performing. So, in the requisitioning cases considered above, the charterers were able to pay the hire, and may have been willing to do so notwithstanding the non-availability of the ship, since the rate paid by the Government for requisitioned ships was higher than that payable under the charter.[58] Nevertheless, if the event is a frustrating one, it excuses both parties even where this may be to the advantage of the party who is unable to perform.

II. The Test for Frustration

(a) Theoretical Basis

Tests or 'theories' of frustration

Considerable judicial attention has been paid to the theoretical basis on which the doctrine of discharge of a contract by frustration rests, perhaps because of a perceived need to explain why a finding of frustration does not constitute a reallocation of risks nor permit an escape from a bad bargain.[59]

Successive pronouncements of the House of Lords have set forth a number of learned, but often contradictory, opinions concerning this issue and a number of theories have been put forward at various times. Since there is now general agreement on the appropriate test to be applied, it is necessary to refer only briefly to the four principal tests or 'theories' which have been advanced.[60]

(i) Implied term

At one time the preponderance of judicial opinion favoured the view that frustration of a contract depended upon the implication of a term although, as we have noted, this did not explain discharge where the performance of the contract

[56] *Ertel Bieber & Co.* v. *Rio Tinto Co. Ltd.* [1918] A.C. 260; *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.* [1943] A.C. 32 (*post*, p. 528); McNair and Watts, *The Legal Effects of War*, 4th edn. (1966), ch. 3.

[57] *Ertel Bieber & Co.* v. *Rio Tinto Co. Ltd.* (*supra*, n. 56).

[58] *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Co. Ltd.* [1916] 2 A.C. 397, at p.p. 405, 410, 422; *Bank Line Ltd.* v. *Capel (A.) & Co.* [1919] A.C. 435, *ante*, p. 509.

[59] *Pacific Phosphates Co. Ltd.* v. *Empire Transport* (1920) 4 L.L.R. 189, at p. 190.

[60] In *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675, Lord Hailsham L.C. stated, at p. 687, there were at least five theories; in addition to those considered *infra*, he referred to and rejected one based on total failure of consideration.

is made *legally* impossible by a change in the law or its operation.[61] The following passage from the speech of Lord Loreburn in *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Co. Ltd.*[62] is generally considered to be the classic exposition of the reasons on which the implied term theory of frustration was based:

> [A] Court can and ought to examine the contract and the circumstances in which it was made, not of course to vary, but only to explain it, in order to see whether or not from the nature of it the parties must have made their bargain on the footing that a particular thing or state of things would continue to exist. And if they must have done so, then a term to that effect will be implied, though it be not expressed in the contract . . . Sometimes it is put that performance has become impossible and that the party concerned did not promise to perform an impossibility. Sometimes it is put that the parties contemplated a certain state of things which fell out otherwise. In most of the cases it is said that there was an implied condition in the contract which operated to release the parties from performing it, and in all of them I think that was at bottom the principle upon which the Court proceeded. It is in my opinion the true principle, for no Court has an absolving power, but it 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, they 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'?

A contract would therefore be frustrated if a term could be implied that, in the events that subsequently happened, the contract would come to an end. The expression 'an implied term' is, however, ambiguous. It may be used in a subjective sense, that is to say, it may mean a term which the Court reads into the contract in order to give effect to what it regards as the parties' real intention at the time of contracting. As was said in a later case[63] 'the law is only doing what the parties really (though subconsciously) meant to do for themselves'. To such an implied term a number of objections may be raised. In particular, it is difficult to see how the parties could be taken, even impliedly, to have provided for something which never occurred to them.[64] Moreover, had it occurred to them, it is unlikely that they would have agreed that the contract was to come to an end. Lord Wright said:[65]

[61] In the heyday of the implied contract theory they were sometimes said to differ from other categories of frustration: *Joseph Constantine S.S. Line Ltd.* v. *Imperial Smelting Corporation Ltd.* [1942] A.C. 154, at p. 163. In the 20th edition of this book they were said not to be cases of frustration.

[62] [1916] 2 A.C. 397, at pp. 403–4, see *ante*, p. 509 for the facts. For recent support for this theory, see Smith [1994] C.L.J. 400, at p. 403.

[63] *Hirji Mulji* v. *Cheong Yue S.S. Co. Ltd.* [1926] A.C. 497, at p. 504.

[64] *Davis Contractors Ltd.* v. *Fareham U.D.C.* [1956] A.C. 696, at p. 728. Also see the example given by Lord Sands in *James Scott & Sons Ltd.* v. *Del Sel*, 1922 S.C. 592, at p. 597: 'A tiger has escaped from a travelling menagerie. The milkgirl fails to deliver the milk. Possibly the milkman may be exonerated from any breach of contract: but, even so, it would seem hardly reasonable to base that exoneration on the ground that "tiger days excepted" must be held as if written into the milk contract'. See further, *F.C. Shepherd & Co. Ltd.* v. *Jerrom* [1987] 1 Q.B. 301 *per* Mustill L.J at p. 322.

[65] *Denny, Mott & Dickson Ltd.* v. *Fraser (James B.) & Co. Ltd.* [1944] A.C. 265, at p. 275.

It is not possible, to my mind, to say that if they had thought of it, they would have said: 'Well, if that happens, all is over between us'. On the contrary, they would almost certainly on the one side or the other have sought to introduce reservations or qualifications or compensations.

That this is so is shown by the widespread use of *force majeure* clauses which specify what is to happen on the occurrence of an event which affects one or both parties' performance.

On the other hand, the implied term may be formulated more objectively. It may mean a term which, in the light of the events which have actually arisen, the parties *as reasonable people* would have imported into the contract to deal with that possibility.[66] When used in this sense, the implied term is betrayed by a similar artificiality. The 'reasonable person' has no real existence and represents 'no more than the anthropomorphic conception of justice'; an opinion ascribed to such a person is, in fact, that of the Court, which is and must be the spokesman of the fair and reasonable person.[67] An implied term of this sort is no more than a fiction, something added to the contract by the law.

Operation of law

In truth, the discharge of a contract by frustration occurs, not because of the actual or imputed will of the parties, but by operation of law. The doctrine of frustration is, as Lord Sumner pointed out, 'a device, by which the rules as to absolute contracts are reconciled with a special exception which justice demands'.[68] In declaring a contract to have been frustrated, the Court exercises a positive function: it releases the parties from further performance of the obligations which they would otherwise be bound to perform.

(ii) 'Just & reasonable result'

Recognition of these facts led certain of the judges (and notably Lord Wright and Lord Denning) to the conclusion that the basis of the doctrine of frustration was the desire of the Courts to reach a just and reasonable result.[69] 'The truth is', Lord Wright said,[70] 'that the Court or jury as a judge of fact decides the question in accordance with what seems just and reasonable in its eyes'. This view, however, might be taken to suggest that a Court had the power to release the parties from their obligations whenever it was just and reasonable to do so,[71] even, for example, where the only effect of the subsequent event had been to render the contract financially more onerous than the parties had anticipated. But it is clear that the circumstances in which a contract will be held to have been frustrated are far more limited in scope.[72]

[66] *Dahl* v. *Nelson, Donkin & Co.* (1881) 6 App. Cas. 38, at p. 59.

[67] *Davis Contractors Ltd.* v. *Fareham U.D.C.* [1956] A.C. 696, *per* Lord Radcliffe at p. 728.

[68] *Hirji Mulji* v. *Cheong Yue S.S. Co. Ltd.* [1926] A.C. 497, at p. 510.

[69] *Joseph Constantine Steamship Line Ltd.* v. *Imperial Shipping Corporation Ltd.* [1942] A.C. 154, at p. 186.

[70] *Legal Essays and Addresses* (1939), p. 259. See also *Denny, Mott & Dickson Ltd.* v. *Fraser (James B.) & Co. Ltd.* [1944] A.C. 265, at pp. 274–6.

[71] *British Movietonews Ltd.* v. *London and District Cinemas Ltd.* [1951] 1 K.B. 190, at pp. 201–2 (disapproved on appeal: [1952] A.C. 166).

[72] See *Notcutt* v. *Universal Equipment Co. (London) Ltd.* [1986] 1 W.L.R. 641, at pp. 646–7, where the Court of Appeal rejected an argument to the effect that, before a court could determine that a contract was frustrated, it must be shown that it would be unjust to hold the parties to the contract.

(iii) Foundation of the contract

Some test was, therefore, required which would recognize that frustration did not depend on the intentions of the parties, but which would not permit contracts to be too easily discharged. The first such test to be formulated was that of the 'disappearance of the foundation of the contract'. The question to be asked was whether the events that had occurred were of a character and extent so sweeping as to cause the foundation of the contract to disappear.[73] It was adopted, for example, by Goddard J. in *W. J. Tatem Ltd.* v. *Gamboa*:[74]

During the Spanish civil war, the plaintiffs chartered to the defendant, acting on behalf of the Republican Government of Spain, a steamship, for 30 days from 1 July 1937. The ship was to be used for the evacuation of refugees from Northern Spain to French ports. The hire was to be at the rate of £250 a day and was payable until the ship was returned to the plaintiffs. On 14 July, the ship was seized by the Nationalists and detained in the port of Bilbao until 11 September. In answer to the plaintiffs' claim for hire, the defendant pleaded that the contract had been frustrated.

Goddard J. was prepared to assume that the circumstances of the contract (including the very high rate of hire) showed that the parties contemplated that seizure and detention of the vessel might occur. He nevertheless held that the contract was frustrated: the foundation of the contract was destroyed by the seizure, as the defendant thereafter no longer had the use of the vessel. The expression 'foundation' of the contract is, however, imprecise, and it leaves open the question what is the foundation of the contract in a particular case. Moreover, the test is difficult to apply to situations other than those in which the subject-matter of the contract ceases to be available. It has, therefore, been rejected by the House of Lords.[75]

(iv) Radical change in the obligation

There is now general agreement that the appropriate test to apply to determine whether a contract has been frustrated is that of a 'radical change in the obligation'. In *Davis Contractors Ltd.* v. *Fareham U.D.C.*, Lord Radcliffe said:

Frustration occurs whenever the law recognizes that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. *Non haec in foedera veni.* It was not this that I promised to do.[76]

[73] *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Co. Ltd.* [1916] 2 A.C. 397, at p. 406; see also *Russkoe Obschestvo D'lia Izgstovlenia Snariadov I'voennick Pripassou* v. *John Stirk & Sons Ltd.*(1922) 11 Ll. L.R. 214, at p. 217.

[74] [1939] 1 K.B. 132.

[75] *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675.

[76] [1956] A.C. 696, at p. 729, for the facts, see *ante*, p. 511. The Latin phrase is said to be drawn from *The Aeneid*, Book 4, lines 338–9 (see Sir John Megaw, letter to *The Times*, 20 December 1980). But whether the relationship between Aeneas and Queen Dido was affected by a supervening event (Mercury's intervention) or an initial mistake (as to the nature of the relationship) is not entirely clear. Neither is it clear that Aeneas's 'excuses' for his planned desertion of Queen Dido, were as shabby as many (from Ovid to Sir John Megaw) consider them to be; see Williams, *Tradition and Originality in Roman Poetry* (Oxford, 1968) pp. 378–6 and John Sparrow, Jackson Knight Memorial Lecture, *Dido* v. *Aeneas*: *the case for the defence* (Abbey Press, 1973).

This approach has been adopted by the House of Lords in several cases,[77] and the same test was set out, at somewhat greater length, by Lord Simon in *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.*:[78]

> Frustration of a contract takes place when there supervenes an event (without default of either party and for which the contract makes no sufficient provision) which so significantly changes the nature (not merely the expense or onerousness) of the outstanding contractual rights and/or obligations from what the parties could reasonably have contemplated at the time of its execution that it would be unjust to hold them to the literal sense of its stipulations in the new circumstances; in such a case the law declares both parties to be discharged from further performance.

This test has sometimes been called the 'construction' theory, because it requires the Court first to construe the terms of contract in the light of its nature and the relevant surrounding circumstances when it was made. The original obligation undertaken by the parties can thus be determined. The Court must then consider whether there would be a radical change in that obligation if performance were enforced in the circumstances which have subsequently arisen. A mere rise in cost or expense will not suffice. 'It is not hardship or inconvenience or material loss itself which calls the principle of frustration into play. There must be as well such a change in the significance of the obligation that the thing undertaken would, if performed, be a different thing than that contracted for.'[79]

The test is clearly meant to be a difficult one to satisfy. It is, moreover, easier to state than to apply. 'The data for decision are, on the one hand, the terms and construction of the contract, read in the light of the then existing circumstances, and on the other hand the events which have occurred.'[80] If the parties have themselves provided for the situation that has arisen the contract governs and there is no frustration. If they have not provided for it then the new situation must be compared with the situation for which they did provide to see how different it is.[81] The comparison is between the rights and obligations of the parties after the event, assuming the contract still binds them, and what their rights and obligations would have been had the event not occurred. We have noted the factors taken into account in contracts of employment.[82] In contracts for the carriage of goods by sea and charterparties, account may be taken of the extent to which the goods carried or to be carried are liable to damage or to deterioration,[83] or are

[77] *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.* [1962] A.C. 93, at p. 131; *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675, at pp. 688, 700, 717; *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.* [1982] A.C. 724, at pp. 744, 745, 751; *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* [1983] 1 A.C. 854, 909, 918. See also *William Sindall plc* v. *Cambridgeshire County Council* [1994] 1 W.L.R. 1016 at p. 1039 (C.A.).

[78] [1981] A.C. 675, at p. 700, for the facts, see *post*, p. 525.

[79] *Davis Contractors Ltd.* v. *Fareham U.D.C.* (*supra*, n. 76), *per* Lord Radcliffe at p. 729. See also *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.* [1962] A.C. 93.

[80] *Heyman* v. *Darwins* [1942] A.C. 356, at p. 383.

[81] *Ocean Tramp Tankers Corporation* v. *V/O Sovracht, (The Eugenia)* [1964] 2 Q.B. 226, *per* Lord Denning M.R. at p. 239.

[82] *Ante*, p. 508.

[83] *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl GmbH* [1962] A.C. 93, at pp. 115, 118 and 123. See also *Jackson* v. *Union Marine Insurance* (1874) L.R. 10 C.P. 125, at p. 146 (carriage of ice would be frustrated by shorter delay than carriage of iron rails).

subject to a seasonal market,[84] and the extent to which the vessel and crew are fit to proceed in the new circumstances. To constitute frustration, the event or events must make performance of the contract a thing 'radically' or 'fundamentally' different in a commercial sense from that undertaken by the contract. These concepts are elusive and the courts recognize that it is often difficult to draw the line[85] and that the question is one of degree.[86] It is, however, clearly more diffcult to frustrate a long-term contract than a short-term one.[87]

Similarity to test for discharge for breach

The terms 'radical' and 'fundamental' are also used to determine whether a contract may be discharged for breach of an 'intermediate' or 'innominate' term.[88] In *Hong Kong Fir Shipping Co. Ltd.* v. *Kawasaki Kisen Kaisha Ltd.*[89] Diplock L.J. stated that *Jackson* v. *Union Marine Insurance Co. Ltd.*[90] was seeking to apply to frustrating events the same standard as if they had arisen by a breach by one of them; for the purpose of discharge it is the happening of the event and not whether the event was the result of a breach that is crucial.[91] As, however, in the context of breach, factors other than the ratio of failure to the performance undertaken are relevant to the question of whether the breach is fundamental, in practice it is more likely than not that there will be differences between cases of frustration and cases of breach.

Question of law

The application of the 'radical change in the obligation' test is a matter of law; but once it is shown that a judge or arbitrator has correctly applied the test to the facts found by him, an appellate Court should be slow to differ from his conclusion.[92]

(b) Incidence of Risk

Risk

The doctrine of frustration is principally concerned with the incidence of risk—who must take the risk of the happening of the supervening event? The Courts have therefore to determine whether the contract, on its true construction, has made provision for that risk. We have noted that increased expense, even if caused by wholly abnormal fluctuations in prices, does not frustrate.[93] In this connection, the cases show that a number of difficult questions may arise.

[84] *Jackson* v. *Union Marine Insurance* (1874) L.R. 10 C.P. 125, at p. 115. See also *ibid.* at p. 146.

[85] *Ocean Tramp Tankers Corporation* v. *V/O Sovracht (The Eugenia)* [1964] 2 Q.B. 226, at p. 239.

[86] *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675, at p. 688; *Pioneer Shipping* v. *B.T.P. Tioxide (The Nema)* [1982] A.C. 724, at p. 744.

[87] *Lord Strathcona Shipping Co. Ltd.* v. *Dominion Coal Co. Ltd.* [1926] A. C. 108, at p. 115; *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675, *per* Lord Hailsham L.C., at p. 691. See also *Larrinaga & Co.* v. *Societe Franco-Americaine des Phosphates de Medulla, Paris* (1922) 28 Com. Cas. 1, at p. 5.

[88] *Post*, p. 548 ff. See also, *ante*, p. 138.

[89] [1962] 2 Q.B. 26, on which, see *ante*, p. 548.

[90] *Ante*, p. 505.

[91] *Ibid.*, at pp. 49, 68. See also, in the same context, *The Hermosa* [1980] 1 Lloyd's R. 638, at p. 649 (delay by a variety of events, some the consequences of breach and some not).

[92] *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.* (*supra*, n. 86), at pp. 738, 752–3.

[93] *Ante*, pp. 511–12: *Davis Contractors Ltd.* v. *Fareham U.D.C.* [1956] A.C. 696, *per* Lord Reid at p. 724 and *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.* [1962] A.C. 93. But note that in the latter Lord Reid reserved his position on an increase which reached a wholly astronomical figure, and cf. *William Cory* v. *L.C.C.* [1951] 1 K.B. 8, aff'd [1951] 2 K.B. 476.

Express provision

The first question is whether a contract can be held to have been frustrated notwithstanding that the parties have, in their contract, made express provision to deal with the event that has occurred. There is little doubt that it is open to the parties (except in certain cases of illegality)[94] to provide that the contract shall continue, or be merely suspended, and not discharged, upon the occurrence of a particular event, or to allocate the risks attendant upon that event. Where the contract makes provision (that is, full and complete provision, so intended) for a given contingency, this will preclude the Court from holding that the contract is frustrated.[95] But the parties may fail to make complete provision, as happened in the *Bank Line* case,[96] where the option given to one party, i.e. the charterers, to cancel or continue with the charterparty if the ship should be requisitioned, was held not to be intended to apply to requisitioning of so long a duration as to make the charter, as a matter of business, a wholly different thing. And a provision in a building contract, for example, that the contractor is to be allowed an extension of time in the event of 'delays', may be construed as inapplicable to a situation where the delay which occurs is such to bring about a radical change in the obligation.[97] In such cases, the contract can still be frustrated.

Foreseen events

The second question is whether events which were foreseen by the parties at the time of contracting can be relied upon to establish frustration. In many of the cases reference is made to the occurrence of an 'unforeseen' or 'unexpected' or 'uncontemplated' event, and it may be argued that the parties must be taken to have assumed the risk of an event which was present to their minds at the time the contract was made. It is, however, a question of construction of the contract whether it was intended to continue to be binding in that event,[98] or whether, in the absence of any express provision, the issue has been left open,[99] so as to allow the incidence of risk to be determined by the law relating to frustration. In *W. J. Tatem Ltd.* v. *Gamboa*,[100] for example, the fact that seizure of the ship was within the contemplation of the parties did not preclude the operation of frustration since the contract made no express provision for the contingency.

[94] See *ante*, p. 512.

[95] *Bank Line Ltd.* v. *Capel (A.) & Co.* [1919] A.C. 435, at p. 455; *Joseph Constantine Steamship Line Ltd.* v. *Imperial Smelting Corporation Ltd.* [1942] A.C. 154, at p. 163. See also *Bangladesh Export Import Co. Ltd.* v. *Sucden Kerry S.A.* [1995] 2 Lloyd's Rep. 1.

[96] [1919] A.C. 435; *ante*, p. 509. See also *Jackson* v. *Union Marine Insurance Co. Ltd.* (1874) L.R. 10 C.P. 125 (clause excusing one party only from liability in a given contingency).

[97] *Metropolitan Water Board* v. *Dick, Kerr & Co. Ltd.* [1918] A.C. 119; *ante*, p. 512.

[98] *Larrinaga & Co.* v. *Société Franco Americaine des Phosphates de Medulla* (1923) 39 T.L.R. 316; *Maritime National Fish Ltd.* v. *Ocean Trawlers Ltd.* [1935] A.C. 524; *Chandler Bros. Ltd.* v. *Boswell* [1936] 3 All E.R. 179; *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* [1983] 1 A.C. 854, at p. 909.

[99] *W. J. Tatem Ltd.* v. *Gamboa* [1939] 1 K.B. 132, at p. 138; *Ocean Tramp Tankers Corporation* v. *V/O Sovfracht (The Eugenia)* [1963] 2 Q.B. 226, at p. 239; *The Nile Co. for the Export of Agricultural Crops* v. *H. & J.M. Bennett (Commodities) Ltd.* [1986] 1 Lloyd's Rep. 555 at p. 582; *Adelfamar S.A.* v. *Silos E. Mangimi Martini SpA (The Adelfa)* [1988] 2 Lloyd's Rep 466 at p. 471.

[100] [1939] 1 K.B. 132; *ante*, p. 516.

No common assumption

The third question is whether a contract will be frustrated by an event which prevents performance in a manner intended by one party alone. In *Blackburn Bobbin Co. Ltd.* v. *Allen (T. W.) & Sons Ltd.*:[101]

> The defendants agreed to sell and deliver to the plaintiffs at Hull a quantity of Finnish birch timber. They found it impossible to fulfil this contract because the outbreak of war cut off their source of supply from Finland. The plaintiffs were unaware that timber from Finland was normally shipped direct from a Finnish port to England, and that timber merchants did not, in practice, hold stocks of it in England.

The Court of Appeal held that there was no frustration. What had happened was merely that an event had occurred which rendered it practically impossible for the defendants to deliver: that event might have been, but was not, provided for in the contract. To free the defendants from liability, it would have to be shown that the continuance of the normal mode of shipping the timber from Finland was a matter which *both* parties contemplated as necessary for the fulfilment of the contracts. Since this was not the case, the defendants bore the risk.

Delay

Fourthly, there is the question of delay.[102] Frequently, as we have seen, a subsequent event causes delay in the performance of the contract, bringing financial loss to one of the parties. But the risk of delay is one which has to be accepted in commercial transactions. Lord Sumner said:[103]

> Delay even of considerable length and of wholly uncertain duration is an incident of maritime adventure, which is clearly within the contemplation of the parties . . . so much so as to be often the subject of express provisions. Delays such as these may very seriously affect the commercial object of the adventure, for the ship's expenses and overhead charges are running on . . . None the less this is not frustration.

The delay must be such as 'to render the adventure absolutely nugatory',[104] 'to make it unreasonable to require the parties to go on',[105] 'to destroy the identity of the work or service when resumed with the work or service when interrupted',[106] 'to put an end in a commercial sense to the undertaking'.[107] It may, however, be difficult for the parties to determine whether, at any particular point of time, the delay is of this nature. On this point, Lord Roskill, in *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.*,[108] has provided guidance:

[101] [1918] 2 K.B. 467. It was also said in this case that there could never be frustration of a contract for the sale of unascertained goods, but this is probably too wide: see *Re Badische Co. Ltd.* [1921] 2 Ch. 331; *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.* [1962] A.C. 93; *ante*, p. 511.

[102] See Stannard (1983) 46 M.L.R. 738.

[103] *Bank Line Ltd.* v. *Capel (A.) & Co.* [1919] A.C. 435, at p. 458.

[104] *Bensaude & Co.* v. *Thames and Mersey Marine Insurance Co.* [1897] 1 Q.B. 29, *per* Lord Esher at p. 31; [1897] A.C. 609, at pp. 611, 612, 614.

[105] *Metropolitan Water Board* v. *Dick, Kerr & Co. Ltd.* [1918] A.C. 199, *per* Lord Atkinson at p. 131; *F. A. Tamplin Steamship Co. Ltd.* v. *Anglo-Mexican Petroleum Products Co. Ltd.* [1916] 2 A.C. 397, *per* Lord Loreburn at p. 405.

[106] *Metropolitan Water Board* v. *Dick, Kerr & Co. Ltd.* (*supra*, n. 105), *per* Lord Dunedin at p. 128; *Bank Line Ltd.* v. *Capel (A.) & Co.* [1919] A.C. 435, *per* Lord Sumner at p. 460.

[107] *Jackson* v. *Union Marine Insurance Co. Ltd.* (1874) L.R. 10 C.P. 125.

[108] [1982] A.C. 724, at p. 752.

It is often necessary to wait upon events in order to see whether the delay already suffered and the prospects of further delay from that cause will make any ultimate performance of the relevant contractual obligations 'radically different' . . . from that which was undertaken by the contract. But, as has often been said, business men must not be required to await events too long. They are entitled to know where they stand. Whether or not the delay is such as to bring about frustration must be a question to be determined by an informed judgment based upon all the evidence of what has occurred and what is likely thereafter to occur.

While, therefore, it is for the tribunal to whom the issue has been referred to decide as a question of law whether or not the contract has been frustrated, 'that conclusion is almost completely determined by what is ascertained as to mercantile usage and the understanding of mercantile men'[109] about 'the significance of the commercial differences between what was promised and what in the changed circumstances would now fall to be performed'.[110]

Even where the delay is *prima facie* sufficient, where both parties are responsible for it, the rule that reliance cannot be placed on a self-induced frustration will preclude discharge.[111]

Inflation

Finally, some mention must be made of the effects of inflation. In *Staffordshire Area Health Authority* v. *South Staffordshire Waterworks Co.*[112] a contract was entered into in 1929 under which the defendants agreed 'at all times hereafter' to supply water to a hospital at a fixed price of seven (old) pence per 1,000 gallons. By 1978 the equivalent cost of supplying the water was some twenty times the contract price. The Court of Appeal held that the contract was, on its true construction, terminable by the defendants upon reasonable notice.[113] But Lord Denning M.R. expressed the opinion[114] that, by reason of 50 years of continuing inflation, a fundamentally different situation had emerged in which the contract had ceased to bind. His reasoning was not, however, accepted by the other members of the Court of Appeal, and the orthodox view is that any depreciation in the purchasing power of sterling,[115] or the devaluation of a foreign currency in which a debt is expressed,[116] is a risk which must be borne by the creditor.

(c) Self-Induced Frustration

Self-induced frustration

It is well established that a party whose act or election has given rise to the event which is alleged to have frustrated the contract cannot invoke the doctrine of

[109] *Tsakiroglou & Co. Ltd.* v. *Noblee Thorl G.m.b.H.* (*supra*, n. 101), at p. 124.
[110] *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.* (*supra*, n. 108).
[111] *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* [1983] 1 A.C. 854. See *post*, p. 521.
[112] [1978] 1 W.L.R. 1387.
[113] On the implication of a term to this effect (less likely where there is a price variation clause), see *ante*, pp. 501–2.
[114] At pp. 1397–8. He did not, however, hold that the contract was terminated automatically (see *post*, p. 526), but only on reasonable notice.
[115] *Wates Ltd.* v. *G.L.C.* (1987) 25 Build. L.R. 1, at p. 35.
[116] *British Bank for Foreign Trade Ltd.* v. *Russian Commercial and Industrial Bank* (1921) 38 T.L.R. 65; *Re Chesterman's Trusts* [1923] 2 Ch. 466.

frustration; reliance cannot be placed upon a self-induced frustration.[117] In *Maritime National Fish Ltd.* v. *Ocean Trawlers Ltd.*:[118]

> The respondent chartered to the appellant a steam trawler fitted with an otter trawl. Both parties knew at the time of the contract that it was illegal to use an otter trawl without a licence from the Canadian Government. Some months later the appellant applied for licences for five trawlers which it was operating, including the respondent's trawler and three trawlers owned directly or indirectly by the appellant. It was informed that only three licences would be granted, and was requested to state for which of the three trawlers it desired to have licences. It named two trawlers that it owned directly or indirectly and a third chartered from a person other than the respondent, and then claimed that it was no longer bound by the charterparty as its object had been frustrated.

The Judicial Committee of the Privy Council held that the failure of the contract was the result of the appellant's own election, and that since 'reliance cannot be placed upon a self-induced frustration' there was no frustration. Similar conclusions have been reached where, in breach of contract, a charterer of a ship allowed the ship to enter a war-zone, where she was trapped,[119] and where parties to arbitration proceedings were in breach of their mutual contractual obligations to apply to the arbitral tribunal for directions to prevent delay in the conduct of the arbitration.[120]

Choosing between different contracts

The position is more complicated where a party enters into a number of contracts and the supervening event means that, while it is possible to perform one or more of the contracts, it is not possible to perform them all. This was the position in *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)*:[121]

> In July 1980 the defendant contracted with the plaintiff to carry a drilling rig from Japan to a location off Rotterdam using, at its option, either the *Super Servant One* or the *Super Servant Two*. It also entered into two contracts with third parties containing similar substitution clauses, one before the contract with the plaintiff and one afterwards. In its internal schedules the defendant planned to use the *Super Servant Two* for the plainiff's contract and the *Super Servant One* for the other two contracts, but, prior to the time set for performance, the *Super Servant Two* sank. The defendant informed the plaintiff that

[117] *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep. 1 at p. 8. But where the relevant act is caused by a third party for whose action the party claiming frustration is not responsible the result is not considered to be self-induced frustration: *Adelfamar S.A.* v. *Silos E. Mangimi Sp.A. (The Adelfa)* [1988] 2 Lloyd's Rep. 466 at p. 471.

[118] [1935] A.C. 524 (see [1934] 1 D.L.R 621, esp. at p. 623 and [1934] 4 D.L.R. 288, esp. at p. 299 for a full statement of the facts). See also *Bank Line Ltd.* v. *Capel (A.) & Co.* [1919] A.C. 435, at p. 452; *Ocean Tramp Tankers Corporation* v. *V/O Sovfracht (The Eugenia)* [1964] 2 Q.B. 226, at p. 237; *Denmark Productions Ltd.* v. *Boscobel Productions Ltd.* [1969] 1 Q.B. 699, at pp. 725, 736–7; *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* [1983] 1 A.C. 854.

[119] *Ocean Tramp Tanker Corporation* v. *V/O Sovfracht (The Eugenia)* (*supra*, n. 118).

[120] *Paal Wilson & Co. A/S* v. *Partenreederei Hannah Blumenthal* (*supra*, n. 118). The position in arbitration caused difficulties in commercial practice; see *ante*, p. 31 for another, only partially successful, attempt to deal with the problem of stale arbitrations, which has now been addressed by legislation empowering the arbitrator to dismiss a claim in the case of inexcusable and inordinate delay where the delay results in a substantial risk that it would not be possible to have a fair resolution of the issues or of serious prejudice to the respondent: see now Arbitration Act 1996, s. 41 and *L'Office Cherifien Des Phosphates* v. *Yamashita-Shinnihon Steamship Co. Ltd.* [1994] 1 A.C. 486.

[121] [1990] 1 Lloyd's Rep. 1, affirming [1989] 1 Lloyd's Rep. 149.

it would not transport the rig with either the *Super Servant One* or the *Super Servant Two*, but the parties agreed, without prejudice to their rights under the contract that the drilling rig would be transported by another, more expensive, method. In answer to the plaintiff's claim for the losses suffered, the defendant counterclaimed *inter alia* that the sinking of the *Super Servant Two* frustrated the contract.

The Court of Appeal held that the contract was not frustrated. Even if the sinking of the *Super Servant Two* occurred without any fault on the part of the defendant, it was not the cause of the inability to perform. The real cause was said to be the defendant's election not to use the *Super Servant One*, something which it would have been physically possible for it to do. It was said that that exercise of choice meant that the defendant had accepted the risk of the *Super Servant Two* being unable to perform with the result that its unavailability gave rise to a breach not a frustrating event. Moreover, to allow the defendant to rely on the unavailability of the *Super Servant One* as a frustrating event would allow it to rely on its own act of election whereas frustration in theory occurs automatically.

The reasoning in this case has been criticized[122] for not taking sufficient account of the fact that, in the *Maritime National Fish* case, it was possible for the respondent to perform all contracts made with third parties, and because the rule that frustration is automatic is not an absolute one.[123] The defendant's 'election' was only as to which contract it was not going to perform and it is submitted that the decision is likely to lead to practical difficulties. It would appear to mean, for instance, where a farmer agrees to sell 250 tons of a crop to be grown on specific land which normally yields over 500 tons to A, and 250 tons to B, if there is a poor harvest and the yield is only 250 tons, that neither contract would be frustrated. But this result is difficult to reconcile with cases, apparently not considered in *The Super Servant Two*, in which neither party to a contract for the sale of a specific crop was held to be liable if the crops failed to materialize.[124] It is also difficult to reconcile with cases in which a seller who, following a partial failure of supply, delivered to other customers or delivered the available supply to all customers on a *pro rata* basis, was held entited to rely on a *force majeure* clause.[125] In the present state of the law, however, a promisor who wishes protection in the case of a partial failure of supply 'must bargain for the inclusion of a suitable *force majeure* clause in the contract'.[126]

[122] Treitel, *Frustration and Force Majeure*, §14–017. Treitel's earlier arguments on the issue were considered and rejected by the Court: [1989] 1 Lloyd's Rep. 148, at pp. 152–3, 154, 158; [1990] 1 Lloyd's Rep. 1, at pp. 9, 13–14.

[123] See *post*, p. 527.

[124] e.g. *Howell* v. *Coupland* (1876) 1 Q.B.D. 258; *H.R & S. Sainsbury Ltd.* v. *Street* [1972] 1 W.L.R. 834, on which see *post*, p. 534.

[125] *Intertradex S.A.* v. *Lesieur Tourteaux S.A.R.L.* [1978] 2 Lloyd's Rep. 509, at p. 513; *Bremer Handelgesellschaft m.b.H.* v. *Mackprang Jr. (No. 2)* [1979] 1 Lloyd's Rep. 221; *Bremer Handelgesellschaft m.b.H.* v. *Continental Grain Co.* [1983] 1 Lloyd's Rep. 169, at p. 292; *Bremer Handelgesellschaft m.b.H.* v. *Vanden Avenne-Izegem P.V.B.A.* [1978] 2 Lloyd's Rep. 109. In *The Super Servant Two* the *force majeure* cases were said to be of no assistance in the context of frustration: [1989] 1 Lloyd's Rep. 148, at 158; [1990] 1 Lloyd's Rep. 1 at p. 9. *Sed quaere*, see Hudson (1968) 31 M.L.R. 535.

[126] *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1989] 1 Lloyd's Rep. 148 *per* Hobhouse J. at p. 158, although the distinction from frustration may be put into question since his Lordship also accepted that protection might be afforded by an implied term.

Negligent acts

The rule, however, is not altogether clear when such an act was inadvertent, and merely negligent. Although there have been frequent statements to the effect that the frustrating event must occur without the 'default' of either party, this point has never been expressly decided. It was discussed by the House of Lords in *Joseph Constantine Steamship Line Ltd.* v. *Imperial Smelting Corporation Ltd.*, where Lord Russell, commenting on the kind or degree of fault which might debar a party from relying on a self-induced frustration, said:[127]

> The possible varieties are infinite, and can range from the criminality of the scuttler who opens the sea-cocks and sinks his ship, to the thoughtlessness of the prima donna who sits in a draught and loses her voice. I wish to guard against the supposition that every destruction of corpus for which a contractor can be said, to some extent or in some sense, to be responsible, necessarily involves that the resultant frustration is self-induced within the meaning of the phrase.

In that case:

> The appellant chartered to the respondent its steamship *Kingswood* to proceed to Australia and load a cargo there. Before this could be done, a violent explosion occurred in the boiler of the ship which resulted in such a delay as would discharge the contract. The cause of the explosion was never ascertained, but the respondent alleged that the appellant had first to establish that it occurred without its fault before it could rely on the doctrine of frustration and so not be liable for breach of contract.

It was not necessary for the House of Lords to decide whether mere negligence would suffice, for it held that the burden of proving that the event which causes the frustration is due to the act or default of a party lies on the party alleging it to be so. Since the respondent failed to satisfy the Court on this point, the contract was discharged. In would appear logical, however, for a finding of negligence to prevent a party claiming that the contract was frustrated where that negligent act caused the alleged frustrating event.[128]

(d) Leases and Contracts for the Sale of Land

Leases

There was at one time considerable doubt as to whether the doctrine of frustration applied to leases of land. In 1945, in *Cricklewood Property and Investment Trust Ltd.* v. *Leighton's Investment Trust Ltd.*[129] the House of Lords held unanimously that, since wartime restictions preventing the performance of a building lease cover only a small part of the 90 years remaining on the lease, it had not been frustrated. But on the question whether a lease could in any circumstances be terminated by frustration the House was evenly divided. Viscount Simon and Lord Wright considered that, on very rare occasions, frustration could occur, giving as illustrations some vast convolution of nature which might sweep the property into the sea, or the frustration of a building lease by a perpetual statutory prohibition

[127] [1942] A.C. 154, at p. 179.
[128] See *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep. 1, at p. 10.
[129] [1945] A.C. 221.

on building for the remainder of the term. Lord Russell and Lord Goddard took the contrary view. A lease was more than a contract: it vested an estate in land in the lessee, and the contractual obligations which it contained were merely incidental to the relationship of landlord and tenant. If all or some of these should become impossible of performance, the lease would remain.[130] The estate in the land would still be vested in the tenant. Lord Porter, the fifth member of the House, refused to express an opinion.

In 1981, this question was re-considered by the House of Lords in *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.*:[131]

The plaintiff let a warehouse to the defendant for 10 years from 1 January 1974. The defendant covenanted that it would not without the plaintiff's consent use the premises for any purpose other than that of warehousing in connection with its business, or assign, underlet, or part with possession. In May 1979, the local authority temporarily closed the street which provided the only vehicular access to the warehouse. The closure lasted for 20 months and during this period the warehouse could not be used for the purpose contemplated by the lease. In answer to a claim for rent, the defendant counterclaimed that the lease had been frustrated.

Their Lordships unanimously held that there was no frustration. A majority,[132] however, agreed with Viscount Simon and Lord Wright in the *Cricklewood* case that in principle the doctrine of frustration was applicable to leases, although the view was expressed[133] that in practice the doctrine would 'hardly ever' apply. In the present case, having regard to the nature and length of the interruption, and in particular to the fact that the lease would still have some 3 years to run after the interruption came to an end, it could not be said that the lease had been frustrated.

There appears to be no reported English case in which it has been held that a lease has been frustrated.[134] The reason for this may be the relative indestructibility of land. But the absence of cases of frustration is more likely to be due to the fact that the events which are most likely to occur, for example, fire,[135] are normally expressly provided for in the lease, and the incidence of the risk of less common events (such as requisitioning)[136] may be held to have been assumed by the tenant and not by the landlord. It is also very improbable that some personal incapacity which prevents the tenant from using the premises would be sufficient to terminate the lease,[137] at least if the tenant's personal occupation was not the

[130] But there may be excuses for non-performance of covenants short of frustration: *ibid.*, *per* Lord Russell, at p. 233–4; *John Lewis Properties plc.* v. *Viscount Chelsea* [1993] 2 E.G.L.R. 77, at p. 82.
[131] [1981] A.C. 675. For criticism see Price (1989) 10 J.L.H. 90, at pp. 101–3.
[132] Lord Russell of Killowen dissenting.
[133] At pp. 692, 697, 717.
[134] Cf. *Rom Securities Ltd.* v. *Rogers (Holdings) Ltd.* (1967) 205 E.G. 427 (agreement for a lease). Contrast *Tay Salmon Fisheries Co. Ltd.* v. *Speedie*, 1929 S.C. 593 (Scotland).
[135] Cf. *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* [1981] A.C. 675, 690.
[136] *Whitehall Court Ltd.* v. *Ettlinger* [1920] 1 K.B. 680; *Matthey* v. *Curling* [1922] 2 A.C. 180; *Swift* v. *Mackean* [1942] 1 K.B. 375. See also (before the *National Carriers* case) *Simper* v. *Coombs* [1948] 1 All E.R. 306; *Redmond* v. *Dainton* [1920] 2 K.B. 256 (destruction of premises).
[137] *London and Northern Estates Co.* v. *Schlesinger* [1916] 1 K.B. 20 (internment of tenant). See also *Youngmin* v. *Heath* [1974] 1 W.L.R. 135 (death).

common basis of the venture.[138] But if commercial premises are let (particularly for a short term) for one principal purpose known to the lessor, and one which gives to the premises a large part of its rental value, the failure of that purpose by legal prohibition or otherwise might be sufficient to bring about the radical change in the obligation required to frustrate the lease.

Contract for the sale of land

Similar problems arise in relation to contracts for the sale of land where a change of circumstances occurs after exchange of contracts but before completion. The risk that the premises may be destroyed or damaged, for example, by fire, is one which must be borne by the purchaser, and in respect of which it is usual to insure. It has further been held that such a contract was not frustrated when the land agreed to be sold was made the subject of a compulsory purchase order[139] and where a building intended for development was listed as being of historic or architectural interest.[140] The position is in doubt, but the answer to the question whether a contract of sale of land can be frustrated would again appear to be 'hardly ever' rather than 'never'.[141]

III. Effects of Frustration

(a) Common Law

Effects of frustration

It remains to consider the position of the parties when the performance of the contract has been frustrated.

(i) Contract generally determined automatically

In the first place, generally the contract is not merely dischargable at the option of one or other of the parties; it is brought to an end forthwith and automatically. In *Hirji Mulji* v. *Cheong Yue Steamship Co. Ltd.*:[142]

> In November 1916 shipowners chartered their ship, the *Singaporean*, agreeing that it should be placed at the charterers' disposal on 1 March 1917, for 10 months. Shortly before this date the ship was requisitioned by the Government. Believing that she would soon be released, the shipowners asked if the charterers would be willing to take up the charter. The charterers said that they would. The ship was, however, not released until February 1919, and the charterers then refused to accept her.
>
> The shipowners contended that the charterers had so conducted themselves as to oust the doctrine of frustration. But the House of Lords held that frustration, unlike breach, brings the contract to an end automatically, and could not be waived in this manner.[143]

[138] See *Sumnall* v. *Statt* (1984) 49 P. & C.R. 367, and *ante*, p. 507.
[139] *Hillingdon Estates Co.* v. *Stonefield Estates Ltd.* [1952] Ch. 627; *E. Johnson & Co. (Barbados) Ltd.* v. *N.S.R. Ltd.* [1997] A.C. 400.
[140] *Amalgamated Investment & Property Co. Ltd.* v. *John Walker & Sons Ltd.* [1977] 1 W.L.R. 164.
[141] See also *Denny, Mott & Dickson Ltd.* v. *Fraser (James B.) & Co. Ltd.* [1944] A.C. 265, at pp. 274–6 (option to purchase land).
[142] [1926] A.C. 497. See also *J. Lauritzen A.S.* v. *Wijsmuller B.V. (The Super Servant Two)* [1990] 1 Lloyd's Rep. 1 at p. 8.
[143] *Ibid.*, *per* Lord Sumner, at p. 509. See also *B.P. Exploration (Libya) Co. Ltd.* v. *Hunt* [1979] 1 W.L.R. 783, at p. 809 (waiver or estoppel could not prevent reliance on frustration).

The rule precluding a party relying on a self-induced frustration, considered above, shows that the rule that discharge is automatic is not absolute. We have seen that the party whose act or default has caused the frustrating event is not entitled to treat himself as discharged. But *F.C. Shepherd & Co. Ltd.* v. *Jerrom*,[144] shows that this will not affect the position of the other party, for whom the event is not 'self'-induced. In that case:

But not if frustrating event caused by one party

An employee was sentenced to a term of detention, and his employer stated that it would not take him back on his release. Once released, he instituted proceedings for unfair dismissal, which the employer defended *inter alia* on the ground that the contract had been frustrated by the imposition of the sentence of imprisonment.

Although it was clear that the employee could not rely on his detention as frustrating the contract of employment, it was held that the employer could.

Secondly, the effect of frustration *at common law* is to release both parties from any further performance of the contract. All obligations falling due for performance after the frustrating event occurred are discharged. In *Appleby* v. *Myers*,[145] for example:

(ii) Future obligations discharged

The plaintiffs undertook to erect certain machinery upon the defendant's premises, the agreement providing that the work was to be paid for on completion. While the work was in progress, and before it was completed, the premises and the machinery already erected were wholly destroyed by fire.

The contract was frustrated, but since it had been agreed that payment was to be made only on completion, the plaintiffs could recover nothing for the work already done.

But any legal right or obligation already accrued and due, before the frustrating event occurred, was left undisturbed. In *Chandler* v. *Webster*:[146]

But accrued obligations remain

The plaintiff agreed to hire from the defendant a room in Pall Mall to watch the Coronation procession. The price for the hire was to be £141, payable immediately. The plaintiff paid £100 of this sum, but before he paid the balance, the procession was cancelled. He claimed to recover back the money paid.

It was held not only that he could not recover the £100 already paid, but that he was also liable to pay the other £41 as this obligation had fallen due before the frustrating event occurred. In part because of the underdevelopment of restitutionary principles at that time, the Court of Appeal rejected the plaintiff's argument that he was entitled to recover the £100 in restitution as money paid under a consideration which had totally failed. The effect of the frustration was not to wipe out the contract altogether but only to release the parties from further performance, so it could not be said that the 'consideration' had failed completely.

[144] [1987] 1 Q.B. 301. See also *Joseph Constantine Steamship Line Ltd.* v. *Imperial Smelting Corporation Ltd.* [1942] A.C. 154, *per* Lord Porter, at pp. 199–200; *Notcutt* v. *Universal Equipment Co. (London) Ltd.* [1986] 1 W.L.R. 641.

[145] (1867) L.R. 2 C.P. 651. See also *Compania Naviera General S.A.* v. *Kerametal Ltd.* [1983] 1 Lloyd's Rep. 372.

[146] [1904] 1 K.B. 493.

Development of a restitutionary response

The harshness of the decision in *Chandler* v. *Webster*, which allocated all the risks of the frustrating event on the plaintiff, excited considerable criticism,[147] and in 1942 it was overruled by the House of Lords in *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.*:[148]

> The respondent contracted with the appellant, a Polish company, to manufacture certain machinery and deliver it to Gdynia. Part of the price was to be paid in advance, and the appellant accordingly paid £1,000. The contract was frustrated by the occupation of Gdynia by hostile German forces in September 1939. The appellant thereupon requested the return of the £1,000. This request was refused on the ground that considerable work had been done, and expense incurred, under the contract.

Under the rule in *Chandler* v. *Webster* this money would have been irrecoverable, as it had already been paid at the time the frustrating event occurred. The House of Lords, however, allowed the appellants to recover. It was pointed out that an action for the recovery of the sum paid was not an action on the contract, which *ex hypothesi* had ceased to exist, but an action in restitution to recover money paid on a consideration which had totally failed.[149] The House held that, in the context of a claim to recover money paid, the term 'consideration' should be understood not in the sense of the consideration which is necessary to the formation of a contract, but rather in the sense of the performance of an obligation already incurred. A party who has paid money but has received no part of the bargained-for performance, is entitled to recover it, for the consideration has totally failed.

Remaining problems at common law

The law as the *Fibrosa* case left it was still not satisfactory, for the party who had to return the pre-payment might have incurred expenses for the purpose of the performance of the contract, or might be left with goods which were made valueless by the failure of the contract.[150] Moreover, the insistence that the failure of consideration be total[151] meant that if the party seeking recovery of the money had received any part, however small, of the performance of the contract, the *Fibrosa* case did not apply, and the money was irrecoverable. It was to remedy this situation that the Law Reform (Frustrated Contracts) Act 1943 was passed.

(b) Law Reform (Frustrated Contracts) Act 1943[152]

It has been stated that the 'fundamental principle underlying the Act . . ., is prevention of the unjust enrichment of either party to the contract at the other's expense' and not the apportionment of the loss caused by the frustrating event between the parties.[153] Although it has been argued that the law is defective in not

[147] *Cantiare San Roco S.A.* v. *Clyde Shipbuilding & Engineering Co. Ltd.* [1924] A.C. 226, at p. 257.
[148] [1943] A.C. 32.
[149] See *post*, p. 605.
[150] This was probably not a problem in *Fibrosa* since, although the sellers had done a considerable amount of work in manufacuring the machines ([1942] 1 K.B. 12 at p. 14), it was accepted that they could be resold without loss: [1943] A.C. 32, at p. 49.
[151] See *post*, p. 605.
[152] See Williams, *Law Reform (Frustrated Contracts) Act 1943*; Goff and Jones, *The Law of Restitution* 4th edn. (1993), p. 450 ff; McKendrick, *Force Majeure and Frustration of Contract*, 2nd edn. (1994), ch. 11.
[153] *B.P. Exploration (Libya) Co. Ltd.* v. *Hunt (No. 2)* [1979] 1 W.L.R. 783, *per* Robert Goff J. at pp. 799–800. Cf. Lawton L.J. *ibid.* [1981] 1 W.L.R. 232.

providing for such loss-apportionment,[154] especially since the line between action in reliance on a contract which results in a benefit and action which does not can be very fine,[155] the case for a financial adjustment is stronger where such pre-frustration action has resulted in a realizable benefit in the hands of one of the parties. But in the present state of the law, it is important not to allow an over-wide interpretation of 'enrichment' or 'benefit' to operate as loss-apportionment by subsuming virtually all action taken by a contracting party in reliance on the contract.

Money paid or payable

By section 1(2) of the 1943 Act:

> 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 payable:
>
> Provided that, if the party to whom the sums were so paid or payable incurred expenses before the time of the 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.

A careful reading of this sub-section reveals that it has two effects.

In the first place, it embodies the rule in the *Fibrosa* case, although it is now no longer necessary to prove a total failure of consideration. So if A agrees to manufacture and deliver to B certain machinery, B promising to pay £10,000 down and the balance on completion, then even if A has delivered part of the machinery to B before the frustrating event occurs, B can recover the £10,000, if paid, and, if not paid, it ceases to be payable.[156]

Expenses incurred by payee

Secondly, the Act goes further than the *Fibrosa* case in that it gives to the Court a discretionary power to allow the payee to set off against the sum so paid or payable a sum not exceeding the value of any expenses which the payee has incurred in or for the purpose of performing the contract before the frustration.[157] So if, in the above example, A has incurred expenses totalling, say, £6,000, then the Court has power to permit A to recover or retain the whole or part of this sum from the £10,000 due from B under the contract. But expenses can only be set off against 'the sums so paid or payable', i.e. those due before frustration, so that if the expenses amounted to, say, £12,000, it would not be possible to charge the

[154] Williams, *Law Reform (Frustrated Contracts) Act 1943*, p. 35; McKendrick, 'Frustration, Restitution and Loss Apportionment' in Burrows, ed., *Essays on the Law of Restitution* (1991), p. 147; cf. Posner and Rosenfield (1977) 6 J.L.S. 83, at p. 112 ff (part-performer can generally evaluate the risk better and insure more cheaply than the other party); Stewart and Carter [1992] C.L.J. 66, at pp. 86–9, 109–10; Burrows, *The Law of Restitution* (1993), p. 286.

[155] *Post*, pp. 605–6.

[156] A's position may be protected by s. 1(3), on which see *infra*.

[157] 'Expenses' include a reasonable sum in respect of overhead expenses: s. 1(4), and the onus of proof lies on the payee: *Gamerco S.A.* v. *I.C.M./Fair Warning (Agency) Ltd.* [1995] 1 W.L.R. 1226, at p. 1235. See also *Lobb* v. *Vasey Housing Auxiliary (War Widows Guild)* [1963] V.R. 239 (Victoria, Australia).

£2,000 in excess of £10,000 against the unpaid balance due after the frustrating event occurred.

The approach to the proviso

In *Gamerco S.A.* v. *I.C.M./Fair Warning (Agency) Ltd.*[158] Garland J. considered three methods by which the Court should exercise its discretion; allowing the payee to retain all the expenses incurred[159] as a statutory recognition of the defence of change of poition,[160] equal division of the loss caused by the frustrating event,[161] and a broad discretion to do what the Court considers just, 'having regard to all the circumstances of the case'.[162] His Lordship favoured the third, concluding that the task of the court 'is to do justice in a situation which the parties neither contemplated nor provided for, and to mitigate the possible harshness of allowing all loss to lie where it has fallen'.[163] In *Gamerco's* case:

> $775,000 was payable by the promoters of a pop concert to the defendant group at the time the contract was frustrated, $412,500 of which had been paid. Both parties had incurred expenses before the date of frustration which was wholly wasted; the defendant $50,000, and the promoters $450,000. Neither party was left with any residual benefit or advantage.

In these circumstances, and having particular regard to the promoters' loss, and his view that there was no question of any change of position by the defendant as a result of the promoters' advance payment,[164] his Lordship made no deduction under the proviso and ordered repayment of the $412,500.

Obligations other than to pay money

Section 1(3) of the 1943 Act provides for the adjustment of the financial relations of the parties:

> 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 sub-section 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 sub-section, and
>
> (b) the effect, in relation to the said benefit, of the circumstances giving rise to frustration of the contract.

The result is that recompense may be awarded in respect of a valuable benefit conferred by either party upon the other party in pursuance of the contract. In *B.P.*

[158] [1995] 1 W.L.R. 1226.
[159] This was favoured by the Law Revision Committee (Cmd. 6009, 1939), p. 7.
[160] As suggested in *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* [1979] 1 W.L.R. 783 at p. 800. Note that this decision was substantially approved by the House of Lords: [1983] 2 A.C. 352.
[161] Williams, *Law Reform (Frustrated Contracts) Act 1943*, pp. 35–6.
[162] Treitel, *Frustration and Force Majeure* (1994), §§15-059–15-060.
[163] [1995] 1 W.L.R. 1226, at p. 1237.
[164] *Sed quaere*, see *Lipkin Gorman* v. *Karpnale Ltd.* [1991] 2 A.C. 548; Carter and Tolhurst (1996) 10 J.C.L. 265.

Exploration Co. (Libya) Ltd. v. *Hunt (No. 2)*[165] Robert Goff J. pointed out that the sub-section must be applied in two distinct stages. The first is the identification and valuation of the benefit. The second stage is for the Court to assess what sum (not exceeding the value of the benefit) it considers just to award to the party by whom the benefit has been conferred.

Benefit and its value

There are three situations to be considered. The first is where the performance rendered results in the delivery of an item which is unaffected by the frustrating event. If, for example, in the illustration set out above, A has delivered to B some of the machinery, the machinery so delivered could constitute a benefit to B. The value of that benefit will ordinarily be its value to B at the date of frustration. This may be more or less than the expenses incurred by A in manufacturing and delivering that machinery. It was stated by Robert Goff J. that as a matter of construction 'benefit' in the sub-section normally meant the end product of services rather than the services themselves.[166]

The second is where, although the performance results in the delivery of an item or an end-product, in our example the machinery, the event which frustrates the contract (as in *Appleby* v. *Myers*),[167] destroys it or renders it useless and of no value to B without delivery of the remainder. Under paragraph (b) of the sub-section regard is to be had to 'the effect, in relation to the . . . benefit, of the circumstances giving rise to the frustration of the contract'. The interpretation of this provision is problematical. Robert Goff J. stated[168] that 'benefit' in section 1(3)(b) clearly refers to the end-product of the services, rather than the services themselves, and that the sub-section 'makes it plain that the plaintiff [the party conferring the benefit] is to take the risk of depreciation or destruction by the frustrating event'. If this view is correct,[169] then the value of the benefit in such a case will be nil, and no award could be made in favour of A under the sub-section.

The third situation is where the performance rendered is a 'pure' service, without any end-product, such as gardening, surveying, or transporting goods.[170] Here, Robert Goff J. stated that the 'benefit' in the sub-section was the services themselves,[171] and it is these that must be valued. In such cases care must be taken not to cross the line between restitution in respect of a benefit conferred, which is permitted by the sub-section, and recompense for action taken by one party in

[165] [1979] 1 W.L.R. 783 (affirmed by the Court of Appeal [1981] 1 W.L.R. 232, and by the House of Lords [1983] 2 A.C. 352), for the facts see *infra*.

[166] *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* (*supra*, n. 165) at pp. 801–2.

[167] (1867) L.R. 2 C.P. 651; *ante*, p. 527. See also *Parsons Bros. Ltd.* v. *Shea* (1965) 53 D.L.R. (2d) 86 (Canada).

[168] *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* [1979] 1 W.L.R. 783, at p. 803. Contrast Glanville Williams, *Law Reform (Frustrated Contracts) Act 1943*, pp. 48–51.

[169] Cf. Treitel, *Frustration and Force Majeure* (1994), § 15–054 (s. 1(3) applies where a valuable benefit has been obtained 'before the time of discharge' and sub-paragraphs (a) and (b) are relevant to the assessment of the just sum, not the identification of the benefit); Birks, *An Introduction to the Law of Restitution* (1985), p. 253.

[170] See e.g. *Angus* v. *Skully* 44 NE 674 (1900) (USA) and the facts of *Cutter* v. *Powell* (1795) 6 T.R. 320, *ante*, pp. 484–5.

[171] *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* (*supra*, n. 168) at p. 803.

reliance on the contract: 'if in fact the performance of services has conferred no benefit on the person requesting them, it is pure fiction to base restitution on a benefit conferred'.[172]

The 'just sum'

The second stage is for the Court to assess what sum (not exceeding the value of the benefit) it considers just to award to the party by whom the benefit has been conferred. This has been termed the 'just sum'. The purpose of the award has been said to be to prevent the unjust enrichment of the other party at his expense.[173] In the example given above, if the machinery delivered remained of value to B after the frustrating event, the just sum would probably be assessed as the reasonable value of that machinery,[174] or a rateable part of the contract price.

The principles applied

In *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)*:[175]

The plaintiff entered into a contract to explore and develop an oil concession in Libya owned by Hunt. The plaintiff was to make initial payments and a transfer of oil to Hunt, and in return was to get a 50 per cent share in the concession and 'reimbursement oil' calculated by a formula. A significant oil field was discovered and oil was produced and transferred under the contract for 4 and a half years, but the contract was then frustrated when both parties' interests were expropriated by the Libyan Government, which paid some compensation to Hunt. The plaintiff claimed under section 1(3) of the 1943 Act.

It was held that, under section 1(3), the 'valuable benefit' had to be not the work exploring and extracting oil but the end-product of that work, the enhancement of the value of Hunt's concession. But the effect of the frustrating event was to make this valueless and unrealizable by Hunt, and sub-paragraph (b) required this to be reflected in the valuation of the benefit. But Hunt had received considerable amounts of oil produced prior to the expropriation, and compensation thereafter, and half the value of this ($85 million) was held to be the benefit obtained from the plaintiff's exploration and development, and the upper limit of any award.[176] The 'just sum' was determined by taking account of the cost to the plaintiff of the work done for Hunt and the oil it initially transferred to Hunt reduced by the amount of the 'reimbursement oil' it had received. This amounted to just under $35 million. Since this was in effect the value of 'reimbursement oil' due to the plaintiff but not transferred at the date of frustration, the remedy given approximately corresponded to a scaled-down contract price, that percentage of the contract price which the part-performer had 'earned' by performance before the frustrating event.

Neither under sub-section (2) nor under sub-section (3) can any allowance be made for the time-value of money, that is to say, for the fact that money may have been paid, or expenses incurred, long before the date of frustration.[177]

[172] *Coleman Engineering* v. *North American Airlines* 420 P. 2d 713, *per* Traynor C.J. at p. 729 (1966) (California).

[173] *Ibid.*, at p. 805.

[174] *Ibid.*, at pp. 805–6.

[175] [1979] 1 W.L.R. 783 (affirmed by the Court of Appeal [1981] 1 W.L.R. 232, and by the House of Lords [1983] 2 A.C. 352).

[176] The other half was attributed to Hunt's ownership of the concession prior to the exploration and development under the contract.

[177] *B.P. Exploration Co. (Libya) Ltd* v. *Hunt (No. 2)* [1979] 1 W.L.R. 783, at 800.

The Act does not apply if there is a provision to the contrary in the contract;[178] and certain types of contract are expressly exempted from its operation.[179] The first is a contract for the carriage of goods by sea or a charterparty (other than a time charterparty or a charterparty by way of demise). This recognizes a well-established custom, which has become part of the business practice of shipowners and insurers, that freight paid or payable in advance under such contracts is not recoverable even though the completion of the voyage is frustrated.[180]

Exception: (i) Carriage of goods by sea & voyage charters

The second is a contract of insurance.

(ii) Contracts of insurance

The third concerns the sale of goods:

(iii) Sale of goods

> Any contract to which section seven 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 . . . 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.

It will be remembered that the general rule in the case of the sale of goods is that they are at the risk of the person whose property they are: *res perit domino*.[181] Where there is a sale of *specific* goods property in the goods normally passes to the buyer at the time the contract is made,[182] and so it follows that they are also at the buyer's risk. To this type of contract the Act has no application.

> Suppose that A buys from a shopkeeper, B, a particular wardrobe, arranging for it to be delivered next day. During the night the shop catches fire and the wardrobe is destroyed. The risk has passed to A, who must pay the purchase price.

But the sub-section quoted above also exempts cases where there is an agreement to sell specific goods and the risk has not yet passed to the buyer. If the goods then perish without the fault of either party, the contract is *avoided* by section 7 of the Sale of Goods Act 1979 and the 1943 Act does not apply.

Specific and unascertained goods

Specific goods are defined by section 61(1) of the Sale of Goods Act 1979 as 'goods identified and agreed on at the time a contract of sale is made'. Goods which are unascertained at this time do not therefore come within this exception, although it must be noted that the doctrine of frustration rarely then applies. If A agrees to sell to B 'six hundred tons of coal', there can normally be no frustration of this contract. Even though A may have had in mind a particular source, this assumption is not common to both parties. The contract can be fulfilled at any time and A must obtain sufficient coal from another source or be liable for breach.[183] On the other hand, if the goods, though unascertained, are to come from a source which is specifically defined, for example, 'six hundred tons of coal from the ship *Rose Marie* now in dock', and subsequently the ship and cargo are destroyed by fire, this contract is clearly capable of frustration, but there is some

[178] 1943 Act, s. 2(3). Cf. *B.P. Exploration (Libya) Ltd.* v. *Hunt* [1983] 2 A.C. 352, at 372, 373.
[179] 1943 Act, s. 2(5).
[180] *Compania Naviera General S.A.* v. *Kerametal Ltd.* [1983] 1 Lloyd's Rep. 372.
[181] Sale of Goods Act 1979, s. 20.
[182] *Ibid.*, s. 18, Rule 1.
[183] *Blackburn Bobbin Co. Ltd.* v. *Allen (T. W.) & Sons Ltd.* [1918] 2 K.B. 467; *ante*, p. 520. Cf. *Re Badische Co. Ltd.* [1921] 2 Ch. 331; see *ante*, p. 518.

doubt as to whether or not it falls outside the 1943 Act. In one case,[184] goods of this nature were held not to be specific goods for the purposes of section 52 of the Sale of Goods Act 1979 (specific performance), and it is submitted that, for the purposes of frustration, the goods are likewise not specific goods and so are subject to the provisions of the 1943 Act.[185]

Partial failure

A similar problem may arise in the type of situation exemplified by *Howell* v. *Coupland*:[186]

> The defendant agreed to sell to the plaintiff 200 tons of potatoes to be grown on a particular field. The crop failed, so that the defendant was able to deliver only 80 tons. In answer to the plaintiff's claim for non-delivery of the other 120 tons, the defendant pleaded that he had duly delivered all that it was possible for him to deliver and that he was excused from delivering the remainder.

It was held that the defendant was not liable. Mellish L.J. said:[187]

> This is not like the case of a contract to deliver so many goods of a particular kind, where no specific goods are to be sold. Here there was an agreement to sell and buy 200 tons of a crop to be grown on specific land, so that it is an agreement to sell what will be and may be called specific things; therefore neither party is liable if the performance becomes impossible.

Despite the use by Mellish L.J. of the word 'specific' in this case, it is clear that the potatoes were not 'specific goods' within the meaning of the Sale of Goods Act. Nevertheless this is not a situation to which the provisions of the 1943 Act would appear to apply. It has been held[188] that a contract of sale of this nature is subject to a condition. Depending on the intention of the parties, the condition which will be implied may be one that neither party shall be liable if any part of the promised goods fails to materialize;[189] alternatively, it may, as in *Howell* v. *Coupland*, be a condition that the buyer can require such performance as remains possible, but the seller is excused from delivering the remainder of the goods.[190]

Arbitration

There are very few reported decisions on the interpretation of the 1943 Act: most disputes simply concern the amount of each party's liability, and are referred to arbitration.[191]

[184] *Re Wait* [1927] 1 Ch. 606.
[185] See also Hudson (1968) 31 M.L.R. 535.
[186] (1876) 1 Q.B.D. 258.
[187] At p. 262.
[188] *H.R. & S. Sainsbury Ltd.* v. *Street* [1972] 1 W.L.R. 834. See also *Re Wait* [1927] 1 Ch. 606, at p. 631.
[189] See the Sale of Goods Act 1979, s. 5(2) (condition precedent). The sale might also be subject to a condition subsequent: *ante*, pp. 134, 501–2.
[190] *H.R. & S. Sainsbury Ltd.* v. *Street* (*supra*, n. 188).
[191] *Pioneer Shipping Ltd.* v. *B.T.P. Tioxide Ltd.* [1982] A.C. 724.

15

Discharge by Breach

Breach of contract

If one of two parties to a contract breaks an obligation which the contract imposes, a new obligation will in every case arise—an obligation to pay damages to the other party in respect of any loss or damage sustained by the breach. Besides this, there are circumstances under which the breach not only gives rise to a right of action for damages but also gives the innocent party the right to decide not to render further performance under the contract and to be discharged from its obligations.[1] However, not every breach of contract operates as a discharge. In order to have this effect the breach must be such as to constitute a repudiation by the party in default of its obligations under the contract.

I. Discharge at Option of the Injured Party

Does not itself discharge but confers option o innocent party

It is common to speak of the contract as having been 'discharged by the breach'. The phrase, though convenient, is not strictly accurate. A breach does not, of itself, effect a discharge;[2] what it may do is to justify the innocent party, if that party so chooses, in regarding itself as absolved or discharged from further performance of the contract. It does not automatically terminate the innocent party's obligation since that party has the option either to treat the contract as still continuing or to regard itself as discharged by reason of the repudiation of the contract by the other party. An acceptance of a repudiation must be clear and unequivocal.[3] Once the option is exercised to either keep the contract on foot or terminate it, the decision is not revocable.[4] A fresh option may arise, however, if the repudiation continues or there is another separate repudiatory breach.

Contract remair 'in full effect'

In principle an innocent party who does not 'accept' the repudiation is entitled to continue to insist on performance because the contract remains in full effect.

[1] See Treitel (1967) 30 M.L.R. 139.

[2] See *post*, pp. 540, 547.

[3] *Vitol S.A.* v. *Norelf Ltd.* [1996] A.C. 800, *per* Lord Steyn at 810–11. See also *Heyman* v. *Darwins Ltd.* [1942] A.C. 356, at p. 361; *Northwest Holt Group Administration Ltd.* v. *Harrison* [1985] I.C.R. 668; *Bliss* v. *South East Thames Regional Health Authority* [1987] I.C.R. 700, at pp. 716–17; *State Trading Corporation of India Ltd.* v. *M. Golodetz Ltd.* [1989] 2 Lloyd's Rep. 277 at p. 286.

[4] *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corporation of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep. 391 *per* Lord Goff at p. 398; *Peyman* v. *Lanyani* [1985] Ch. 457.

Thus, in *White and Carter (Councils) Ltd.* v. *McGregor*:[5]

The appellant, an advertising contractor, agreed with the respondent, a garage proprietor, to display advertisements for his garage for 3 years. On the same day, the respondent refused to perform the agreement and requested the appellant to cancel the contract. The appellant refused to do so, and elected to treat the contract as still continuing. It made no effort to relet the space, displayed advertisements as agreed, and sued for the full amount due.

It was contended on behalf of the respondent that, since he had renounced the agreement before anything had been done under it, the appellant was not entitled to carry out the agreement and sue for the price: its remedy, if any, lay in damages. A bare majority of the House of Lords rejected this contention and held that the appellant was entitled to the full contract sum.

The decision has been criticized as encouraging wasteful and unwanted performance. The criticisms are considered in Chapter 18, Specific Remedies.[6] It is in any event clear from the speeches of the majority in this case that the party not in breach will not always thus be entitled to complete the contract and sue for the contract price. In the first place, if the contract cannot be carried out without the co-operation of the party who has refused to perform, and such co-operation is withheld, the innocent party's only remedy is to sue for damages and not for the price.[7] So an employee who is wrongfully dismissed employment can only claim damages. The employee cannot claim the salary payable after dismissal on the ground that he is ready, able, and willing to serve the employer if only the employer would allow him to do so.[8] Secondly, the rule in *White and Carter (Councils) Ltd.* v. *McGregor* does not apply 'if it can be shown that a person has no legitimate interest, financial or otherwise, in performing the contract rather than claiming damages',[9] in which case a plaintiff may be compelled to resort to the remedy of damages, provided the damages are an adequate remedy for any loss suffered.

Limited effect of unaccepted repudiation

The need for acceptance of a repudiation for the contract to be discharged led to Asquith L.J.'s famous and influential aphorism that 'an unaccepted repudiation is a thing writ in water'.[10] But an unaccepted repudiation is not altogether without effect. An innocent party who remains ready and willing to perform[11] can rely on the unaccepted repudiation as a defence in an action brought by the guilty party.[12]

[5] [1962] A.C. 413, on the facts of which, see Rodger (1977) 93 L.Q.R. 168.

[6] See *post*, p. 595.

[7] At pp. 430, 432, 439.

[8] *Vine* v. *National Dock Labour Board* [1956] 1 Q.B. 658, at p. 674; *Denmark Productions Ltd.* v. *Boscobel Productions Ltd* [1969] 1 Q.B. 699; *Hill* v. *C. A. Parsons & Co. Ltd.* [1972] Ch. 305, at p. 314; *Gunton* v. *Richmond L.B.C.* [1980] I.C.R. 755. Cf. *Boyo* v. *Lambeth London Borough Council* [1994] I.C.R. 727 at pp. 742–4, 747.

[9] *White and Carter (Councils) Ltd.* v. *McGregor* [1962] A.C. 413, *per* Lord Reid at p. 431; *Attica Sea Carriers Corp.* v. *Ferrostaal Poseidon Bulk Reederei GmbH (The Puerto Buitrago)* [1976] 1 Lloyd's Rep. 250; *Gator Shipping Cpn.* v. *Trans-Asiatic Oil Ltd. S.A.* [1978] 2 Lloyd's Rep. 357, at pp. 372–4; *Stocznia Gdanska S.A.* v. *Latvian S.S. Co.* [1996] 2 Lloyd's Rep. 132; [1998] 1 W.L.R. 574.

[10] *Howard* v. *Pickford Tool Co. Ltd.* [1951] 1 K.B. 417, at p. 421. See also *Fercometal S.A.R.L.* v. *Mediterranean Shipping Co. S.A.* [1989] A.C. 788 at p. 800; *State Trading Corporation of India Ltd.* v. *M. Golodetz Ltd.* [1989] 2 Lloyd's Rep. 277 at p. 285.

[11] *Fercometal S.A.R.L.* v. *Mediterranean Shipping Co. S.A. (The Simona)* [1989] A.C. 788.

[12] *Peter Turnbull & Co. Pty. Ltd.* v. *Mundus Trading Co. (Australasia) Pty. Ltd.* (1954 90 C.L.R. 235, at pp. 245, 251; *Foran* v. *Wight* (1989) 168 C.L.R. 385 at p. 438 (Australia). See further Carter, *Breach of Contract*, 2nd edn. (1991) p. 242 ff.

Again, while the suggestion that contracts of employment are an exception to the normal rule and are discharged by a unilateral repudiation without the need for acceptance has been rejected,[13] it has been held that an employee's right to damages following an unlawful dismissal does not continue beyond the time at which the employer could have lawfully brought the contract to an end.[14]

Failure of performance

In cases of a failure of performance by one party which goes to the root of the contract,[15] the contract is likewise not determined by the breach,[16] and it is open to the innocent party to treat the contract as continuing or to accept the defective performance when tendered. An innocent party who adopts this course, is sometimes said to have elected to *affirm* the contract, i.e. to have waived the right to be treated as discharged, although the right to claim damages for the breach is still retained.[17] Affirmation may be express or implied. Affirmation will be implied if, to the knowledge of the party in default, the innocent party does some unequivocal[18] act which shows an intention to go on with the contract regardless of the breach or from which it may be inferred that the right to be treated as discharged will not be exercised.[19] And affirmation must be total. A contracting party cannot affirm part of the contract and disaffirm the rest, for that would be to make a new contract.[20]

Is knowledge required?

Affirmation is a voluntary act, and requires knowledge. Although old authorities to the contrary can be found, the traditional position was that a party need only have knowledge of the facts which give rise to the right to affirm or terminate.[21] Recent cases go further and suggest that a party cannot be called upon to make an election or be held to have made an election, unless, in addition to knowledge of the relevant facts, that party has knowledge of the right to elect.[22] Despite this debate, as we have seen,[23] there are circumstances where the innocent party will be deprived of the right to be treated as discharged even though that party has no knowledge of the breach. There may also be cases where an innocent party who has led the party in default to believe that it will not exercise that right will be estopped from exercising it.[24]

[13] *Gunton* v. *Richmond L.B.C.* [1980] I.C.R. 755.

[14] *Boyo* v. *Lambeth London Borough Council* [1994] I.C.R. 727.

[15] See *post*, p. 548.

[16] *Photo Productions Ltd.* v. *Securicor Transport Ltd.* [1980] A.C. 827 (overruling *Harbutt's 'Plasticine' Ltd.* v. *Wayne Tank and Pump Co. Ltd.* [1970] 1 Q.B. 447).

[17] See *ante*, p. 141.

[18] *China National Foreign Trade Transportation Cpn.* v. *Evlogia Shipping Co. S.A. of Panama* [1979] 1 W.L.R. 1018; *Yukong Line Ltd. of Korea* v. *Rendsburg Investments Corp. of Liberia* [1996] 2 Lloyd's Rep. 604 (very clear evidence required).

[19] *Pust* v. *Dowie* (1863) 5 B. & S. 33; *Bentsen* v. *Taylor, Sons & Co.* [1893] 2 Q.B. 274; *Hain SS. Co. Ltd.* v. *Tate & Lyle Ltd.* (1936) 41 Com. Cas. 350, at pp. 355, 363; *Suisse Atlantique Société d'Armement Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale* [1967] 1 A.C. 361.

[20] *Suisse Atlantique Société d'Armement Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale* (*supra*, n. 19), at p. 398.

[21] *Matthews* v. *Smallwood* [1910] 1 Ch. 777 at p. 786; *Kammins Ballrooms Co. Ltd.* v. *Zenith Investments (Torquay) Ltd.* [1971] A.C. 850, at pp. 877–8, 883.

[22] *Peyman* v. *Lanjani* [1985] Ch. 457; *Sea Calm Shipping Co. S.A.* v. *Chantiers Navals de L'Esterel* [1986] 2 Lloyd's Rep. 294. See also *Kendall* v. *Hamilton* (1879) 4 App Cas. 504 at p. 542. Cf. *Motor Oil Hellas (Corinth) Refineries S.A.* v. *Shipping Corpn. of India (The Kanchenjunga)* [1990] 1 Lloyd's Rep. 391 at p. 398.

[23] See *ante*, p. 500.

[24] The incidence of estoppel in this situation depends upon interpretation of the difficult case of *Panchaud Frères S.A.* v. *Etablissements General Grain Co.* [1970] 1 Lloyd's Rep. 53 (esp. at pp. 57–8) and cases consequent thereon.

Effect of election to accept repudiation

If the innocent party decides to accept the repudiation, this discharges all the future contractual obligations of that party which have not already been performed. At the same time, the primary obligations of the party in default to perform any of that party's contractual promises which remain unperformed are likewise discharged.[25] However, in the case of the party in default, in place of the primary obligations imposed by the contract there arises a secondary obligation to pay damages for the breach. This point was clearly made in *Moschi* v. *Lep Air Services Ltd.*:[26]

R Ltd., was indebted to L Ltd., the respondent, in the sum of £40,000, which it agreed to pay to L Ltd at the rate of not less than £6,000 *per* week. M, the appellant, guaranteed to L Ltd. the performance by R Ltd. of its obligation to make these payments. R Ltd. defaulted from the outset and, after 3 weeks, paid only some £10,000 of the £18,000 then due. L Ltd. elected to treat this default as a repudiation of the contract which it accepted. R Ltd went into liquidation and L Ltd. sued M in respect of both the accrued and future instalments unpaid.

M argued that, since the repudiation had been accepted, the obligation of the company to pay the outstanding instalments due after that time came to an end, and in consequence his obligation as guarantor also came to an end. The House of Lords found little difficulty in disposing of this argument and held that he was liable on the guarantee. In the first place, upon acceptance of the repudiation, although the company's primary obligation to pay the future instalments came to an end, it was replaced, by operation of law, by a secondary obligation to pay damages for the breach. This secondary obligation was just as much an obligation arising from the contract as were the primary obligations it replaced. Secondly, M had undertaken that R Ltd. would perform its contract and so was in breach of his contract of guarantee. The damages which R Ltd. had not paid constituted the loss flowing from M's breach of contract for which M was liable.

No reason or bad reason given

Where one party refuses to go on with the contract, giving no reason for this refusal or the wrong or an inadequate reason, the action can still be justified if (even if this is unknown to that party) the other party had at the time committed a breach of contract which would have provided a good reason.[27] So, for example, if an employer dismisses an employee without giving any reason at all, the employer can justify the dismissal should it subsequently be discovered that, prior to the dismissal, the employee had been guilty of dishonesty which would have entitled the dismissal of the employee.[28] Similarly if a buyer of goods rejects the goods on the

[25] It may, however, be the intention of the parties that certain primary obligations, for example, an arbitration or jurisdiction clause, should continue notwithstanding that their other primary obligations have come to an end: see *Heyman* v. *Darwins Ltd.* [1942] A.C. 356; *Moschi* v. *Lep Air Services Ltd.* [1973] A.C. 331, at p. 350. See also *ante*, p. 173 (exemption clauses).

[26] [1973] A.C. 331. See also *Photo Production Ltd.* v. *Securicor Transport Ltd.* [1980] A.C. 827, at p. 849.

[27] *Taylor* v. *Oakes Roncoroni & Co.* (1922) 127 L.T. 267, at p. 269; *British & Beningtons Ltd.* v. *N.W. Cachar Tea Co.* [1923] A.C. 48, at p. 71; *The Mihalis Angelos* [1971] 1 Q.B. 164, at pp. 195, 200, 204; *Scandinavian Trading Co. A/B* v. *Zodiac Petroleum S.A.* [1981] 1 Lloyd's Rep. 81; *Sheffield* v. *Conrad* (1987) 22 Con. L.R. 108.

[28] *Ridgway* v. *Hungerford Market Co.* (1835) 3 A. & E. 171, at pp. 177, 178, 180; *Boston Deep Sea Fishing & Ice Co.* v. *Ansell* (1888) 39 Ch. D. 339, at pp. 352, 364; *Cyril Leonard & Co.* v. *Simo*

erroneous ground that they are defective in quality, that rejection will still be lawful should the goods turn out not to have been in conformity with the contract description—a breach of contract which would have justified rejection. This rule, though well established, could be criticized on the ground that it allows a party to a contract to 'blow hot and cold', first alleging one reason then in fact relying on another. There is some authority[29] for the view that a party will be estopped from relying on a ground which was not specified at the time of the refusal to perform if that party has thereby led the other party to believe that no reliance would be placed on that ground and it would be unfair or unjust now to allow such reliance.

II. Forms of Discharge by Breach

THE right of a party to be treated as discharged from further performance may arise in any one of three ways: the other party to the contract (a) may renounce its liabilities under it, (b) may by its own act make it impossible to fulfil them, (c) may fail to perform what it has promised.[30] In each of these three cases the contracting party has repudiated its contractual obligations. In the first case, the repudiation is by the refusal to perform; in the second, it is by the inability to perform; in the third, it is by a total or substantial failure to perform, and not the less so because that failure may not have been wilful or deliberate.

Of these forms of breach the first two may take place not only in the course of performance but also while the contract is still wholly executory, i.e. before either party is entitled to demand a performance by the other of the other's promise. In such a case the breach is usually termed an 'anticipatory breach'.[31] The last can only take place at or during the time for performance of the contract.

(a) Renunciation

Renunciation

Renunciation occurs where one of the parties evinces an intention not to go on with the contract. If there is an express and unqualified refusal to perform, this intention will, of course, be clear and obvious. But it can also be evinced by conduct, and 'the test of whether an intention is evinced by conduct is whether the party renunciating has acted in such a way as to lead a reasonable person to the conclusion that he does not intend to fulfil his part of the contract'.[32] Acts or

Securities Trust [1972] 1 W.L.R. 80, at pp. 85, 87, 89. But the rule does not apply to cases of unfair dismissal under statute: *W. Devis & Co.* v. *Atkins* [1977] A.C. 931.

[29] *Panchaud Frères S.A.* v. *Etablissements General Grain Co.* [1970] 1 Lloyd's Rep. 53, at pp. 57–8. See also *Heisler* v. *Anglo-Dal Ltd.* [1954] 1 W.L.R. 1273, at p. 1278.

[30] This statement of the law was approved by Lord Porter in *Heyman* v. *Darwins Ltd.* [1942] A.C. 356, at p. 397 and by Devlin J. in *Universal Cargo Carriers Corporation* v. *Citati* [1957] 2 Q.B. 401, at p. 436 (affirmed in part [1957] 1 W.L.R. 979 and reversed in part [1958] 2 Q.B. 254).

[31] See *post*, pp. 541, 543; Dawson [1981] C.L.J. 83.

[32] *Universal Cargo Carriers Corporation* v. *Citati* (*supra*, n. 30), *per* Devlin J. at p. 436. See also *Forslind* v. *Becheley Crundall*, 1922 S.C. (H.L.) 173; *The Hermosa* [1982] 1 Lloyd's Rep. 570; *Nottingham Building Society* v. *Eurodynamics plc.* [1995] F.S.R. 605 at pp. 611–12.

omissions from which renunciation can be inferred may also entitle the injured party to be treated as discharged on one or both of the two other grounds previously mentioned.[33] But if the injured party relies upon renunciation as a ground for discharge, they must be such as to lead to the conclusion that the other party no longer intends to be bound by the contract.

Intention required

The importance of this intention was emphasized in the case of *Freeth* v. *Burr*,[34] where there was a failure on the part of the buyer to pay for one instalment of several deliveries of iron, under an erroneous impression that he was entitled to withhold payment as a set-off against damages for non-delivery of an earlier instalment. The seller was not discharged. Keating J. said:[35] 'It is not a mere refusal or omission of one of the contracting parties to do something which he ought to do, that will justify the other in repudiating the contract; but there must be an absolute refusal to perform his part of the contract'. Note here that the word 'repudiating' is being used in the sense of an election to terminate the contract.

Also in *Mersey Steel and Iron Co.* v. *Naylor, Benzon & Co.*:[36]

NB bought from MS 5,000 tons of steel, to be delivered at the rate of 1,000 tons each month commencing in January 1881, payment to be made within 3 days of the receipt of the shipping documents. MS delivered part only of the first instalment in January, but delivered another in February. Shortly before payment for these was due, a petition was presented for the winding up of MS, whereupon NB refused to pay as it had been erroneously advised not to do so unless MS obtained the leave of the Court. MS informed NB that it would treat this refusal as breach, but NB continued to express its willingness to take delivery and to make the payments if possible.

The House of Lords held that MS was not entitled to treat itself as discharged. The Earl of Selborne L.C. said:[37]

I cannot ascribe to their [NB's] conduct, under these circumstances, the character of a renunciation of the contract, a repudiation of the contract, a refusal to fulfil the contract. It is just the reverse; the purchasers were desirous of fulfilling the contract; they were advised that there was a difficulty in the way, and they expressed anxiety that that difficulty should be as soon as possible removed.

In neither of these two cases did the breach, in the particular circumstances in which it had been committed, indicate, in the view taken by the Court, an intention in the party in default to throw up the contract altogether, so as to set the

[33] *Mersey Steel and Iron Co.* v. *Naylor, Benzon & Co.* (1884) 9 App. Cas. 434, at p. 441 (renunciation) and p. 444 (failure of performance).

[34] (1874) L.R. 9 C.P. 208 applied in *Aktion Maritime Corpn. of Liberia* v. *S. Kasmas & Brothers Ltd.* [1987] 1 Lloyd's Rep. 283 at p. 306. See also *Mitsibushi Heavy Industries Ltd.* v. *Gulf Bank K.S.C.* [1997] 1 Lloyd's Rep. 343.

[35] At p. 214.

[36] (1884) 9 App. Cas. 434. See also *Sweet & Maxwell Ltd.* v. *Universal News Services Ltd* [1964] 2 Q.B. 699; *Woodar Investment Development Ltd.* v. *Wimpey Construction U.K. Ltd.* [1980] 1 W.L.R. 277 (reliance on *bona fide*, but mistaken, construction); *Alfred C. Toepfer International GmbH* v. *Itex Itagram Export S.A.* [1993] 1 Lloyd's Rep. 360 at p. 361; *Mitsubishi Heavy Industries Ltd.* v. *Gulf Bank K.S.C.* [1997] 1 Lloyd's Rep. 342, at pp. 350, 354.

[37] At p. 441.

other party free. Moreover, a court may be reluctant to find that there has been a renunciation where a party insists on performing the contract in a particular way which, although ultimately held to be a breach of contract, arose from a *bona fide* belief as to the construction of the contract which is also consistent with its continuance.[38] On the other hand, an unequivocal refusal, by words or conduct, to perform the contract will entitle the other party to be discharged from any further performance of its obligations. So, for example, if a buyer contracts to buy goods by instalments and agrees to pay cash for them, but then demands credit in respect of all future deliveries of the goods, the seller may refuse to make any further deliveries.[39] Similarly if, in breach of a contract of employment, a gardener insolently refuses to carry out instructions,[40] or a school teacher refuses to supervise school meals when required to do so,[41] the employer is justified in dismissing that person, i.e. terminating the contract of employment.

Renunciation may take place either before performance is due or during performance itself.

(i) Before performance is due

Anticipatory breach

The parties to a contract which is wholly executory have a right to something more than the performance when the time arrives. They have a right to the maintenance of the contractual relation right up to that time, as well as to a performance of the contract when due.

may be accepted

The renunciation of a contract by one of the parties before the time for performance has come does not, of itself, put an end to the contract, but the 'anticipatory breach' entitles the other to choose to be discharged to sue at once for damages. A contract is a contract from the time it is made, and not from the time that performance is due. A leading case upon this subject is *Hochster* v. *De la Tour*:[42]

The defendant engaged the plaintiff on 12 April to enter into his service as a courier and to accompany him upon a tour; the employment was to commence on 1 June. On 11 May the defendant wrote to the plaintiff to inform him that his services would no longer be required. The plaintiff at once brought an action, although the time for performance had not yet arrived.

The Court held that he was entitled to do so.

The rule has also been applied to situations where the performance is not absolute as in *Hochster* v. *De la Tour*, but contingent. In that case a time was fixed for performance, and before it arrived the defendant renounced the contract, but in *Frost* v. *Knight*,[43] performance was contingent upon an event which might not happen within the lifetime of the parties:

The defendant, a bachelor, promised to marry the plaintiff upon his father's death; but during his father's lifetime he renounced the contract.

[38] *Vaswani* v. *Italian Motors (Sales and Services) Ltd.* [1996] 1 W.L.R. 270 (Privy Council).
[39] *Withers* v. *Reynolds* (1831) 2 B. & Ad. 882.
[40] *Pepper* v. *Webb* [1969] 1 W.L.R. 514.
[41] *Gorse* v. *Durham C.C.* [1971] 1 W.L.R. 775.
[42] (1853) 2 E. & B. 678.
[43] (1872) L.R. 7 Ex. 111.

The plaintiff was held entitled to sue on the ground explained above. The principle of anticipatory breach was justified by Cockburn C.J. as follows:[44]

> The promisee has an inchoate right to the performance of the bargain, which becomes complete when the time for performance has arrived. *In the meantime he has a right to have the contract kept open as a subsisting and effective contract.* Its unimpaired and unimpeached efficacy may be essential to his interests.

It can also be said that the principle is convenient as it enables the innocent party to assert its rights speedily and so to minimize the damage which may be suffered from the breach. Nevertheless, it is important to note that a party who has been guilty of an anticipatory breach by renunciation is accorded no privilege of withdrawing that renunciation once it has been accepted by the other party,[45] even though the guilty party tenders performance within the time originally fixed by the contract and even though the position of the other party has in no way changed as a result of the renunciation.

or refused at risk of promisee

The promisee, however, has the right to continue to insist on the performance of the promise and to refuse to accept the renunciation. If this is done, the promisee loses the right to rely on the anticipatory breach and the contract remains in existence for the benefit and at the risk of both parties. Should anything occur subsequently to discharge the contract from other causes, the promisor, whose renunciation has been refused, may take advantage of such discharge. Thus in *Avery* v. *Bowden*:[46]

> A chartered his ship to B. It was agreed that the ship would sail to Odessa, and there take a cargo from B's agent, which was to be loaded within a certain number of days. The vessel reached Odessa, and her master demanded a cargo, but B's agent was unable to supply one. Nevertheless, the master of the ship continued to demand a cargo, but before the specified number of days had elapsed the Crimean war broke out between England and Russia and the performance of the contract became legally impossible. A afterwards sued for breach of the charterparty.

His action failed. If B's agent had positively informed the master that no cargo would be provided, and that there was no use in his remaining there any longer, the master might have treated this as an anticipatory breach and sailed away. A would then have had the right to sue at once upon the contract. But the Court found that as the conduct of B's agent was not such as to constitute a renunciation of the contract there was therefore no breach committed by B before the contract was frustrated. Even, however, if there had been a renunciation of the contract, the Court considered that it could not be treated as a cause of action after the master still continued to insist upon having a cargo in fulfilment of the charterparty. Again, it has been held by the House of Lords[47] that where, following an

[44] At p. 114. But see Vold (1928) 41 Harv. L.R. 340.

[45] *Xenos* v. *Danube, etc., Ry.* (1863) 13 C.B.N.S. 824; but see *Aegnoussiotis Shipping Cpn. of Monrovia* v. *A/S Kristian Jebsens Rederi of Bergen* [1977] 1 Lloyd's Rep. 268, at p. 276 (new contract).

[46] (1855) 5 E. & B. 714; (1856) 6 E. & B. 953. See also *Michael* v. *Hart & Co.* [1902] 1 K.B. 482; *Berners* v. *Fleming* [1925] Ch. 264.

[47] *Fercometal S.A.R.L.* v. *Mediterranean Shipping Co. S.A. (The Simona)* [1989] A.C. 788.

anticipatory breach by charterers which was not accepted by the shipowners, the owners later failed to tender the vessel ready to load on time, the charterers were entitled to cancel the charterparty.

Criticism of term 'anticipatory breach'

Despite the utility of the principle of 'anticipatory breach', the term itself is somewhat misleading. It suggests that the cause of action lies in the future breach that will occur on the date fixed for performance, which the innocent party is, in some sense, permitted to anticipate. But it is clear from the cases cited that, at any rate where the anticipatory breach consists of a renunciation of the contract, the breach is constituted by the renunciation itself, and, if this is accepted, the innocent party is immediately entitled to recover by way of damages the true value of the contractual rights which have been lost, subject to the innocent party's duty to mitigate.[48]

(ii) During performance

Renunciation during performance

If during the performance of a contract one of the parties by words or conduct unconditionally refuses to perform its side of the contract, the other party is forthwith released from any further performance of its obligations, and is entitled at once to sue.

In *Cort* v. *Ambergate etc. Railway Company*:[49]

C contracted with the defendant to supply it with 3,900 tons of railway chairs, at a certain price, to be delivered in certain quantities at specified dates. After 1,787 tons had been delivered, the defendant requested C to deliver no more, as they would not be wanted. C brought an action upon the contract, averring that he was always ready and willing to perform his part, but had been prevented from doing so by the action of the defendant.

C obtained a verdict, and when the defendant moved for a new trial on the ground that he should have proved not merely that he was ready and willing to deliver, but an actual delivery, the Court rejected this submission. Since the contract had been renounced, C could maintain an action without manufacturing and tendering the rest of the goods.

(b) Impossibility Created by One Party

Impossibility

If, by the act or default of, one party further commercial performance of the contract is made impossible,[50] although that party has not, by words or conduct, renounced the intention to fulfil it, the other party will be discharged.

differs from renunciation

Renunciation is usually easier to establish because the innocent party need only show that the conduct of the promisor was such as to lead a reasonable person to believe that the promisor did not intend to perform the promise, whereas if reliance is placed on impossibility the innocent party must show that the contract was in fact impossible of performance due to the default of the promisor. But it is

[48] *The Mihalis Angelos* [1971] 1 Q.B. 164.

[49] (1851) 17 Q.B. 127.

[50] If the impossibility arises through the occurrence of some external event, which radically alters the nature of the obligation (but not otherwise), the contract may be discharged by frustration: see *ante*, pp. 503, 506.

an independent ground for discharge, as can be seen from *Universal Cargo Carriers Corporation* v. *Citati*:[51]

UCC chartered a ship to C who agreed to nominate a berth and a shipper, and to provide a cargo, all before a certain day. Three days before the due date C had done none of these things. Although C was willing to perform the contract if he could, UCC cancelled it and found another charterer.

Devlin J. held that C had not renounced the contract, but, since he could not have performed before the delay became so long as to frustrate the commercial purpose of the contract, UCC was entitled to treat this inability to perform as discharging its obligations.

Here also the impossibility may be created either before performance is due or in the course of performance.

(i) Before performance is due

Anticipatory breach

If the act or default of a promisor which makes performance impossible occurs before the time for performance arrives, the effect is the same as though the promisor had renounced the contract at that time. Such impossibility need not be deliberately created: 'Anticipatory breach was not devised as a whip to be used for the chastisement of deliberate contract-breachers, but from which the shiftless, the dilatory, or the unfortunate are to be spared. It is not confined to any particular class of breach, deliberate or blameworthy, or otherwise; it covers all breaches that are bound to happen.[52]

The aggrieved party may sue at once. In *Lovelock* v. *Franklyn*:[53]

The defendant promised to assign to the plaintiff within 7 years from the date of his promise, all his interest in a lease for the sum of £140. Before the end of 7 years he assigned his interest to another person.

It was held that the plaintiff need not wait until the end of the 7 years to bring an action. Lord Denman C.J stated:[54]

The plaintiff has a right to say to the defendant: 'You have placed yourself in a situation in which you cannot perform what you have promised; you promised to be ready during the period of seven years; and, during that period, I may at any time tender you the money and call for an assignment, and expect that you should keep yourself ready; but, if I now were to tender you the money, you would not be ready'. That is a breach of the contract.

Similarly, in *Universal Cargo Carriers Corporation* v. *Citati* (*supra*), the shipowners' cancellation of the contract was not premature. They were permitted to anticipate a breach which was in fact inevitable.

It was argued on behalf of the defendant that he might have bought the ship back in time to place *her* at the plaintiff's disposal, but this was regarded by the Court as too speculative a possibility to take into account. By his sale of the ship,

[51] [1957] 2 Q.B. 401 (affirmed in part [1957] 1 W.L.R. 979 and reversed in part [1958] 2 Q.B. 254). See also *Sanko Steamship Co. Ltd.* v. *Eacom Timber Sales Ltd.* [1987] 1 Lloyd's Rep. 487 at p. 492.

[52] *Ibid.*, at p. 438.

[53] (1846) 8 Q.B. 371.

[54] *Ibid.*, at p. 378. See also *Omnium D'Enterprises* v. *Sutherland* [1919] 1 K.B. 618.

the defendant had put it out of his power to perform thereafter his contract with the plaintiff; the contract was at an end and the plaintiff might bring an action for damages forthwith.

(ii) During performance

Impossibility created during performance

The rule is similar where the complete performance of the contract is made impossible by the act or default of one party. This is illustrated by the case of *O'Neil* v. *Armstrong*:[55]

O'N, a British subject, was engaged by A, the captain of a warship owned by the Japanese Government, to act as a fireman on a voyage from the Tyne to Yokohama. In the course of the voyage the Japanese Government declared war on China. O'N was informed that performance of the contract would bring him under the penalties of the Foreign Enlistment Act. He consequently left the ship, and sued A for the wages agreed upon.

It was held that he was entitled to succeed in his action, for the act of A's principal, the Japanese Government, had made his performance of the contract legally impossible.

Prevention of performance by promisee

It will be seen from this case that discharge by breach may occur, not only where one party disables itself from performing the contract, but also where it prevents completion of the contract by the other party.[56] The Courts are often ready to imply a term that each party undertakes to do all that is necessary to secure performance of the contract.[57] Thus if a licence is required for the export of goods, and the buyer fails to provide the seller with the information necessary to obtain the licence, no action will lie against the seller for non-delivery.[58] In some situations, where performance has thus been prevented by the promisee, the contract is taken as satisfied and the promisor can sue for the full remuneration or price.[59] But in most cases the promisor will be forced to sue for damages for the breach, since the contract cannot be fulfilled without the co-operation of the party in default.[60]

(c) Failure of Performance

Failure of performance

Failure of performance, whether total or partial, is the most common ground for the discharge of a party by breach. But it is not every failure of performance by one party which entitles the other to be discharged from its own liabilities under it. In order to determine if this is so, it is necessary to ask a number of questions.

[55] [1895] 2 Q.B. 418.

[56] See also *Ogdens Ltd.* v. *Nelson* [1905] A.C. 109. Cf. *Bremer Vulkan* v. *South India Shipping Co.* [1981] A.C. 909 (both parties in breach).

[57] *Stirling* v. *Maitland* (1864) 5 B. & S. 840, at p. 852; *Southern Foundries (1936) Ltd.* v. *Shirlaw* [1940] A.C. 701; *The Unique Mariner (No. 2)* [1979] 1 Lloyd's Rep. 37. Cf.. *Rhodes* v. *Forwood* (1876) 1 App. Cas. 256; *Luxor (Eastbourne) Ltd.* v. *Cooper* [1941] A.C. 108. See Bateson [1960] J.B.L. 187; Burrows (1968) 31 M.L.R. 390.

[58] *Kyprianou* v. *Cyprus Textiles Ltd.* [1958] 2 Lloyd's Rep. 60.

[59] *Mackay* v. *Dick* (1881) 6 App. Cas. 256. See also *Metro Meat Ltd.* v. *Fares Rural Co. Pty. Ltd.* [1985] 2 Lloyd's Rep. 13.

[60] *Colley* v. *Overseas Exporters* [1921] 3 K.B. 302. Contrast *White and Carter (Councils) Ltd.* v. *McGregor* [1962] A.C. 413 (*ante*, pp. 535–6) where no co-operation necessary.

(i) Are the promises independent?

Independent promises

In certain circumstances, the obligations entered into by each party may be independent of each other in the sense that neither party can claim to be released from its promise by the failure of the other to perform its part. Put in another way, each party can enforce the obligations undertaken by the other even though it has not performed its own. For example, in the case of leases, a tenant's covenant to pay rent is independent of a landlord's covenant to repair; the tenant cannot withhold payment on the ground that the landlord has failed to repair the premises.[61] Again, a covenant by a husband in a separation deed to pay his wife maintenance has been said to be independent of any covenant on her part, e.g. not to molest him.[62] And, because of the involvement of third parties in documentary sales, the obligation of a buyer to pay when the shipping documents are tendered has been held to be independent of the seller's obligation to supply goods conforming to the contract.[63] But the tendency of the Courts is against construing a contract in this way unless the parties clearly intend to do so because such a construction means that both parties are inadequately protected from the risk of non-performance by the other.[64] Thus, in a contract for work or services, the obligation to pay would fall due although the work had not been done.

Inter-dependent promises & concurrent conditions

Normally, however, the obligations of each party will be regarded as *interdependent*. For example, an employee who has been wrongfully dismissed is not bound to observe a covenant in restraint of trade.[65] The clearest example of obligations which are dependent on each other arises if the parties agree that the performance of their respective promise shall be simultaneous, or at least that each shall be ready and willing to perform its promise at the same time. Then the obligation to perform each promise is dependent or conditional on this concurrence of readiness and willingness to perform the other; their mutual promises are *concurrent conditions*. Thus section 28 of the Sale of Goods Act 1979 provides that in a contract for the sale of goods:

> Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions, that is to say, the seller must be ready and willing to give possession of the goods to the buyer in exchange for the price and the buyer must be ready and willing to pay the price in exchange for possession of the goods.

Failure to tender the goods discharges the buyer from its obligation to pay the price; failure to tender the price discharges the seller from its obligation to deliver the goods.

[61] *Taylor* v. *Webb* [1937] 2 K.B. 283.

[62] *Fearon* v. *Earl of Aylesford* (1884) 14 Q.B.D. 792, at p. 800. See also *Winstone* v. *Linn* (1823) 1 B. & C. 460 (contract of apprenticeship). Cf.. *Ellen* v. *Topp* (1851) 6 Exch. 424.

[63] *Gill & Duffus S.A.* v. *Berger & Co.* [1984] A.C. 382 (c.i.f. sale). See also *Vagres Comp. Maritima S.A.* v. *Nissho-Iwai America Corp. (The Karin Vatis)* [1988] 2 Lloyd's Rep. 330 (terms of contract rendered obligation to pay freight when cargo loaded independent of charterer's obligations).

[64] See also, *ante*, pp. 485–6.

[65] *General Billposting Co. Ltd.* v. *Atkinson* [1909] A.C. 118. See also *Rock Refrigeration Ltd.* v. *Jones* [1997] 1 All E.R. 1, but cf. the doubts of Phillips L.J. at pp. 18–19 and note that some primary obligations do continue after discharge, *post*, p. 551.

(ii) Is the obligation an 'entire' obligation?

Entire obligations

It has already been pointed out in Chapter 12, Performance,[66] that certain obligations are 'entire' in the sense that the liability of one party is dependent upon the complete performance of the obligation by the other. Subject to the doctrine of substantial performance,[67] if A agrees to make a dress for B in return for a promise to pay for the dress on completion, anything less than complete performance by A will release B from her obligation to pay. It is immaterial how the failure to effect complete performance comes about. It may be due to a deliberate abandonment of the contract, to a negligent act or omission, or, as in *Cutter* v. *Powell* noted above,[68] to a simple misfortune occurring without any fault.

Divisible obligations

Entire obligations are, however, the exception rather than the rule. The obligations in most bilateral contracts are 'divisible' in the sense that the breach of any one or more of them will not necessarily constitute a ground of discharge. The contract may, for example, be a complex one, composed of a number of undertakings differing in character or importance; or it may be a promise to do a number of successive acts; or to do a single act which can be partly or defectively performed. A failure by one party precisely to perform its obligations under the contract will give a right of action in damages to the other; but it will not necessarily discharge the innocent party from the performance of its own obligations under the contract.

(iii) Is the term broken a condition?

Conditions

Assuming that the obligations in the contract are divisible, and not entire, the question then arises whether the particular term which has been broken is a condition of the contract. From an historical point of view, the right of the innocent party to choose to be treated as discharged was said to turn upon the non-performance of a 'condition precedent' in the contract.[69] Performance by one party of that party's promise or 'covenant' was regarded as a condition precedent to the liability of the other. The classification of contractual terms has been dealt with in Chapter 4 of this book,[70] and it was there noted that, at the present day, a term will only be classified as a condition if it has been so categorized by statute (for instance by the Sale of Goods Act 1979) or by judicial decision, or if the parties have so agreed in their contract, either expressly or by implication.[71] Any breach of a condition will entitle the innocent party to choose to be treated as discharged.[72] It was also noted, however, that there has now emerged a category of 'intermediate terms', the breach of which will not necessarily produce that effect.[73]

[66] See *ante*, p. 475.

[67] See *ante*, p. 487.

[68] (1795) 6 Term R. 320, *ante*, pp. 484–5.

[69] *Pordage* v. *Cole* (1669) 1 Wms. Saund. 319; *Kingston* v. *Preston* (1773) 2 Doug. 689, at p. 691. The history of the expression is expounded in *Cehave N.V.* v. *Bremer Handelsgesellschaft* [1976] Q.B. 44, at pp. 57, 72; *United Scientific Holdings Ltd.* v. *Burnley B.C.* [1978] A.C. 904, at p. 927. See also Dawson [1981] C.L.J. 83, at p. 87.

[70] *Ante*, pp. 133–41.

[71] *Ante*, pp. 143–56.

[72] See e.g., *Union Eagle Ltd.* v. *Golden Achievement Ltd* [1997] A.C. 514.

[73] *Ante*, p. 138.

(iv) Does the breach go to 'the root of the contract'?

Breach going to root of contract

If the term broken is not a condition, but an intermediate term, the right of the innocent party to choose to be treated as discharged from further performance will depend upon the nature and consequences of the breach. Differing terminology has been used by the Courts to describe the test to be applied, the most common being that the breach must go to 'the root of the contract'.[74] It has also been said that the breach must be 'fundamental',[75] that it must 'affect the very substance of the contract'[76] or 'frustrate the commercial purpose of the venture'.[77] The use of these and similar expressions emphasizes that the breach must be far-reaching in its effect in order to justify discharge. A test which is nowadays frequently applied is that stated by Diplock L.J. in *Hongkong Fir Shipping Co. Ltd.* v. *Kawasaki Kisen Kaisha Ltd.*:[78] 'Does the occurrence of the event deprive the party who has further undertakings to perform of substantially the whole benefit which it was the intention of the parties as expressed in the contract that he should obtain as the consideration for performing those undertakings?' In that case:

> The plaintiff chartered to the defendant the m.v. *Hongkong Fir* for a period of 24 months, on terms that she was 'in every way fitted for ordinary cargo service'. The vessel was an old one, and by reason of its age needed to be maintained by an experienced, competent, careful, and adequate engine room staff. This the plaintiff did not provide. The chief engineer was addicted to drink and inefficient, and the engine room complement inadequate, with the result that there were many serious breakdowns in machinery. In the first 7 months of the charter the ship was only 8 and a half weeks at sea, the rest of the time being spent in breakdowns and repair to make the ship seaworthy; but this was eventually achieved. The defendant refused to continue with the charterparty.

It was argued on behalf of the defendant that the term as to seaworthiness was a condition of the contract, and that it was therefore entitled as of right to treat itself as discharged. This argument was not accepted by the Court of Appeal.[79] The Court then went on to hold, on the facts, that the delays which had already occurred, and the delay which was likely to occur, as a result of the vessel's unseaworthiness, and the conduct of the plaintiff in taking steps to remedy the same, were not, when taken together, such as to deprive the defendant of substantially the whole benefit which it was the intention of the parties the defendant should obtain from further use of the ship under charterparty. The defendant had therefore unjustifiably treated the contract as repudiated.

[74] *Mersey Steel & Iron Co.* v. *Naylor, Benzon & Co.* (1884) 9 App. Cas. 434, at p. 444; *Heyman* v. *Darwins Ltd.* [1942] A.C. 356, at p. 397; *Suisse Atlantique Société d'Armement S.A.* v. *N.V. Kolen Centrale* [1967] 1 A.C. 361, at p. 422; *Cehave N.V.* v. *Bremer Handelsgesellschaft* [1976] Q.B. 44, at pp. 60, 73; *Federal Commerce & Navigation Co. Ltd.* v. *Molena Alpha Inc.* [1979] A.C. 757, at p. 779.

[75] *Suisse Atlantique Société d'Armement S.A.* v. *N.V. Kolen Centrale* (*supra*, n. 74), at pp. 397, 409–10, 421–2, 431.

[76] *Wallis, Son and Wells* v. *Pratt and Haynes* [1910] 2 K.B. 1003, at p. 1012.

[77] *MacAndrew* v. *Chapple* (1866) L.R. 1 C.P. 643, at pp. 647, 648; *Jackson* v. *Union Marine Insurance Co.* (1874) L.R. 10 C.P. 125, at pp. 145, 147, 148; *Trade and Transport Inc.* v. *Iino Kaiun Kaisha Ltd.* [1973] 1 W.L.R. 210, at p. 223.

[78] [1962] 2 Q.B. 26, at p. 66.

[79] See *ante*, p. 138.

Instalment contracts

The same approach has been adopted with respect to contracts to deliver and pay for goods by instalments. If the seller makes defective deliveries in respect of one or more instalments, or the buyer neglects or refuses to take delivery of or pay for one or more instalments, this will not necessarily permit the innocent party to choose to be treated as discharged. The question will arise whether the breach is a repudiation of the whole contract or whether it is a severable breach giving rise to a claim for damages but not to a right to treat the whole contract as repudiated.[80] The breach or breaches may, of course, amount to an express or implied renunciation of the contract.[81] But if they amount only to a failure of performance, they must go to the root of the contract in order to justify discharge. Thus in *Simpson* v. *Crippin*[82] it was agreed that 6,000 to 8,000 tons of coal should be delivered in equal monthly instalments during a period of 12 months, the buyer to send waggons to receive the coal; the buyer sent waggons for only 158 tons in the first month, but the seller was not held entitled to cancel the contract as the breach did not go 'to the whole root and consideration of the agreement'.

On the other hand, in *Honck* v. *Muller*:[83]

H, in October 1879, bought from M 2,000 tons of pig iron to be delivered 'in November, 1879, or equally over November, December and January next at 6*d. per* ton extra'. H failed to take delivery of any iron in November, but claimed to have delivery of one-third of the iron in December and one-third in January. M refused, and gave notice that he considered the contract discharged.

H brought an action for breach and failed, as a majority of the Court considered that his failure of performance was so substantial as to discharge M from further liability. [84]

In contracts for the sale and delivery of goods by instalments, the most relevant factors have been said to be, 'First, the ratio quantitatively which the breach bears to the contract as a whole, and secondly the degree of probability or improbability that such a breach will be repeated'.[85] The importance of the second factor was clearly emphasized by Bingham J. in *Millar's Karri and Jarrah Co.* v. *Weddel*:[86]

If the breach is of such a kind, or takes place in such circumstances as reasonably to lead to the inference that similar breaches will be committed in relation to subsequent deliveries, the whole contract may there and then be regarded as repudiated and may be rescinded. If, for instance, a buyer fails to pay for one delivery in such circumstances as to lead to the inference that he will not be able to pay for subsequent deliveries; or if a seller delivers goods differing from the requirements of the contract, and does so in such circumstances as to lead to the inference that he cannot, or will not, deliver any other kind of

[80] Sale of Goods Act 1979, s. 30(2) and (2A).
[81] See *ante*, p. 539.
[82] (1872) L.R. 8 Q.B. 14.
[83] (1881) 7 Q.B.D. 92. See also *Munro & Co. Ltd.* v. *Meyer* [1930] 2 K.B. 312 (nearly half of goods seriously adulterated).
[84] *Maple Flock Co. Ltd.* v. *Universal Furniture Products (Wembley) Ltd.* [1934] 1 K.B. 148, *per* Lord Hewart C.J. at p. 157.
[85] *Ibid.*
[86] (1909) 100 L.T. 128, at p. 129.

goods in the future, the other contracting party will be under no obligation to wait to see what may happen; he can at once cancel the contract and rid himself of the difficulty.

It follows that, the further parties have proceeded with the due performance of a contract, the less likely it is that one party will be able to claim that it has been discharged by a single breach.[87]

The right of discharge therefore depends on the answer to this question: Does the breach go so far to the root of the contract as to entitle the injured party to say, 'I have lost all that I cared to obtain under this contract; further performance cannot make good the prior default'?[88]

III. Consequences of Discharge[89]

Effect of discharge

An innocent party who is entitled to, and does, choose to be treated as discharged by the other party's breach, is thereby released from further performance of those future obligations which remain still to be performed. After such discharge the innocent party is not bound to accept, or pay for, any further performance by the party in breach. The duty of the party in default to perform future unperformed obligations likewise comes to an end, as does that party's right to perform them.

Contract not rescinded *ab initio*

In the terminology employed in many of the cases, these consequences are often described as a 'rescission' of the contract; or it is stated that the contract is 'terminated' or 'put an end to' by the breach. But these expressions are somewhat misleading:

> To say that the contract is rescinded or has come to an end or ceased to exist may in individual cases convey the truth with sufficient accuracy, but the fuller expression that the injured party is thereby absolved from future performance of his obligations under the contract is a more exact description of the position. Strictly speaking, to say that on acceptance of the renunciation of the contract the contract is rescinded is incorrect.[90]

and accrued obligations remain

Certainly, this so-called rescission is quite different from rescission *ab initio*, such as may arise, for example, in cases of misrepresentation or mistake.[91] The contract is not set aside as from the beginning. Rights and obligations which arise from the partial execution of the contract and causes of action which have accrued from its breach alike continue unaffected.[92] So, for instance, if a time charterparty of a

[87] *Cornwall* v. *Henson* [1900] 2 Ch. 298, at p. 304.

[88] Cited with approval in *Alkok* v. *Grymek* (1966) 56 D.L.R. (2d) 393 (Canada).

[89] See Shea (1979) 42 M.L.R. 623; Beatson (1981) 97 L.Q.R. 389; Rose (1981) 34 C.L.P. 235; Law Commission Report, *Pecuniary Restitution on Breach of Contract* (1983), No. 121.

[90] *Heyman* v. *Darwins Ltd.* [1942] A.C. 356, *per* Lord Porter at p. 399. This statement was unanimously approved by the House of Lords in *Johnson* v. *Agnew* [1980] A.C. 367. See also *Bank of Boston Connecticut* v. *European Grain and Shipping Ltd.* [1989] A.C. 1056, at pp. 1098–9 and *State Trading Corpn. of India Ltd* v. *M. Golodetz Ltd.* [1989] 2 Lloyd's Rep. 277, at p. 286.

[91] *Johnson* v. *Agnew* (*supra*, n. 90), at p. 393.

[92] *McDonald* v. *Dennys Lascelles Ltd.* (1933) 48 C.L.R. 457, *per* Dixon J. at p. 476. But, once the contract has been discharged, equitable relief, e.g. an injunction, cannot be granted: *Walker* v. *Standard Chartered Bank plc* [1992] B.C.L.C. 535.

ship is repudiated by the charterer, the shipowner can recover arrears of hire charges due but unpaid up to the date of the shipowner's acceptance of the repudiation,[93] and if building work is to be paid for by instalments, the builder can sue for any instalment due but unpaid at the time of discharge.[94] It makes no difference in this respect whether the accrued obligation is one in favour of the innocent or the guilty party. An employee who repudiates a contract of employment, can nevertheless sue for wages earned before that time.[95] Admittedly, if money has been paid by one party to the other under the contract, and the consideration for the payment has wholly failed, the money may be recoverable in restitution by an action for money had and received.[96] But, in principle, accrued liabilities remain enforceable despite the discharge. Moreover, as we have seen,[97] only the primary obligations of the parties as a general rule come to an end. The primary obligations of the party in default are then replaced by a secondary obligation to pay compensation to the injured party for the breach. Note, however, certain primary obligations will survive discharge and continue to be enforceable. The continued enforcement of such obligations simply reflects the presumed intention of the parties.[98]

Quantum meruit claims

With respect to payments not yet due at the time of discharge, for example, for goods supplied or for services performed under the contract, the innocent party can sue for the reasonable value of these on a *quantum meruit* or *quantum valebat*,[99] or include them in his claim for damages for breach. Whether the guilty party has any claim will depend on whether the contract is entire or divisible. If it is entire, in principle no claim is possible.[100] But if it is divisible, the guilty party may be entitled to claim in respect of performance completed, subject to a counterclaim for damages by the innocent party in respect of loss suffered by the breach.

IV. Loss of the Right of Discharge

THE right of discharge may be lost by waiver, affirmation, acceptance, and operation of law. In addition a party may be estopped from claiming to be entitled to treat a contract as discharged. This has been dealt with earlier in this book.[101]

[93] *Leslie Shipping Co.* v. *Welstead* [1921] 3 K.B. 420. See also *Chatterton* v. *Maclean* [1951] 1 All E.R. 561 (hire-purchase).

[94] *Hyundai Heavy Industries Co. Ltd.* v. *Papadopoulos* [1980] 1 W.L.R. 1129 (H.L.).

[95] *Taylor* v. *Laird* (1856) 25 L.J. Ex. 29. Cf.. Apportionment Act 1870, s. 2.

[96] See *post*, p. 604.

[97] See *ante*, p. 550.

[98] The best examples are arbitration clauses and other dispute resolution mechanisms: *Heyman* v. *Darwins Ltd.* [1942] A.C. 356. In addition, there are clauses that may only come into operation upon discharge such as certain liquidated damages clauses. See also the interesting example in *Yasuda Fire & Marine Insurance Co. of Europe Ltd.* v. *Orion Marine Insurance Underwriting Agency Ltd.* [1995] Q.B. 174 (agent's duty to provide records to its principal).

[99] See *post*, p. 610.

[100] See *ante*, pp. 485–7. But see *post*, p. 607.

[101] See *ante*, pp. 494–500 and 110.

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Discharge by Operation of Law

THERE are rules of law which, operating upon certain sets of circumstances, will bring about the discharge of a contract, and these we will briefly consider.

I. Merger

Merger

IF a higher security is accepted in place of a lower, the security which in the eye of the law is inferior in operative power,[1] in the absence of a contrary intention manifested by the parties, merges and is extinguished in the higher.

Thus, if two parties to a simple contract embody its contents in a deed which they both execute, the simple contract is thereby discharged. This most often happens in the case of contracts for the sale of land, the written agreements being merged and extinguished in the subsequent conveyance under seal.[2]

The rules governing this process may thus be summarized:

(1) The later security must be of higher efficacy than that which it is sought to replace. A negotiable instrument is not a higher security for the purposes of this rule,[3] although the giving of a negotiable instrument may constitute payment of a debt.[4]

(2) The subject-matter of the two securities must be the same, that is, they must secure the same obligation and be made between the same parties.[5]

Vesting in same person

The rights and liabilities under a contract are also extinguished if they become vested by assignment or otherwise in the same person and in the same right, for it is not possible to contract with oneself. So where a tenant for a term of years retains the lease and acquires the reversion, the lease merges in the reversion and is destroyed.[6] Similarly, a bill of exchange is discharged if the acceptor is or becomes the holder of it at or after its maturity in his own right.[7]

[1] *Price* v. *Moulton* (1851) 10 C.B. 561.

[2] *Knight Sugar Co. Ltd.* v. *Alberta Ry. and Irrigation Co.* [1938] 1 All E.R. 266, at p. 269. Cf. *Tito* v. *Waddell (No. 2)* [1977] Ch. 107, at p. 284 (contrary intention).

[3] *Drake* v. *Mitchell* (1803) 3 East 251.

[4] See *ante*, p. 479.

[5] *Twopenny* v. *Young* (1824) 3 B. & C. 208; *Holmes* v. *Bell* (1841) 3 M. & G. 213; *Hissett* v. *Reading Roofing Co. Ltd.* [1969] 1 W.L.R. 1757.

[6] *Capital and Countries Bank Ltd.* v. *Rhodes* [1903] 1 Ch. 631. By a rule of equity, however, the intentions of the parties may operate to prevent the occurrence of such merger. Under the provisions of the Law of Property Act 1925, s. 185 the equitable rule now prevails in all cases.

[7] Bills of Exchange Act 1882, s. 61.

II. Discharge by Judgment of a Court

By judgment

A RIGHT of action arising from breach of contract is discharged by the judgment of a Court of Record[8] in the plaintiff's favour for the same demand. The right is thereby merged in the more solemn form of obligation called a Contract of Record. The result of legal proceedings taken upon a broken contract may be summarized as follows:

Effect of bringing action

The bringing of an action has not itself any effect in discharging the right to bring the action. Another action may be brought for the same cause, although proceedings in such an action would, if they were merely vexatious, be struck out or stayed upon application to the summary jurisdiction of the Court.[9]

Effect of judgment for plaintiff

But when judgment is given in the plaintiff's favour, the cause of action is merged into matter of record, and only the judgment can be enforced.[10] Further, 'damages resulting from one and the same cause of action must be assessed and recovered once for all',[11] so that successive judgments cannot be obtained for different breaches of a single undertaking.[12]

Adverse judgments

A person may be estopped *per rem judicatam* from re-litigating in subsequent proceedings a cause of action in respect of which judgment was given against that person in earlier proceedings, or an issue raised and determined against him or her in such proceedings.[13] But, for such an estoppel to arise, certain conditions must be satisfied:[14] first, there must have been a final judgment on the merits[15] in the earlier proceedings by a court of competent jurisdiction;[16] secondly, there must be identity of parties in the two sets of proceedings;[17] thirdly, there must be identity of subject-matter in the two proceedings.[18] Cause of action and issue estoppel are based upon the public interest in finality of litigation.[19]

[8] A county court is a court of record: County Courts Act 1984, s. 1(2).

[9] R.S.C. Ord. 18, r. 19; C.C.R., Ord. 13, r. 5; County Courts Act 1984, s. 35.

[10] *Kendall* v. *Hamilton* (1879) 4 App. Cas. 504.

[11] *Brunsden* v. *Humphrey* (1884) 14 Q.B.D. 141, *per* Bowen L.J. at p. 147; *Furness, Withy & Co. Ltd.* v. *Hall Ltd.* (1909) 25 T.L.R. 233.

[12] *Conquer* v. *Boot* [1928] 2 K.B. 336. But see *Overstone Ltd.* v. *Shipway* [1962] 1 W.L.R. 117 (separate causes of action).

[13] *Palmer* v. *Temple* (1839) 9 A. & E. 508.

[14] *Carl Zeiss Stiftung* v. *Rayner & Keeler Ltd. (No. 2)* [1967] 1 A.C. 853, at pp. 909, 910.

[15] *Hines* v. *Birbeck College (No. 2)* [1992] Ch. 33.

[16] *Midland Bank Trust Co. Ltd.* v. *Green* [1980] Ch. 590; *Hines* v. *Birbeck College (No. 2)* [1992] Ch. 33; *The European Gateway* [1987] Q.B. 206.

[17] *Gleeson* v. *J. Wippell & Co. Ltd.* [1977] 1 W.L.R. 510; *North West Water Ltd.* v. *Binnie & Partners* [1990] 3 All E.R. 547; *House of Spring Gardens Ltd.* v. *Waite* [1991] 1 Q.B. 241, at p. 252; *Talbot* v. *Berkshire C.C.* [1994] Q.B. 290, at pp. 296–7. Cf. *Marginson* v. *Blackburn B.C.* [1939] 2 K.B. 426; *C (a minor)* v. *Hackney London B.C.* [1996] 1 All E.R. 973.

[18] *Haystead* v. *Commissioner of Taxation* [1926] A.C. 155.

[19] *Republic of India* v. *India Steamship Co. Ltd.* [1993] A.C. 410, at p. 415; *Thrasyvoulou* v. *Secretary of State for the Environment* [1990] 2 A.C. 273, at p. 289. While a foreign judgment does not operate as a merger, under Civil Jurisdiction and Judgments Act 1982, s. 34, further proceedings are barred unless waived: [1993] A.C. 410, at pp. 423–4.

III. Alteration or Cancellation of a Written Instrument

Rule as to alteration

If a deed or contract in writing is altered by addition or erasure, it is discharged, except as against a party making or assenting to the alteration, for 'no man shall be permitted to take the chance of committing a fraud, without running any risk of losing by the event, when it is detected'.[20]

This principle is subject to the following rules:

(1) The alteration must be made deliberately by the promisee or by one acting with the promisee's consent;[21] and even an alteration by a stranger while the instrument is in the custody of the promisee will have the same effect.[22] Previous editions of this book stated that this responsibility for the acts of officious burglars, could not be supported, but although recently described as 'a harsh and ancient common law doctrine', it is good law.[23]

(2) The alteration must be made without the consent of the other party, else it would operate as a new agreement.

(3) The alteration must be made in a material part. What amounts to a material alteration necessarily depends upon the character of the instrument, and it is possible for the character of an instrument to be affected by an alteration which does not touch the contractual rights set forth in it. In a Bank of England note an alteration in the number of the note is not an alteration of the contractual terms which the document contains; but the fact that a bank note is a part of the currency, and that the number placed on it is put to important uses by the Bank and by the public for the detection of forgery and theft, causes an alteration in the number to be regarded as material and to invalidate the note.[24] In most cases, however, a material alteration will be one which imposes a greater liability on the promisor.

Bills of Exchange

The Bills of Exchange Act 1882, section 64, provides that a bill shall not be avoided as against holder in due course, though it has been materially altered, if the alteration is not apparent, and the holder may enforce payment of it according to its original tenor.

Cancellation and loss

Intentional cancellation of a written instrument by the promisee also discharges the obligation, but the loss of the instrument only affects the rights of the parties in so far as it may occasion a difficulty of proof. In the case of bills of exchange and promissory notes, if the holder of the instrument loses it, *he* may require the drawer to give him another bill upon his giving an indemnity against possible claims.[25]

[20] *Master* v. *Miller* (1791) 4 Term Rep. 320, *per* Lord Kenyon C.J. at p. 329.

[21] *Pattinson* v. *Luckley* (1875) L.R. 10 Ex. 330; *Hongkong & Shanghai Banking Corporation* v. *Lo Lee Shi* [1928] A.C. 181. Cf. *Co-operative Bank* v. *Tipper* [1996] 4 All E.R. 366, at p. 371 (pencilled alteration insufficient).

[22] *Pigot's Case* (1614) 11 Co. Rep. 26b; *Davidson* v. *Cooper* (1844) 13 M. & W. 343.

[23] *Goss* v. *Chilcott* [1996] A.C. 788; *Co-operative Bank* v. *Tipper* (*supra*, n. 21) at p. 369. But the nullifying operation is confined to cases falling strictly within its ambit: *Farrow Mortgage Services Pty. Ltd.* v. *Slade* (1996) 38 N.S.W.L.R. 636, at p. 640.

[24] *Suffell* v. *Bank of England* (1882) 9 Q.B.D. 555.

[25] Bills of Exchange Act 1882, s. 69.

IV. Bankruptcy

Bankruptcy

A CONTRACT is not discharged by bankruptcy of one of the parties to it;[26] but it effects a statutory release from debts and liabilities provable under the bankruptcy, when the bankrupt has obtained from the Court an order of discharge. It is sufficient to call attention to this mode of discharge, without entering into a discussion of the nature and effects of bankruptcy, or the provisions of the Insolvency Act 1986.

[26] *Re Edwards, ex parte Chalmers* (1873) L.R. 8 Ch. App. 289; see *ante*, p. 470.

PART 5

Remedies for Breach of Contract

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Damages

WE have already endeavoured to state the rules which govern the discharge of a contract by breach, and it now remains to consider the various remedies which are available apart from the entitlement of the innocent party in an appropriate case to be treated as discharged from further performance.

These remedies fall under three heads:[1]

(1) Every breach of contract entitles the injured party to damages for the loss he or she has suffered.

(2) In certain circumstances the injured party may obtain the enforcement of the promise by an order for specific performance of the contract, an injunction to restrain its breach or for the payment of the sum due under the contract.

(3) In certain circumstances the parties to a contract that has been broken may be entitled to the return of money paid, recompense for services rendered or goods transferred, or a money award reflecting the gain to the defendant. These are restitutionary remedies. Although some of them are based on a distinct branch of the law of obligations, restitution, and are not based on breach of contract, others are based on contract.

In this and the following three chapters we shall consider each of these remedies in turn, and also how the rights of action created by a breach of contract may be barred by lapse of time.

Except in the case of a debt, the repayment of which may be specifically enforced at common law by an award of the agreed sum, the common law remedy for breach of a contractual promise is that of damages. We have mentioned the overlap between the law of contract and the law of restitution. In certain cases, for example professional negligence cases, there will be overlapping claims in contract and in tort. The rules discussed in this section only apply to contractual damages. However, it should be borne in mind that in cases of overlap with the law of tort an alternative, and sometimes preferable, remedy may be available.[2]

[1] See Burrows, *Remedies for Torts and Breach of Contract*, 2nd edn. (1993); Harris, *Remedies in Contract and Tort* (1988); Treitel, *Remedies for Breach of Contract* (1988).

[2] *Ante*, p. 21. See, for example, *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145; *Midland Bank Trust Co. Ltd.* v. *Hett Stubbs & Kemp* [1979] Ch. 384 (limitation). But cf. *Parsons (H.) (Livestock) Ltd.* v. *Uttley Ingham & Co. Ltd.* [1978] Q.B. 791 (remoteness).

I. Compensatory Nature of Damages

Compensatory nature of damages

DAMAGES for breach of contract are designed to compensate for the damage, loss or injury the plaintiff has suffered through that breach. A plaintiff who has not, in fact, suffered any loss by reason of the breach, is nevertheless entitled to a verdict, but the damages recoverable will be purely nominal (usually £2).

Whereas physical losses are the most frequent subject of actions in tort, commercial losses are the most frequent subject of actions for breach of contract. However, as will be seen, damages for breach of contract are not necessarily limited to compensation of financial loss alone. Damages may also be awarded in contract to compensate for physical damage to the person or property, for the loss of an attribute of property (such as comfort or privacy) even where this has not affected its value, for inconvenience, and, in certain circumstances, for disappointment.

(a) Difficulty of Assessment No Bar

Difficulty of assessment no bar

Difficulty in assessing damages does not, however, disentitle a plaintiff from having an attempt made to assess them, unless they depend altogether on remote and hypothetical possibilities. This can be seen from the case of *Simpson* v. *London and North Western Railway Company*,[3] where the plaintiff was deprived of the opportunity of exhibiting his products at an agricultural show. Although the ascertainment of damages was difficult and speculative, it was held that this was no reason for not giving any damages at all. So, too, in *Chaplin* v. *Hicks*,[4] where a candidate in a beauty competition, who had successfully passed the earlier stages of the competition, was, in breach of contract, not allowed to compete in the later stages with 49 others from whom 12 winners were to be chosen, she was awarded substantial damages for the loss of the chance of being successful (approximately 25 per cent), of which she had been wrongfully deprived. Similar considerations may affect the measure of damages in the cases where an offer to consider all conforming tenders is held to give rise to an enforceable obligation.[5]

(b) Damages are Not Punitive

Damages are not punitive

Damages for breach of contract are given by way of compensation for loss suffered, and not by way of punishment for wrong inflicted. The measure of damages is therefore not affected by the motive of the breach. 'Vindictive' or 'exemplary' damages have no place in the law of contract.[6] Contractual damages

[3] (1876) 1 Q.B.D. 274; *post*, p. 576.

[4] [1911] 2 K.B. 786. *Allied Maples Group* v. *Simmons & Simmons* [1995] 1 W.L.R. 1602. Cf. *Sapwell* v. *Bass* [1910] 2 K.B. 486.

[5] *Blackpool and Fylde Aero Club Ltd.* v. *Blackpool B.C.* [1990] 1 W.L.R. 25, *ante*, p. 35, where the measure of damages was not considered.

[6] They may be recoverable in certain circumstances in tort: see *Rookes* v. *Barnard* [1964] A.C. 1129, at p. 1221; *Broome* v. *Cassell & Co. Ltd.* [1972] A.C. 1027; *A.B.* v. *South West Water Services* [1993] Q.B. 507. For the arguments for and against the imposition of restitutionary damages in cases of 'cynical' breach, see *post*, p. 615.

cannot be used to punish, however outrageous the defendant's conduct. In *Addis* v. *Gramophone Co. Ltd.*:[7]

The appellant was employed by the respondents as manager of their business in Calcutta at a salary together with a commission on trade done. The respondents wrongfully dismissed him without giving him the required 6 months' notice.

The House of Lords held that, although he might recover a sum representing his salary for the period of notice and the commission he would have earned during that period, his employers were not to be penalized in damages for the sharp and oppressive manner in which they had dismissed him.[8]

(c) Compensation for Inconvenience or Disappointment

No compensation for distress or disappointment

Contractual damages may be recovered for substantial physical inconvenience or discomfort arising from a breach. For example, where a family were transported by a railway company to the wrong station, with the result that they had to walk several miles home on a drizzling wet night,[9] and where the plaintiff, with his wife and child, was forced to live for 2 years in discomfort with his wife's parents owing to the failure of a solicitor to take any effective steps to obtain possession of a house,[10] damages for the physical inconvenience were recovered. But damages are not generally recoverable for 'any distress, frustration, anxiety, displeasure, vexation, tension or aggravation' caused by the breach even where it was in the contemplation of the parties that the breach would expose the parties to distress.[11]

Unless the contract is to provide enjoyment or prevent distress

However, after some hesitation,[12] it now appears to be established that damages for distress can be given where the contract is one to provide enjoyment or to prevent distress[13] or where the plaintiff's distress is directly consequential on physical loss caused by the breach of contract.[14] In *Jarvis* v. *Swans Tours Ltd.*:[15]

[7] [1909] A.C. 488, followed on this point but not others (*post*, p. 563) by *Malik* v. *Bank of Credit & Commerce International S.A.* [1997] I.C.R. 606, at pp. 626–7. See also *Co-operative Insurance Society Ltd.* v. *Argyll Stores (Holdings) Ltd.* [1997] 2 W.L.R. 898, at p. 906 (H.L.). Cf. McBride (1995) 24 Anglo-American L.Rev. 369 for the argument that punitive damages should be awarded for deliberate breaches of contract.

[8] See also *Malik* v. *Bank of Credit & Commerce International S.A.* [1997] I.C.R. 606, at pp. 626–7, but note that the manner and circumstances of a dismissal may increase the plaintiff's financial loss: see *post*, p. 562.

[9] *Hobbs* v. *L. & S.W. Ry.* (1875) L.R. 10 Q.B. 111. [10] *Bailey* v. *Bullock* [1950] 2 All E.R. 1167.

[11] *Watts* v. *Morrow* [1991] 1 W.L.R. 1421, *per* Bingham L.J. at p. 1445. See also *Bliss* v. *S.E. Thames R.H.A.* [1987] I.C.R. 700 (contract of employment); *Hayes* v. *James & Charles Dodd* [1990] 2 All E.R. 815 (solicitor's contract to provide professional services); *Branchett* v. *Beaney* [1992] 3 All E.R. 910 (covenant for quiet enjoyment of property).

[12] Cf. *Addis* v. *Gramophone Ltd.* (*supra*, n. 7), *post*, p. 493; *Bailey* v. *Bullock* (*supra*, n. 10).

[13] *Jarvis* v. *Swan Tours Ltd.* [1973] Q.B. 233, *per* Lord Denning M.R. at p. 238; *Ruxley Electronics & Constructions Ltd.* v. *Forsyth* [1996] A.C. 344, *per* Lord Lloyd at p. 374. Cf. Lord Mustill, *ibid*, at pp. 360–1, on which see *post*, p. 566.

[14] *Perry* v. *Sydney Phillips & Son* [1982] 1 W.L.R. 1297 (anxiety and distress of living in a house in poor condition which had been bought in reliance on negligence in breach of contract in a surveyor's report); *Calebar Properties* v. *Sticher* [1984] 1 W.L.R. 287 (unpleasantness of living in deteriorating premises until they became uninhabitable because of landlord's delay in repairing). But such damages should be 'modest': *Watts* v. *Morrow* (*supra*, n. 11) at pp. 1443, 1445.

[15] [1973] Q.B. 233. See also *Jackson* v. *Horizon Holidays Ltd.* [1975] 1 W.L.R. 1468.

The plaintiff, a solicitor, was entitled to two weeks' paid holiday a year and booked with the defendant a 15–day Christmas winter sports holiday at a hotel in Switzerland. He did so on the faith of the defendant's brochure which described the holiday as a 'house-party', and promised a variety of entertainments including excellent skiing, a yodeller evening, a bar, and afternoon tea and cakes. In the first week there were only thirteen people at the hotel and in the second week he was entirely alone. The promised entertainments proved to be wholly inferior in quality in comparison with the description in the brochure.

The Court of Appeal held that he was entitled to damages consisting of the amount which he had paid for the holiday and an additional sum of some £60 to compensate him for the disappointment he had suffered. Similarly damages were awarded for anxiety and distress suffered by a woman whose solicitors failed to take prompt and effective measures against a man who was pestering her,[16] by a woman whose solicitors had failed to obtain proper financial relief in matrimonial proceedings,[17] by a bride when a photographer failed to keep his promise to be present and take photographs at her wedding,[18] and by children when a cemetery owner broke its contract to grant exclusive burial rights in a plot adjacent to that in which their parents were buried.[19] Such damages are nevertheless compensatory in nature and are not designed to inflict retribution on the defendant for inflicting the harm.

(d) Loss of Reputation

Loss of reputation

Although damages cannot be recovered in a contractual action for injury to reputation per se,[20] it has recently been established that they may be where the loss of reputation caused by the breach of contract causes financial loss. In *Malik* v. *Bank of Credit & Commerce International S.A.*:[21]

The plaintiffs, relatively senior employees of the defendant bank, were made redundant following the bank's insolvency. They claimed that they were unable thereafter to obtain employment in the financial services industry because of the stigma attached to former employees of the defendant, and sought substantial compensation for this handicap in the labour market. For the purposes of the proceedings it was assumed that the bank had carried on its business in a corrupt and dishonest manner, that this had become widely known, that the plaintiffs were innocent of any involvement, were at a handicap in the labour market because of the stigma, and had suffered financial loss as a result.

The House of Lords held that contracts of employment contained an implied term of mutual trust and confidence so that the defendant was under an implied obligation not to carry on a dishonest or corrupt business, and that, in principle,

[16] *Heywood* v. *Wellers* [1976] Q.B. 446; *McLeish* v. *Amoo-Gottfried & Co.*, *The Times*, 13 October 1995 (solicitor's negligence led to wrongful conviction). Cf. *Cook* v. *Swinfen* [1967] 1 W.L.R. 457, at p. 461; *Hayes* v. *James & Charles Dodd* [1990] 2 All E.R. 815.

[17] *Dickinson* v. *James Alexander & Co.* (1990) 20 Fam. L.R. 137 (C.A.).

[18] *Diesen* v. *Sampson* 1971 S.L.T. (Sh. Ct.) 49.

[19] *Reed* v. *Madon* [1989] Ch. 408.

[20] *Addis* v. *Gramophone Co. Ltd* [1909] A.C. 488, *ante*, p. 561.

[21] [1997] I.C.R. 606. See also *Edwards* v. *Society of Graphical and Allied Trades* [1971] Ch. 354, at p. 379.

financial loss in respect of damage to reputation caused by breach of this term is recoverable in a contractual action. It was, however, stated by their Lordships that it would often be difficult to prove a handicap on the labour market, and that the damage had to result from a relevant breach of contract; in the ordinary way any loss of reputation an employee may suffer from being wrongfully dismissed or from having been associated with an unsuccessful or grossly incompetent business will not found a claim.

The effect of this decision is to establish that financial loss resulting from a loss of reputation caused by a breach of contract is governed by general contractual principles. The contrary statements in *Addis* v. *Gramophone Co. Ltd.*[22] were explained in *Malik*'s case on the basis that the earlier case was decided before the development of the implied obligation of mutual trust and confidence so that the loss of reputation there had not been caused by a breach of contract,[23] and other cases will require reconsideration.[24]

Cases previously regarded as exceptional can now be seen as examples of the general rule. So, where a banker refuses to pay a customer's cheque when it has funds of the customer to meet, it will be liable in respect of any loss to the customer's trade reputation or credit-rating caused by the breach.[25] It is, moreover, no longer necessary to distinguish a breach of contract which causes injury to a reputation which a person already possesses from a breach of a specific undertaking to protect or enhance a person's reputation, for which damages were awarded prior to the decision in *Malik*'s case.[26] So, where a contract entitles an actor to be advertised as playing a leading part at a well-known music-hall, the actor may recover damages for the loss of publicity and for any injury that his failure to appear may cause to his existing reputation.[27] In view of the assumed facts in *Malik*'s case, there was no need to deal with a breach of contract that causes non-financial loss, for instance distress and injured feelings resulting from loss of reputation, but the increased willingness to award contractual damages for such losses[28] suggests that this aspect of *Addis*'s case may also be ripe for reconsideration.

[22] [1909] A.C. 488, for example *per* Lord Loreburn, at p. 491. For the facts, see *ante*, p. 561.

[23] [1997] I.C.R. 606, *per* Lord Nicholls, at p. 615 and *per* Lord Steyn at p. 627.

[24] e.g *Groom* v. *Crocker* [1939] 1 K.B. 194 (solicitors who wrongfully admitted negligence on the part of their motorist client, held not to be liable to him for 'loss of credit' as a careful driver).

[25] *Kpoharor* v. *Woolwich Building Society* [1996] 4 All E.R. 119, suggesting that a distinction between trade and personal transactions should no longer be made. *Gibbons* v. *Westminster Bank Ltd.* [1939] 2 K.B. 882; *Rae* v. *Yorkshire Bank* [1988] F.L.R. 1 (C.A.) in which non-traders were awarded only nominal damages, may no longer be justifiable in the light of *Malik* v. *Bank of Credit & Commerce International S.A.* (*supra*, n. 21).

[26] *Clayton & Waller Ltd.* v. *Oliver* [1930] A.C. 209.

[27] *Marbe* v. *George Edwardes (Daley's Theatre) Ltd.* [1928] 1 K.B. 269, at pp. 281, 288. The contrary decision in *Withers* v. *General Theatre Cpn. Ltd.* [1933] 2 K.B. 536, was overruled by *Malik* v. *Bank of Credit & Commerce International S.A.* (*supra*, n. 21), as must be *Joseph* v. *National Magazine Co. Ltd.* [1959] Ch. 14 (author) and *Dunk* v. *George Waller & Son Ltd.* [1970] 2 Q.B. 163 (apprentice).

[28] For the conditions under which such an award will be made see *ante*, pp. 561–2.

II. Basis of Assessment of Damages

Basis of assessment

THE general principle that damages are compensatory in nature is nevertheless only a starting point, and the question must still be asked—when a contract is broken and action is brought upon it, how are we to arrive at the amount which the plaintiff, if successful, is entitled to recover in respect of its loss?

(a) The 'Expectation' or 'Performance' Measure

The 'expectation' or 'performance' measure

The object of an award of damages for breach of contract is to place the plaintiff, so far as money can do it, in the same situation, with respect to damages, as if the contract had been performed.[29] Plaintiffs are thus enabled to recover damages in respect of the loss of gains of which they have been deprived by the breach. For example, if machinery is not delivered to a person or delivered late in breach of contract, that person will have a claim for loss of profits for being deprived of its use. Such a claim, however, is not peculiar to an action in contract, since a similar claim would lie if the machinery were damaged or destroyed by a tort. But the law of contract goes further and entitles plaintiffs (in appropriate circumstances) to damages for the loss of the bargained-for performance, that is to say, for the loss of the particular benefit which it was expected would be received by the contract which has been broken: an art dealer contracts to purchase a painting which is worth far more than the agreed price; a record company by contract obtains for a relatively modest sum the sole right to distribute the records of what proves to be a highly successful pop-group; a caterer obtains an extremely lucrative contract to cater for a banquet. In each case, if the contract is broken by the other party, the damages will be assessed by reference to the plaintiff's 'expectation' or 'performance' loss, consisting of what would have been received had the contract been duly performed.[30] It is, however, important to consider the precise scope of the duty undertaken. Thus, it has been held that a surveyor's contractual duty to value property is a duty to take reasonable care to provide information on which the other party would decide whether to lend money on mortgage; the performance expected is different and narrower than where the duty undertaken is to advise the potential lender as to whether to make the loan.[31] A person giving negligent advice in breach of a contractual duty to advise will, subject to the rules of remoteness considered below, be responsible for all the loss which is a consequence of the advice being taken. A person who negligently provides incorrect information is only responsible for the consequences of the information being wrong.

[29] *Robinson* v. *Harman* (1848) 1 Exch. 850, at p. 855.

[30] See Fuller and Perdue (1936–7) 46 Yale L.J. 52, 573; Taylor (1982) 45 M.L.R. 139; Burrows (1983) 99 L.Q.R. 217; Friedmann (1995) 111 L.Q.R. 628; Coote [1997] C.L.J. 537. Cf. Atiyah (1978) 94 L.Q.R. 193.

[31] *South Australia Asset Management Co.* v. *York Montague Ltd.* [1997] A.C. 191, *per* Lord Hoffmann at p. 214 (valuers not liable for loss attributable to collapse of property market).

Assessment by reference to contract terms

Damages must be assessed by reference to the terms of the contract sued upon, and the Court cannot take account of 'the expectations, however reasonable, of one contractor that the other will do something that it has assumed no legal obligation to do'.[32] Thus, an employee who is wrongfully dismissed and sues the employer for breach of contract will be unable to recover contractual damages for the loss of 'fringe benefits' from the employment unless the employer has assumed a contractual obligation to provide those benefits.[33] Also, where the defendant has a choice of two methods of performance, damages will be assessed on the basis of the minimum legal obligation, i.e. that the contract would have been performed by the method least onerous to the defendant and least beneficial to the plaintiff.[34]

Diminution in value or 'cost of cure'

In many cases the assessment of the plaintiff's loss of bargain will be the difference in value between the performance received and that promised in the contract; 'diminution in value'.[35] However, in appropriate circumstances, damages may either be assessed on the basis of what it has cost or will cost the plaintiff to have the contract performed by a third party; the 'cost of cure',[36] or another basis which reflects the loss truly suffered by the plaintiff. These alternatives may be more appropriate where the plaintiff's purpose in contracting is non-monetary. For instance, a contract for small building works on a house may be made to make it 'more comfortable, more convenient, and more conformable' to the owner's particular tastes,[37] or to ensure privacy.[38] These factors may not affect the value of the property to be benefited or may, as where the work consists of redecorating, to the owner's execrable taste, a house in good decorative order,[39] reduce it. In such cases the value of the promise to the promisee differs from the financial effect on its position which full performance will ensure. Where the value of the performance to the promisee exceeds the financial enhancement of the promisee's position, the value beyond the market price has been called the 'consumer surplus'.[40]

If work contracted for is not performed or is performed badly, the plaintiff is entitled to the cost of substitute or remedial work to be carried out by a third party where it is possible to do so,[41] unless, in all the circumstances, this is unreasonable,

[32] *Lavarack* v. *Woods of Colchester Ltd.* [1967] 1 Q.B. 278, at p. 294. [33] *Ibid.*

[34] *Re Thornett & Fehr and Yuills Ltd.* [1921] 1 K.B. 219; *Abraham* v. *Herbert Reiach Ltd.* [1922] 1 K.B. 477; *Bunge Cpn.* v. *Tradax Export S.A.* [1981] 1 W.L.R. 711. Cf. *Paula Lee Ltd.* v. *Robert Zehil & Co Ltd.* [1983] 2 All E.R. 390. See Hudson (1975) 91 L.Q.R. 20.

[35] See *post*, p. 577. Landlord and Tenant Act 1927, s. 18; Sale of Goods Act 1979, ss. 50(3), 51(3), 53(3).

[36] *Jones* v. *Herxheimer* [1950] 2 K.B. 106; *East Ham Cpn* v. *Bernard Sunley & Sons Ltd.* [1966] A.C. 406, at p. 434; *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at p. 329; *Radford* v. *de Froberville* [1977] 1 W.L.R. 1262, at pp. 1269–70; *Ruxley Electronics & Constructions Ltd.* v. *Forsyth* [1996] 1 A.C. 344. Where the 'cost of cure' is less than the reduction in value, the mitigation principle (*post*, p. 582) will restrict the plaintiff to the former.

[37] *Ruxley Electronics & Constructions Ltd.* v. *Forsyth* [1996] 1 A.C. 344, *per* Lord Mustill at pp. 360–1.

[38] *Radford* v. *de Froberville* (*supra*, n. 36) (the erection of a wall).

[39] See *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* [1979] 1 W.L.R.783, *per* Robert Goff J. at p. 803.

[40] Harris, Ogus, Phillips (1979) 95 L.Q.R. 58; Muris (1983) 12 J.L.S. 379.

[41] Cf. *Ward* v. *Cannock Chase D.C.* [1985] 3 All E.R. 537 (a tort case where cost of cure was awarded subject to planning permission) and note that where a surveyor in breach of contract fails to identify defects in the property surveyed the *prima facie* measure is the diminution in the value of the

as where the cost of cure is wholly disproportionate to any resulting benefit[42] and where it would not be reasonable for the plaintiff to have the work done, whether or not the plaintiff does so intend.[43] In such cases, unless the plaintiff's interest in performance is not wholly financial, only the diminution in value should be recovered. Thus, in *Ruxley Electronics & Constructions Ltd.* v. *Forsyth*:[44]

F contracted with R for the construction of a swimming pool in his garden with a diving area 7 feet 6 inches deep at a price of £17,797. In breach of contract the diving area was only 6 feet deep but was suitable for diving and there was no adverse effect on the market value of the pool. The estimated cost of rebuilding the pool to the specified depth was £21,560.

The House of Lords held that F was not entitled to the 'cost of cure' but as he had lost his personal preference for a deeper pool he was entitled to £2,500 for loss of amenity. It is submitted that this is best regarded as compensation, albeit imprecise, for F's loss of his performance and of non-monetary 'consumer surplus'.[45] In cases where there was never any question of being able to 'cure' the breach, for example where a carrier provided a low grade delivery service rather than the 'enhanced' service that was promised and paid for, it should, in principle, also be possible to put a figure to any non-monetary loss suffered.[46]

(b) The Reliance Measure

The reliance measure

An alternative basis for the assessment of damages is that the plaintiff should recover its 'reliance loss', that is to say, expenses which it has incurred in preparing to perform or in part performance of the contract and which have been rendered futile by the breach. Even expenses incurred prior to, and in anticipation of, the making of the contract are recoverable, provided it was reasonably in the contemplation of the parties that they would be wasted if the contract was broken. Thus

property not the cost of repairing it: *Phillips* v. *Ward* [1956] 1 W.L.R. 491; *Watts* v. *Morrow* [1991] 1 W.L.R. 1421.

[42] *Ruxley Electronics & Constructions Ltd.* v. *Forsyth* [1996] 1 A.C. 344, at pp. 354, 361; *Sealace SS Co. Ltd.* v. *Oceanvoice Ltd.* [1991] 1 Lloyd's Rep. 120; *Channel Island Ferries Ltd.* v. *Cenargo Navigation Ltd.* [1994] 2 Lloyd's Rep. 160, at p. 167 (plaintiff's interest wholly financial). In principle 'benefit' should include non-monetary benefits such as bathroom tiles matching an existing colour scheme.

[43] *Ruxley Electronics & Constructions Ltd.* v. *Forsyth* (*supra*, n. 42), *per* Lord Jauncey and Lord Lloyd at pp. 354, 359, 372–3. See also *Watts* v. *Morrow* [1991] 1 W.L.R. 1421; *Taylor* v. *Hepworths Ltd* [1977] 1 W.L.R. 659 (tort); *De Cesare* v. *Deluxe Motors Pty. Ltd.* (1996) 67 S.A.L.R. 28, at pp. 33–5 (Australia). Cf. *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at p. 317; *Radford* v. *de Froberville*, (*supra*, n. 36), at p. 1248; *Dean* v. *Ainley* [1987] 1 W.L.R. 1729 (Glidewell L.J. and Sir George Waller).

[44] [1996] 1 A.C. 344, on which see Coote [1997] C.L.J. 537; O'Sullivan, ch. 1 in Rose, ed., *Failure of Contracts* (1997). See also *Harbutt's 'Plasticine' Ltd.* v. *Wayne Tank and Pump Co. Ltd.* [1970] 1 Q.B. 447, at p. 473.

[45] *Ibid.*, *per* Lord Bridge and Lord Mustill at pp. 354, 360–1. Cf. *ibid.*, *per* Lord Lloyd, at p. 374, reserving his position but regarding it as compensation for F's disappointment, on which see *ante*, p. 561.

[46] See Beale (1996) 112 L.Q.R. 205, discussing *White Arrow Express Ltd.* v. *Lamey's Distribution Ltd.* (1995) 15 Tr L.R. 69.

in *Anglia Television Ltd.* v. *Reed*,[47] the plaintiff obtained damages in respect of expenses of £2,750 which had been thrown away by reason of the defendant's refusal, in breach of contract, to play the leading part in a television play, even though the expenses had been incurred before the contract was made. A plaintiff may be compelled to claim damages for wasted expenses rather than for the loss of its bargain by reason of its inability to prove that financial benefit would have accrued to it had the contract been performed.[48]

No escape from bad bargain

If, however, the defendant can prove that the plaintiff would not have benefited financially had the contract been performed, the plaintiff will not be permitted to escape from a bad bargain by recovering as damages sums spent in reliance on the contract instead of loss of expectancy.[49] In such a case the plaintiff would only recover nominal damages because the reliance losses are considered to flow from entering into a losing contract and not from the defendant's breach.[50] A plaintiff who recovers for the loss of bargain cannot, as a general rule, combine a claim for reliance loss with one for loss of expectation so as to recover twice in respect of the same loss.[51] Thus damages for expenses rendered futile by the breach cannot be sought at the same time as damages for loss of profit, since such expenses would have had to be laid out in order to earn the profit claimed.

III. Causation

Causation

In order to establish a right to damages the plaintiff must show that the breach of contract was a cause of the loss which has been sustained in the sense that the breach of contract is the 'effective' cause of the loss, as opposed to an event which merely gives the opportunity for the plaintiff to sustain the loss.[52] Where another event has also affected the fact situation, if that other event was *likely*[53] to happen once the breach of contract had occurred it will generally not be held to break the chain of causation. In *Monarch Steamship Co. Ltd.* v. *Karlshamms Oljefabriker (A/B)*[54] a voyage was delayed by the unseaworthiness of the vessel so that it arrived in European waters after the outbreak of the Second World War and was diverted by the Admiralty to Glasgow. It was held that the outbreak of war and

[47] [1972] 1 Q.B. 60. See also *Lloyd* v. *Stanbury* [1971] 1 W.L.R. 535.

[48] *Anglia Television Ltd.* v. *Reed* (*supra*, n. 47) (inability to prove what profits from TV play would have been); *McRae* v. *Commonwealth Disposals Commission* (1950) 84 C.L.R. 377 (value of ship to be salvaged too speculative; price paid and cost of salvage expedition recovered).

[49] *C. & P. Haulage* v. *Middleton* [1983] 1 W.L.R. 1461; *CCC (London) Films Ltd* v. *Impact Quadrant Films Ltd.* [1985] Q.B. 16.

[50] Cf. *post*, p. 604 (restitutionary remedies can 'save' a plaintiff from a bad bargain).

[51] See *Cullinane* v. *British 'Rema' Manufacturing Co. Ltd.* [1954] 1 Q.B. 292, *post*, p. 581.

[52] *Galoo Ltd.* v. *Bright Grahame Murray* [1994] 1 W.L.R. 1360; *Young* v. *Purdy*, [1997] P.N.L.R. 130, disapproving of the 'but for' test. But cf. *Weld-Blundell* v. *Stephens* [1920] A.C. 956; *Banco de Portugal* v. *Waterlow & Sons Ltd.* [1932] A.C. 542; *Compania Naviera Maropan S/A* v. *Bowaters Lloyd Pulp & Paper Mills Ltd.* [1955] 2 Q.B. 68; *Quinn* v. *Burch Bros. (Builders) Ltd.* [1966] 2 Q.B. 370.

[53] In the sense used in the context of remoteness, *infra*.

[54] [1949] A.C. 196. On the position where the other event is the act of the plaintiff, see *post*, p. 584.

the Admiralty's action did not break the chain of causation; the cause of the plaintiff's loss was the defendant's breach of contract in failing to provide a seaworthy ship. But where that other event was *not likely* to happen once the breach of contract has occurred, the chain of causation may well be held to have been broken. Thus, a breach of contract by a solicitor in wrongfully ceasing to act for a client gave rise to the opportunity for the client to sustain loss by acting without alternative legal advice and lodging a defective application, but was not the cause of such loss.[55]

IV. Remoteness of Damages

Remoteness of damage

WHERE the test of causation is satisfied the law does not, however, compel the defendant to assume liability for all the loss which the plaintiff may have suffered as a consequence of the breach. Certain losses may nevertheless be too 'remote', and for these the plaintiff is not entitled to compensation.

(a) The Basic Rule

The basic two-branched rule

The foundation of the law on this subject is contained in the judgment of Alderson B. in the Court of Exchequer in the case of *Hadley* v. *Baxendale*:[56] What has become known as 'the rule in *Hadley* v. *Baxendale*', lays down that where the parties have made a contract which one of them has broken damages are recoverable: (1) when they are 'such as may fairly and reasonably be considered arising naturally, i.e., according to the usual course of things' from the breach, or (2) when they are 'such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract', provided that in both cases, they are the probable result of the breach.[57]

The effect of the rule was explained by Alderson B. as follows:[58]

> [I]f the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been

[55] *Young* v. *Purdy* [1997] P.N.L.R. 130; *Galoo Ltd.* v. *Bright Grahame Murray* [1994] 1 W.L.R. 1360. See also *South Australia Asset Management Co.* v. *York Montague Ltd.* [1997] A.C. 191, *per* Lord Hoffmann at p. 212–13. Cf. *ibid.* [1995] Q.B. 375, *per* Bingham M.R. at pp. 406, 420–1.

[56] (1854) 9 Exch. 341, at p. 354.

[57] The final words govern both branches: *Koufos* v. *Czarnikow Ltd.* [1969] 1 A.C. 350.

[58] (1854) 9 Exch. 341, at pp. 354, 355.

known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them.

From this it will be seen that liability under the second branch of the rule will depend upon the special circumstances made known to the party in default at the time the contract was made. In the case in which these principles were formulated:

The plaintiffs' mill was stopped by the breakage of a crankshaft, and it was necessary to send the crankshaft to the makers as a pattern for a new one. The defendants, who were carriers, undertook to deliver the shaft to the makers, but the only information given to them was 'that the article to be carried was the broken shaft of a mill, and that the plaintiffs were the millers of the mill'.[59] By some neglect on their part the delivery of the shaft was delayed, and in consequence the mill could not be restarted until some time after it could otherwise have been. The plaintiffs lost profits which they would otherwise have made.

The question was whether this loss of profits ought to be taken into account in estimating the damages. Applying the principles quoted above, the Court pointed out that the circumstances communicated to the defendants did not show that a delay in the delivery of the shaft would entail loss of profits of the mill; the plaintiffs might have had another shaft, or there might have been some other defect in the machinery to cause the stoppage. Accordingly they could not recover for this loss because the Court stated[60] that:

[I]n the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred; and these special circumstances were here never communicated by the plaintiffs to the defendants.

The rule was further considered in *Victoria Laundry (Windsor) Ltd.* v. *Newman Industries Ltd.*:[61]

The plaintiff, a launderer and dyer, wished to expand its business, and for this purpose entered into a contract with the defendant to purchase from it a new boiler. It was agreed that the boiler was to be delivered on 5 June, but when the plaintiff sent to collect the boiler on that day it was informed that it had been damaged by a fall and was not ready. The boiler was not, in fact, delivered until November. In consequence of this delay, the plaintiff lost the profits which it would have earned during this period, and, in particular, certain highly lucrative dyeing contracts which it could have obtained with the Ministry of Supply. The plaintiff sued *inter alia* to recover these losses.

Streatfield J. held that the plaintiff was not entitled to include in its measure of damages the loss of any business profits during the period of delay. His decision was reversed. Asquith L.J., delivering the judgment of the Court of Appeal,

[59] *Ibid.*, *per* Alderson B. at p. 355. It was stated by Asquith L.J. in *Victoria Laundry (Windsor) Ltd.* v. *Newman Industries Ltd.* [1949] 2 K.B. 528, at p. 537, that the headnote is misleading in that it wrongly ascribes to the defendants knowledge that the mill was stopped for want of the shaft.

[60] (1854) 9 Exch. 341, *per* Alderson B. at p. 356.

[61] [1949] 2 K.B. 528.

pointed out that the defendant knew before, and at the time of the contract, that the plaintiff was a launderer and dyer and required the boiler for immediate use in its business. From the defendant's own technical experience, and from the business relations existing between the parties, the defendant must be presumed to have anticipated that some loss of profits would occur by reason of its delay. But in the absence of special knowledge on its part, the defendant could not reasonably foresee the additional losses suffered by the plaintiff's inability to accept the highly lucrative dyeing contracts. The case was therefore to be referred to an Official Referee who would decide as to what loss might reasonably be considered to be normal in the circumstances.

Relation of the two branches of the rule

Although there are two branches to the rule in *Hadley* v. *Baxendale*, in essence they both form a part of a single general principle.[62] An attempt to elucidate their relationship was made by Asquith L.J. in *Victoria Laundry (Windsor) Ltd.* v. *Newman Industries Ltd.*[63] The general principle which governs both branches of the rule is that the aggrieved party is only entitled to recover such part of the loss actually resulting from the breach as was at the time of the contract reasonably foreseeable as liable to result from the breach. What was at that time reasonably so foreseeable depends on the knowledge then possessed by the parties or, at all events, by the party who later commits the breach. For this purpose, knowledge 'possessed' is of two kinds: one imputed, the other actual. Everyone, as a reasonable person, is taken to know the 'ordinary course of things' and consequently what loss is liable to result from a breach of contract in that ordinary course. This is the subject-matter of the first branch of the rule. But to this knowledge, which a contract-breaker is assumed to possess whether it is actually possessed or not, there may have to be added in a particular case knowledge which the plaintiff actually possesses, of special circumstances outside the 'ordinary course of things', of such a kind that a breach in those special circumstances would be liable to cause more loss.[64] Such a situation attracts the operation of the second branch of the rule and makes this additional loss recoverable. Under neither branch is it necessary that the contract-breaker should actually have asked what loss is liable to result from a breach. It suffices that, if the issue had been considered, the contract-breaker would as a reasonable person have concluded that the loss in question was liable to result.

This exposition has been described as 'a justifiable and valuable clarification of the principles which *Hadley* v. *Baxendale* was intending to express'.[65] Nevertheless, there has been some criticism of the way in which Asquith L.J. formulated the general principle in terms of 'reasonable foresight' of the loss 'liable to result'. This, it is said, may engender confusion with the rule regarding remoteness of damage in tort,[66] where a defendant will be held responsible for damage

[62] *Koufos* v. *C. Czarnikow Ltd.* [1969] 1 A.C. 350, at pp. 385, 415.

[63] [1949] 2 K.B. 528, at p. 539.

[64] Knowledge of special circumstances may, however, in some situations be such as to lead the parties to believe that the loss will be reduced: see *Biggin & Co. Ltd.* v. *Permanite Ltd.* [1951] 1 K.B. 422, at p. 436; *Koufos* v. *C. Czarnikow Ltd.* (*supra*, n. 62), at p. 416.

[65] *Koufos* v. *C. Czarnikow Ltd.* (*supra*, n. 62), at p. 417. See also p. 399, but contrast pp. 389, 390.

[66] *Overseas Tankship (U.K.)* v. *Morts Dock and Engineering Co. (The Wagon Mound)* [1961] A.C. 388.

which is reasonably foreseeable as liable to happen even if the risk is very small,[67] because it is said that in tort, unlike in contract, there is often no opportunity for the injured party to protect itself against an unusual risk by informing the defendant.[68] In *Koufos* v. *C. Czarnikow Ltd.*[69] Lord Reid and Lord Morris interpreted the phrase used by Alderson B.—'in the contemplation of the parties'—as meaning the contemplation of a result which was 'not unlikely' to happen;[70] and a majority of their Lordships distinguished the tort rule by requiring that the loss must be 'not very unusual and easily foreseeable',[71] or that there must be 'a real danger' or 'a serious possibility'[72] of its occurrence.

(b) Physical Damage and Economic Loss

Physical damage and economic lo

The interrelation of the tests for remoteness of damage in contract and tort was further considered by the Court of Appeal in *Parsons (H.) (Livestock) Ltd.* v. *Uttley Ingham & Co. Ltd.*[73]

The defendants agreed to supply and erect on the plaintiffs' pig farm a bulk food storage hopper for the purpose of storing pig nuts for the plaintiffs' top grade pig herd. When the hopper was installed, the defendants failed to ensure that a ventilator at the top of the hopper was open, with the result that the pig nuts stored in it became mouldy. The plaintiffs fed the mouldy nuts to their pigs believing (as would normally be the case) that no harm could result. But the pigs suffered an attack of E. *coli*, an intestinal infection triggered by feeding on the mouldy nuts, and 254 pigs died.

At first instance, Swanwick J. held that the damage caused was not within the reasonable contemplation of the parties as a result of the defendants' breach of contract. The Court of Appeal reversed that decision. Lord Denning M.R. expressed the opinion[74] that the observations of the House of Lords in *Koufos* v. *C. Czarnikow Ltd.* were limited to cases where a plaintiff was claiming for loss of profit or, at any rate, for economic loss. In his view, where the claim was for damages for personal injury or damage to property, or for resulting expenses to which the plaintiff had actually been put, the rule in contract was the same as that in tort, so that a defendant would be liable for any loss or damage which ought reasonably to have been foreseen at the time of the breach as a possible consequence, even if it was only a slight possibility. A distinction between loss of profit and physical damage might be justified on the ground that a person is unlikely to consider the possibility of physical injury in advance and thus to disclose unusual risks.[75] However, Orr and Scarman L.JJ., who held that the parties could have contemplated 'a serious possibility' that the pigs might become ill as a result of

[67] *Koufos* v. *C. Czarnikow Ltd.* (*supra*, n. 62), at pp. 385–6, 389.
[68] *Ibid.*, at pp. 385–6, 411, 422–3. But as parties to a tort claim may well be in a contractual or similar relationship this is not an adequate reason. See Burrows, (*supra*, n. 1), p. 54.
[69] [1969] A.C. 350. [70] At pp. 388, 406. [71] At p. 383.
[72] At pp. 414–15, 425. [73] [1978] Q.B. 791. [74] At pp. 803–4.
[75] Burrows, (*supra*, n. 1), p. 53. But this may not be the case for all types of contracts, e.g. a contract for medical services or for instruction in a sporting activity.

the breach, considered that neither authority[76] nor principle supported a distinction in law between loss of profit and physical damage. Nevertheless, Scarman L.J. stated[77] that although the formulation of the remoteness test is not the same in tort and contract because the relationship of the parties in a contractual situation differs from that in tort, it would be absurd if the amount of damages recoverable were to depend upon whether the plaintiff's cause of action was in contract or in tort. In his opinion the difference between 'reasonably foreseeable' (the test in tort) and 'reasonably contemplated' (the test in contract) was semantic, not substantial. While this suggests that where there is a contractual relation between the parties and concurrent liability in contract and tort there should be no difference between the remoteness tests in contract and tort, even in such situations the difference may not yet have been eliminated.[78]

(c) Type of Damage

Type of damage

In the context of physical injury it is established that the word 'damage' refers to the type of damage in question; it is not necessary for a plaintiff to go further and show contemplation of the exact nature of the damage that has arisen, or the amount of damage of the type or kind.[79] Although it has been said that the same principles apply to cases of loss of profit,[80] this is difficult to reconcile with the decision of the Court of Appeal in the *Victoria Laundry* case in which the 'ordinary' loss of profits were recovered but not that from the highly lucrative Ministry of Supply contracts.[81]

(d) Damage Arising in the Usual Course of Things

It will now be convenient to examine separately the operation of each branch of the rule, in view of the fact that each covers a different degree of knowledge pos-

[76] The authority relied on by Lord Denning, *Ashington Piggeries Ltd.* v. *Christopher Hill Ltd.* [1972] A.C. 441 and *Kendall (Henry) & Sons* v. *William Lillico & Sons Ltd.* [1969] 2 A.C. 31, in fact applied *Koufos* v. *C. Czarnikow Ltd.* (*supra*, n. 62) as, more recently, did *Kemp* v. *Intasun Holidays Ltd.* [1987] 2 F.T.L.R. 234 (asthmatic attack caused by dirty hotel room too remote).

[77] At pp. 806–7. See also *Archer* v. *Brown* [1985] Q.B. 401, at p. 418.

[78] Cf. *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145, at p. 185 (remoteness less restricted in tort than in contract) and *Banque Lambert Bruxelles S.A.* v. *Eagle Star Insurance Co. Ltd.* [1995] Q.B. 375, at p. 405 (essence of the test the same) *sub nom. South Australia Asset Management Co.* v. *York Montague Ltd.* [1997] A.C. 191, at p 211 (scope of the duty is the same). See generally Cartwright [1996] C.L.J. 488, at pp. 500–4, 514.

[79] *Koufos* v. *C. Czarnikow Ltd. (supra*, n. 62), at pp. 382, 383, 385–6, 417.

[80] *Parsons (H.) (Livestock) Ltd.* v. *Uttley Ingham & Co. Ltd.* [1978] Q.B. 791, at pp. 804, 813. See also *Wroth* v. *Tyler* [1974] Ch. 30, at pp. 60–2; *Transworld Oil Ltd.* v. *North Bay S.S. Cpn.* [1987] 2 Lloyd's Rep. 173, at p. 175 (relying on cases of physical injury); *Brown* v. *K.M.R. Services Ltd.* [1994] 4 All E.R. 385, at p. 399; *ibid.* [1995] 4 All E.R. 598 at pp. 620–1; *Homsy* v. *Murphy* (1997) 73 P. & C.R. 26, at pp. 36, 45.

[81] *Ante*, p. 569. See also *Islamic Republic of Iran S.S. Lines* v. *Ierax S.S. Co. of Panama* [1991] 1 Lloyd's Rep. 81, at pp. 85–6. Cf. *Brown* v. *K.M.R. Services Ltd.* [1995] 4 All E.R. 598. Stuart-Smith L.J. (at pp. 620–1) stated that although categorization into types is difficult in the case of financial loss, loss of ordinary business profits is different *in kind* from loss flowing from a particular contract which gives rise to very high profits, whereas underwriting losses of a far larger magnitude than any contemplated were of the same *type* as those foreseeable.

sessed by the contracting parties. The first branch of the rule in *Hadley* v. *Baxendale* deals with such damage as may fairly and reasonably be considered arising naturally, i.e., according to the usual course of things, from the breach of contract, as the probable result of the breach. It depends, as we have seen, on the knowledge which the parties are presumed to possess and the scope of the contractual duty undertaken.[82]

(i) Normal business position of parties

Normal business position

Damages will not be too remote if they flow from the normal business position of the parties, for the Court will assume that this is known to both of them. In *Monarch Steamship Co. Ltd.* v. *Karlshamns Oljefabriker (A/B)*,[83] the facts of which are summarized *supra*, as a result of the diversion of the delayed vessel to Glasgow the purchasers of the cargo of soya incurred expenses in having them forwarded to the contractual destination in Sweden.

The House of Lords held that the purchasers were entitled to recover this cost. Lord Wright pointed out that the question in all such cases must always be 'what reasonable business men must be taken to have contemplated as the natural or probable result if the contract was broken. As reasonable business men each must be taken to understand the ordinary practices and exigencies of the other's trade or business'.[84] In this case, the possibility of war must have been present in the minds of the parties, and experienced business people would know that one of the risks that would be consequent upon prolongation of the voyage at that time would be the diversion of the vessel by the order of the Admiralty. The cost of transhipment was therefore not too remote a consequence of the unseaworthiness of the ship.

(ii) Market fluctuations

Market fluctuations

The Sale of Goods Act 1979 contains statutory provisions for the assessment of damages for breach of a contract of sale which are founded on the first branch of the rule in *Hadley* v. *Baxendale*, and these are considered later in this chapter.[85] But the first branch of the rule applies where the seller fails to deliver or is late in delivering what is on the face of it obviously a profit-earning chattel, for instance, a merchant or passenger ship, or some essential part of such a ship.[86] In such cases the party injured will be entitled to recover the loss of profit which might reasonably be expected to arise if the contract were broken.[87]

[82] *South Australia Asset Management Co.* v. *York Montague Ltd.* [1997] A.C. 191, at p. 211, *ante*, p. 564.

[83] [1949] A.C. 196 (*ante*, p. 567). Cf. *Diamond* v. *Campbell-Jones* [1961] Ch. 22.

[84] At pp. 224. See also *Bulk Oil* v. *Sun International* [1984] 1 Lloyd's Rep. 531, at p. 544.

[85] *Post*, p. 577.

[86] *Victoria Laundry (Windsor) Ltd.* v. *Newman Industries Ltd.* [1949] 2 K.B. 528, *per* Asquith L.J. at p. 536. See also *Fletcher* v. *Tayleur* (1855) 17 C.B. 21; *Saint Lines* v. *Richardsons Westgarth & Co.* [1940] 2 K.B. 99.

[87] *Cory* v. *Thames Ironworks & S.S. Co.* (1868) L.R. 3 Q.B. 181 (use of hull as coal store); *Fyffes Group Ltd* v. *Reefer Express Lines Pty Ltd.* [1996] 2 Lloyd's Rep. 171, at p. 203 (sub-charter of vessel on 3-year time charter).

Carriage of goods: loss or delay in transit

In contracts for the carriage of goods, if, by default of a carrier, the goods which he has contracted to deliver are lost or delayed in transit, certain loss will ordinarily be assumed to have been suffered by the consignee as the natural and probable result of the breach. In the case of loss, the normal measure of damages is the market value of the goods at the time when they ought to have arrived, less the freight payable on safe delivery.[88] In the case of delay in delivering the goods, it is the difference between the market value of the goods on the day on which they ought to have arrived and their market value on the day on which they did arrive.[89] Thus, in *Koufos* v. *C. Czarnikow Ltd.*:[90]

The respondent, a sugar merchant, chartered the ship *Heron II* from the appellant to carry a cargo of sugar from Constanza to Basrah. The ship deviated without authority from the agreed voyage, with the result that the cargo was delayed. Owing to a fall in the market for sugar at Basrah, the respondent obtained £3,800 less for the sugar than the price obtainable when it should have been delivered.

The appellant contended that he was not liable for this sum as he had no special knowledge of the seasonal and other fluctuations of the sugar market. But the House of Lords held that a shipowner must be presumed to know that prices in a commodity market were liable to fluctuate, and judgment was given against him.

(iii) Exceptional loss not covered

Exceptional loss not covered by first branch

On the other hand, the first branch of the rule in *Hadley* v. *Baxendale* does not cover losses which are the consequence of special facts not known to the party in default at the time the agreement was made. In *Hadley* v. *Baxendale* itself, the plaintiffs were unable to recover damages arising from the fact that they had only one shaft, and in *Victoria Laundry* they were unable to recover in respect of the exceptionally lucrative Ministry of Supply contracts because information about those facts had not been conveyed to the defendants. Again in *British Columbia etc. Saw-Mill Co. Ltd.* v. *Nettleship*:[91]

A number of cases of machinery intended for the erection of a sawmill at Vancouver were shipped on the defendant's vessel. The defendant failed to deliver one of the cases, but was unaware of the fact that it contained a material part without which the sawmill could not be erected at all. The plaintiff claimed the cost of replacing the lost parts, and the loss incurred by the stoppage of its works during the time that the rest of the machinery remained useless owing to the absence of the lost parts.

It was held that the measure of damages was the cost of replacing the lost machinery at Vancouver only, and the Court said:[92]

The defendant is a carrier, and not a manufacturer of goods supplied for a particular purpose . . . He is not to be made liable for damages beyond what may fairly be presumed to have been contemplated by the parties at the time of entering into the contract. It must be something which could have been foreseen and reasonably expected, and to which he assented expressly or impliedly by entering into the contract.

[88] *Rodocanachi* v. *Milburn* (1886) 18 Q.B.D. 67, at p. 76.
[89] *Wilson* v. *Lancs. & Yorks. Ry.* (1861) 9 C.B.N.S. 632.
[90] [1969] 1 A.C. 350.
[91] (1868) L.R. 3 C.P. 499.
[92] (1868) L.R. 3 C.P. 499, *per* Bovill C.J. at p. 505.

This principle will exclude the recovery of damages in respect of loss of profit on actual or contemplated forward contracts where the carrier has no actual or imputed knowledge of these at the time of the contract. The loss of profit on such sales is too remote. An illustration is provided by *Horne* v. *Midland Railway Company*:[93]

The plaintiff being under contract to deliver military shoes in London for the French army at an unusually high price by a particular day, delivered them to the defendant to be carried, with notice of the contract only as to the date of delivery. The shoes were delayed in carriage, and were consequently rejected by the intending purchasers. The plaintiff sought to recover, in addition to the ordinary loss for delay, the difference between the price at which the shoes were actually sold and the high price at which they would have been sold if they had been punctually delivered.

It was held that this damage was not recoverable unless it could be proved that the company was informed of the exceptional loss which the plaintiff might suffer from an unpunctual delivery. Again, it has been held that a person who contracts to purchase land intending to resell it to an identified sub-purchaser at a profit will not be able to recover in respect of the loss of the sub-sale where the seller does not know of the purchaser's intention and purpose and the consequent exposure of the seller to the risk of such damage in the event of breach.[94]

(iv) Immaterial that breach not contemplated

Immaterial that breach not contemplated

It is, however, immaterial that the breach was of a type not reasonably to be anticipated, for the parties naturally contemplate performance and not breach. Thus, in *Banco de Portugal* v. *Waterlow & Sons Ltd.*:[95]

W & Co. agreed to print for the Bank of Portugal a quantity of Portuguese banknotes of a particular type. They negligently delivered to one M, the head of an international band of criminals, some 580,000 of these notes, and these were subsequently put into circulation in Portugal. Upon discovery of the fraud, the Bank issued notices withdrawing from circulation all notes of that type, and undertook to exchange them for other notes. The Bank then brought an action against W & Co. claiming as damages for breach of contract the value of the notes exchanged, and the cost of printing the genuine notes withdrawn.

It was held by a majority of the House of Lords that these losses were recoverable. The damage suffered, although the result of a breach which could scarcely be said to have been in the contemplation of the parties at the time they made the contract, was nevertheless to be considered as flowing from the business positions of the parties and arising naturally from the breach.

[93] (1873) L.R. 8 C.P. 131. Although this case was one of an exceptionally lucrative contract, the same principle applies to ordinary loss of profit: *Heskell* v. *Continental Express* [1950] 1 All E.R. 1033.
[94] *Seven Seas Properties* v. *Al Essa (No 2)* [1993] 1 W.L.R. 1083 (purchaser concealed purpose). See also *Seven Seas Properties* v. *Al Essa* [1988] 1 W.L.R. 1272, at p. 1276.
[95] [1932] A.C. 452. See *The Portuguese Bank-note Case* by Sir Cecil Kisch for an exciting account of this case.

(e) Damage in the Contemplation of the Parties

Damages reasonably supposed to be in the parties' contemplation

This deals with such damage as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.

As we have seen, the application of this second branch of the rule depends upon the knowledge which the contract-breaker possesses at the time of the contract, of special circumstances outside the 'ordinary course of things', of such a kind that a breach in those circumstances will cause more loss. It is well illustrated by *Simpson* v. *London and North Western Railway Company*:[96]

The plaintiff, a manufacturer, was in the habit of sending specimens of his goods for exhibition to agricultural shows. After exhibiting in a show at Bedford, he entrusted some of his samples to an agent of the defendant company for carriage to a show-ground at Newcastle. On the consignment note he wrote: 'Must be at Newcastle Monday certain'. Owing to a default on the part of the company, the samples arrived late for the Newcastle show. The plaintiff therefore claimed damages for his loss of profits at the show.

It was held that the company was liable. The company's agent had knowledge of the special circumstances, that the goods were to be exhibited at the Newcastle show, and so should have contemplated that a delay in delivery might result in this loss.

Circumstances disclosed so as to fairly infer exceptional loss a probable result

It is usually said that 'bare knowledge' of the special circumstances surrounding the contract is sufficient to make the contract-breaker liable.[97] But there is some authority for the view that, in addition, the contract-breaker should either expressly or impliedly have contracted to assume liability for the exceptional loss. On this view, the mere communication to a party of the existence of special circumstances is not enough: there must be something to show that the contract was made *on the terms* that the defendant was to be liable for that loss.[98]

This view cannot be supported. No doubt a casual intimation would not suffice, for the special circumstances must be disclosed in such a manner as to render it a fair inference of fact that both parties contemplated the exceptional loss as a probable result of the breach. Thus, in *Kemp* v. *Intasun Holidays Ltd.*:[99]

While booking a holiday Mrs K remarked to the travel agent that her husband was not present because he was suffering, as he sometimes did, from an asthma attack. In breach of contract Mr and Mrs K were accommodated for the first 30 hours of their holiday in a filthy and dusty room in an inferior hotel and Mr K had an asthma attack throughout the period. The trial judge awarded Mr K *inter alia* £800 for the consequences of having suffered an asthma attack due to the state of the alternative accommodation.

[96] (1876) 1 Q.B.D. 274.

[97] *Patrick* v. *Russo-British Grain Export Co. Ltd.* [1972] 2 K.B. 535, *per* Salter J. at p. 540.

[98] *British Columbia etc. Saw-Mill Co. Ltd.* v. *Nettleship* (1868) L.R. 3 C.P. 499, at p. 509; *Horne* v. *Midland Ry.* (1873) L.R. 8 C.P. 131, at p. 141. See also *Victoria Laundry (Windsor) Ltd.* v. *Newman Industries Ltd.* [1949] 2 K.B. 528, at p. 538; *Seven Seas Properties* v. *Al Essa (No 2)* [1993] 1 W.L.R. 1083, at p. 1088 (a party should not be exposed to risks of liability going beyond the first branch of *Hadley* v. *Baxendale* without the opportunity of making an informed decision whether to accept such risk and whether to negotiate some exclusion from liability).

[99] [1987] 2 F.T.L.R. 234.

It was held by the Court of Appeal that this casual remark did not suffice to give the defendant the necessary degree of knowledge of special circumstances to make the defendant responsible for the consequences of the asthma attack he had suffered. What is necessary to enlarge the area of contemplation is that the special circumstances should be brought home to the party.[100] But it is unnecessary that it should be a term of the contract that the defendant is to be liable for that loss.[101]

V. Assessment of Damages in Contracts for the Sale of Goods

Damages in sale of goods

USEFUL illustrations of the application of the principles so far discussed are provided by the manner of assessment of damages in contracts for the sale of goods. Sections 50 and 51 of the Sale of Goods Act 1979 state that the measure of damages for non-acceptance or non-delivery of the goods is 'the estimated loss directly and naturally resulting, in the ordinary course of events, from the buyer's or seller's breach of contract'; and where there is an available market for the goods in question, this is *prima facie* to be ascertained by the difference between the contract price and the market or current price at the time when the goods ought to have been accepted or delivered, as the case may be, or, if no time was fixed, then at the time of the refusal to accept or deliver. The reason for this *prima facie* 'breach-date' rule[102] is that in a case of non-delivery by the seller the buyer may go into the market and buy alternative goods at the current price and, in a case of the buyer's failure to accept goods, the seller may take his goods into the market and obtain the current price for them.[103]

(a) Non-Delivery

Non-delivery

Suppose that A Ltd. promises to sell and deliver to B Ltd. 1,000 tons of coal at £112 per ton on 8 February. A fails to carry out its contract. On 8 February the market price of coal of that quality is £120 per ton. B can recover as damages for non-delivery the difference between the contract price and the market price on that day, i.e. £8 per ton.

Uncontemplated forward or sub-sales must ordinarily be disregarded. If, for instance, in the expectation of receiving the coal, B has contracted to sell a similar quantity to C Ltd. at £117 per ton, its damages will still be £8 (and not £5)

[100] See *Heywood* v. *Wellers* [1976] 1 Q.B. 446, at p. 459, *per* Lord Denning M.R. (tort).

[101] *Koufos* v. *C. Czarnikow Ltd.* [1969] 1 A.C. 350, at p. 422.

[102] ss. 50(3) and 51(3). For examples of its displacement see *Van den Hurk* v. *R. Martens & Co. Ltd.* [1920] 1 K.B. 850 (sale of goods); *Johnson* v. *Agnew* [1980] A.C. 367, at pp. 400–1 (sale of land); *South Australia Asset Management Co.* v. *York Montague Ltd.* [1997] A.C. 191 at p. 221 (negligent overvaluation).

[103] *Barrow* v. *Arnaud* (1846) 8 Q.B. 604, at p. 609 (Tindal C.J.); *Kaines (U.K.) Ltd.* v. *Osterreichische Warrenhandelgessellschaft etc.* [1993] 2 Lloyd's Rep. 1 (in a volatile market this must be done at the first practical opportunity).

per ton, since it must go into the market in order to fulfil its contract with C.[104] And the same is probably true where the sub-sale is at a price higher than the market price at the date when delivery should be made.[105]

(b) Late Delivery

Late delivery: sub-sales

Where the seller is late in delivering the goods, the damage is the difference between the market value at the time they ought to have been delivered and the market value at the time when they actually were delivered. Difficulties have arisen where the goods have been resold for more than their market value. In *Wertheim* v. *Chicoutimi Pulp Co. Ltd.*:[106]

> The seller was late in delivering the goods. The market price of the goods at the time when they ought to have been delivered was 70*s.* per ton, and, at the time they were delivered, 42*s.* 6*d.* per ton. The measure of damages ought therefore to have been 27*s.* 6*d.* per ton, and this was the sum claimed by the buyer. But proof was adduced that he had actually sold the goods for 65*s.* per ton.

The Judicial Committee of the Privy Council held that the seller could rely on this sale to reduce the damages to 5*s.* per ton. Lord Atkinson considered that the *prima facie* market value rule was displaced where the sub-sale proves that the value of the goods to the buyer was more than their market value at the time of delivery and that to assess damages by reference to market value would allow the buyer to be 'compensated for a loss he never suffered'.[107] It does not, however, appear that the buyer was obliged to fulfil the sub-contract by delivering the specific goods received and the case has been rightly criticized for taking account of the sub-sale.[108] The buyer would have been free to resell the goods at the time they ought to have been delivered at their then market price (70*s.* per ton) and to procure other goods for the sub-contract. In a falling market a buyer is likely to do this and, on the facts of *Wertheim's* case, to sell one lot at 70*s.* per ton and to fulfil the 65*s.* per ton sub-sale by buying in at the market price of 42*s.* 6*d.* per ton. The late delivery therefore deprived the buyer in that case of the opportunity to sell at the due date, a fact that was unaffected by the sub-sale.

[104] *Williams Bros* v. *E. T. Agius Ltd.* [1914] A.C. 510.

[105] *Great Western Ry.* v. *Redmayne* (1866) L.R. 1 C.P. 329. But contrast *Hall Ltd.* v. *Pim Junr. & Co.* (1928) 139 L.T. 50 (H.L.) and *Coastal International Trading Ltd.* v. *Maroil A.G.* [1988] 1 Lloyd's Rep. 92 where it was contemplated that the buyer might re-sell the particular goods purchased.

[106] [1911] A.C. 301 approved in *Williams Bros.* v. *E.T. Agius Ltd.* [1914] A.C. 510, at p. 522. See also the reasoning in *Pagnan & Fratelli* v. *Corsiba Industrial Agropacuaria* [1970] 1 W.L.R. 1306.

[107] *Ibid.*, at pp. 307–8.

[108] *Slater* v. *Hoyle & Smith Ltd.* [1920] 2 K.B. 11, *per* Scrutton L.J., at p. 23. See also *Campbell Mostyn (Provisions) Ltd.* v. *Barnett Trading Co.* [1954] 1 Lloyd's Rep. 65. But in *Bence Graphics Ltd.* v. *Fasson U.K. Ltd.* [1997] 3 W.L.R. 205, *Slater's* case was not followed, it was stated that the earlier decision 'should be reconsidered', and Auld L.J. approved of *Wertheim's* case. For criticism of the *Bence Graphics* case, see *post*, p. 580.

(c) Non-Acceptance

Non-acceptance

The case of a buyer who fails to accept the goods is slightly more complicated. Although the normal rule, as set out in section 50(3) of the Sale of Goods Act 1979, is that the measure of damages is the difference between the contract price and the market price on the day fixed for acceptance, in modern trading conditions the retail price is frequently that recommended by the manufacturers, so that there is no difference between the contract and the market price. The question then arises whether a seller who is a dealer can recover its loss of profit on the sale. In *W.L. Thompson Ltd.* v. *Robinson (Gunmakers) Ltd.*:[109]

The defendant contracted to buy from the plaintiff a new Vanguard car. The plaintiff was a motor-car dealer and the price of the car was that fixed by the manufacturers, which it was unable to vary in any way. The defendant refused to accept the car, but the plaintiff managed to persuade its wholesale suppliers to take the car back. It nevertheless claimed from the defendant the loss of its profit on the sale.

The defendant claimed that the plaintiff was entitled to only nominal damages, there being no difference between the market price of the car and the contract price. Upjohn J. refused to accept this contention. He held that section 50(3) of the Sale of Goods Act 1979 laid down only a *prima facie* rule, and that it was displaced by proof in this case that the supply of Vanguard cars currently exceeded demand. The plaintiff therefore acted reasonably in returning the car to its suppliers, but it had sold one less Vanguard car than it would otherwise and so was entitled to claim its loss of profit on the transaction. It had therefore suffered a loss in the volume of its sales.[110] On the other hand, in *Charter* v. *Sullivan*,[111] the Court of Appeal held that a motor-car dealer could recover only nominal damages for non-acceptance of a car when the state of the motor trade was such that he could sell all the cars he could get, and he in fact sold the vehicle in question within 10 days of the failure to accept; here the breach did not result in loss of volume of sales. Jenkins L.J. went so far as to doubt whether it could be said that there was an 'available market' for the operation of the market price rule when goods could only be sold at a fixed retail price. But the Court was agreed that the dealer in this case could not be held to have made 'only one sale instead of two', since he was limited in the number of sales he could make by the fact that demand exceeded supply. The dealer had therefore suffered no loss of profit by the breach. The conclusion seems to be that loss of profit is not recoverable where demand exceeds supply, but can be recovered where supply equals or exceeds demand.[112]

[109] [1955] Ch. 177. Contrast *Lazenby Garages Ltd.* v. *Wright* [1976] 1 W.L.R. 459 (second-hand B.M.W. 'unique').

[110] On 'lost volume sellers', see Harris (1962) 60 Mich. L.Rev. 577, at pp. 600–1; (1964) 18 Stan. L. Rev. 66; Childres and Burgess (1973) 48 N.Y.U.L. Rev. 833. Cf. economists' scepticism about an *assumption* of lost volume in the case of retail sales, Goetz and Scott (1979) 31 Stan. L. Rev. 323, at p. 355; Goldberg (1984) 57 S. Cal. Rev. 283.

[111] [1957] 2 Q.B. 117.

[112] See also *Re Vic Mill Ltd.* [1913] 1 Ch. 465.

(d) Delay

Delay

A buyer who delays in accepting delivery may be liable to the seller for any loss occasioned by the delay and also for a reasonable charge for the care and custody of the goods.[113] Otherwise the measure of damages is as above.

(e) Breach of Warranty

Breach of warranty

Where goods are delivered in breach of warranty, section 53 of the Sale of Goods Act 1979 provides a *prima facie* rule that the buyer is entitled to the difference between the value of the goods at the time of delivery to the buyer and the value which they would have had if they had fulfilled the warranty.

Sub-sales: damages paid to sub-buyers

Again, in principle, uncontemplated sub-sales are treated as irrelevant.[114] However, if it was within the reasonable contemplation of the parties at the time they made the contract that the goods would probably be re-sold to sub-purchasers on the same or substantially similar terms either as they were or after manufacturing them into another product, the Court may have regard to the sub-sale. The buyer will, for example, be able to recover from the seller any damages which it has been forced to pay to those sub-purchasers together with any costs reasonably incurred in defending an action against him by them. Thus in *Hammond & Co.* v. *Bussey*:[115]

> The plaintiff (a shipping agent) contracted with the defendant (a coal merchant) for the supply of a quantity of 'steam-coal' to be used in steamships, the defendant knowing at the time of the contract that the plaintiff were buying the coal for resale as fit for this purpose. The plaintiff resold the coal, which was not fit for the purpose of steamships and they reasonably, but unsuccessfully, defended an action brought against them by their sub-purchaser.
>
> It was held that the plaintiff might recover not only the damages paid by it to its sub-purchaser, but the costs incurred in defending the action, for this damage came within the second branch of the rule in *Hadley* v. *Baxendale*, the defendant having had special knowledge of the probability of the sub-contracts.

Sub-sales: no damages paid to sub-buyers

Where, however, the buyer has not been faced with claims by the sub-purchasers, it may not be able to recover from the seller for the difference between the value of the goods delivered and the value which they would have had if they had fulfilled the warranty. Thus, in *Bence Graphics Ltd.* v. *Fasson U.K. Ltd.*:[116]

[113] Sales of Goods Act 1979 s. 37. Also under s. 48(3) of the Act, an unpaid seller has the right to sell perishable goods, or any goods after notice, and to recover from the original buyer damages for any loss occasioned by the breach.

[114] *Slater* v. *Hoyle & Smith Ltd.* [1920] 2 K.B. 11, at p. 23 (the seller did not know of the sub-sale, and the goods were described differently in the sub-sale). *Slater's* case is inconsistent with *Wertheim* v. *Chicoutimi Pulp Co. Ltd.* [1911] A.C. 301, *ante*, p. 576, and it has been put into question by *Bence Graphics Ltd.* v. *Fasson U.K. Ltd.* [1997] 3 W.L.R. 205, *post*, but see Treitel (1997) 113 L.Q.R. 188.

[115] (1887) 20 Q.B.D. 79. *Biggin & Co. Ltd.* v. *Permanite Ltd.* [1951] 2 K.B. 314. Cf. *Coastal International Trading Ltd.* v. *Marcil AG* [1988] 1 Lloyd's Rep. 92 (terms of sub-sale unusual so loss of profit irrecoverable).

[116] [1997] 3 W.L.R. 205.

The plaintiff bought vinyl film from the defendant for some £564,300, and used it to manufacture decals which it then sold to companies to be used to identify bulk containers. It was a term of the contract that the decals should have a 'guaranteed minimum five year life' but due to a latent defect the vinyl film degraded prematurely and many of the decals became illegible. There were many complaints but only one claim, for which the defendant had compensated the plaintiff. The plaintiff returned some £22,000 worth of defective decals to the defendant, and the defendant conceded that the plaintiff was entitled to be reimbursed for this. The lack of durability was found by the trial judge to render the vinyl film worthless, and he awarded the plaintiff £564,300, the difference between the value of the product had it fulfilled the warranty and its actual value. By the date of the trial, there was no possibility of further claims against the plaintiff by its customers because the limitation period for such claims had expired.

A majority of the Court of Appeal allowed an appeal by the defendant, and held that since the parties contemplated that the vinyl film would be manufactured and sold on, they contemplated that the measure of damages would be the plaintiff's liability to the ultimate users, thus displacing the *prima facie* measure of damages in section 53 of the Sale of Goods Act 1979. This greater willingness to depart from the statutory *prima facie* rule has been criticized.[117] First, it is said to treat an issue of the valuation of the plaintiff's loss as one of remoteness (i.e. whether the loss so identified can be recovered); the plaintiff had undoubtedly lost the benefit of the performance promised. Secondly, had the plaintiff's customers brought claims against it, the defendant would have undoubtedly been liable for the cost of meeting them so that the effect of the decision gave a defendant who delivered worthless goods a windfall gain, the benefit of the forbearance of the plaintiff's customers from claiming against the plaintiff. Although it might be thought that this second criticism sits uneasily with the rule, considered *infra*, that in general a plaintiff may not recover for loss that has been avoided,[118] for a compensating advantage to reduce the damages it must arise directly out of or as a consequence of the breach. But in this case it arose out of the forbearance of the plaintiff's customers.

Reliance loss and loss of profit

If, at the time of making the contract, the seller knew or may be presumed to have known that goods were to be used to produce a profit, and the breach of warranty precludes or reduces the profit likely to have been made, the buyer may recover damages for the loss of profit caused by the breach.[119] Such a buyer who brings an action for breach of warranty in respect of the quality or performance of goods sold to it cannot recover both the whole capital loss in the value of the goods (reliance loss) and also the whole of the profit (where admissible) which it would have made by its use of them (expectation loss) for this would be to allow the recovery of damages twice over. In *Cullinane* v. *British 'Rema' Manufacturing Co. Ltd.*:[120]

[117] Treitel (1997) 113 L.Q.R. 188 prefers the reasoning in *Slater* v. *Hoyle & Smith Ltd.* [1920] 2 K.B. 11, which the Court of Appeal refused to follow. But cf. *McGregor on Damages*, 16th edn. (1997), paras. 881–2.

[118] *Post*, p. 583. The position would have been different if the limitation period for claims by the plaintiff's customers had not expired, since it would have still been at risk of such a claim.

[119] *Richard Holden Ltd.* v. *Bostock & Co. Ltd.* (1902) 18 T.L.R. 317.

[120] [1954] 1 Q.B. 292. Cf. *T.C. Industrial Plant Pty. Ltd.* v. *Robert's (Queensland) Pty. Ltd.* [1964] A.L.R. 1083 (Australia).

The plaintiff purchased from the defendants a clay pulverizing plant, warranted to be capable of pulverizing clay at the rate of six tons per hour. This warranty was not fulfilled, and the plaintiff claimed as damages (a) the difference between the purchase price of the plant and its residual value, and (b) his loss of profits from the date of installation to the date of trial of the action.

The Court of Appeal held that these claims could not be cumulative but must be alternative because the profits would only have been made if the capital expenditure had been incurred. The plaintiff could claim one or other, but not both.

VI. Mitigation of Damage[121]

Mitigation of damage

A PERSON who has suffered loss from a breach of contract must take any reasonable steps that are available to mitigate the extent of the damage caused by the breach. The innocent party cannot claim to be compensated by the party in default for loss which is really due not to the breach but to its own failure to behave reasonably after the breach[122] but damages will not be reduced where the failure to mitigate the loss is due to the plaintiff's impecuniosity.[123] The underlying policy is the desirability of avoiding waste, in this context a loss which could have been avoided by reasonable action.

cting reasonably

Thus, an employee who is wrongfully dismissed must make reasonable efforts to obtain, and must accept an offer of, suitable alternative employment; a failure to do so, may mean that the employee is in certain circumstances, entitled to nominal damages only.[124] Again, where a seller wrongfully refuses to deliver goods due under a contract for the sale of goods, a buyer who fails to buy substitute goods which are available will be debarred from claiming any part of the damage which is due to the failure to do so.[125] A plaintiff may even be required to accept a reasonable offer from the defendant which would make good the loss or part of it.[126] But there is no obligation to do anything other than in the 'ordinary course of business'[127] and it is a question of fact in each case whether the plaintiff has acted as a reasonable person might have been expected to act. For example, there is no compulsion to accept goods of inferior quality[128] or to risk one's commercial

[121] Bridge (1989) 105 L.Q.R. 398; Harris, *Remedies in Contract and Tort* (1988), ch. 6.

[122] *British Westinghouse Electric Co. Ltd.* v. *Underground Electric Rys. Co. of London Ltd.* [1912] A.C. 673, at p. 689.

[123] *Clippens Oil Co. Ltd.* v. *Edinburgh & District Water Trustees* [1907] A.C. 291, 303; *Robbins of Putney Ltd.* v. *Meek* [1971] R.T.R. 345. Cf. *The Liesbosch* [1933] A.C. 449.

[124] *Beckham* v. *Drake* (1847–9) 2 H.L.C. 579; *Shindler* v. *Northern Raincoat Co. Ltd.* [1960] 1 W.L.R. 1038; *Yetton* v. *Eastwoods Froy Ltd.* [1967] 1 W.L.R. 104.

[125] *Kaines (U.K.)* v. *Osterreichische Warenhandelsgesellschaft Austrowaren Gesellschaft m.b.H.* [1993] 2 Lloyd's Rep. 1 (in volatile market buyer must act quickly); *Coastal (Bermuda) Petroleum Ltd.* v. *VTT Vulcab Petroleum (No. 2)* [1994] 2 Lloyd's Rep. 629, at p. 635.

[126] *Brace* v. *Calder* [1895] 2 Q.B. 253; *Payzu Ltd.* v. *Saunders* [1919] 2 K.B. 581; *Sotiros Shipping Inc.* v. *Sameiet Solholt* [1983] 1 Lloyd's Rep. 605. Cf. Bridge (1989) 105 L.Q.R. 398, at p. 411 ff.

[127] *Dunkirk Colliery Co.* v. *Lever* (1878) 9 Ch. D. 20, at p. 25.

[128] *Heaven & Kesterton Ltd.* v. *Et. Francois Albiac & Cie* [1956] 2 Lloyd's Rep. 316. See also *Strutt* v. *Whitnell* [1975] 1 W.L.R. 870.

reputation[129] or to embark upon complicated litigation[130] or to undergo an operation with the risk of surgical complications[131] in order to mitigate loss. In cases of wrongful dismissal, an employee is not compelled to accept re-employment if it involves lower status, if relations are irretrievably affected by the circumstances of dismissal (as where there has been a public charge of misconduct), or if it is likely to be less permanent than alternatives.[132]

'Duty' to mitigat a misnomer

It is often said that the law imposes 'a duty' on plaintiffs to mitigate their loss. But this expression is misleading. Plaintiffs are under no such duty, and are free to act as they judge to be in their best interests. However, a plaintiff who has acted unreasonably cannot hold the defendant liable for loss which has thus been suffered.[133] Again, the question of reasonableness is a question of fact. For example, it has been held reasonable to incur hire purchase charges to replace a damaged rotor,[134] legal expenses in proceedings with a third party,[135] advertising to safeguard one's commercial reputation,[136] and voluntary expenses to meet the plaintiff's commercial (but legally unenforceable) obligations to the public.[137]

Compensating advantages reduce damages

Where a person mitigates loss and obtains a compensating advantage, the advantage will be deducted from the damages provided it arose directly out of or as a consequence of the breach and the act of mitigation and is not merely an 'indirect' or collateral benefit.[138] Thus, where turbines which were less efficient than the contract specification and used more coal were replaced by turbines which resulted in an overall saving of coal over the whole period, the damages had to be reduced by the savings achieved.[139]

VII. Plaintiff's Contributory Fault[140]

No apportionment common law

As a general rule, where the plaintiff's loss has been caused partly by the defendant's breach of contract and partly by the plaintiff's own conduct the damages are not

[129] *Finlay (James) & Co. Ltd.* v. *N.V. Kwik Hoo Tong H.M.* [1929] 1 K.B. 400; *London & South of England Building Socy.* v. *Stone* [1983] 1 W.L.R. 1242.
[130] *Pilkington* v. *Wood* [1953] Ch. 770.
[131] *Selvanayagam* v. *University of West Indies* [1983] 1 W.L.R. 585.
[132] *Yetton* v. *Eastwoods Froy Ltd.* [1967] 1 W.L.R. 104. Cf. *Brace* v. *Calder* [1895] 2 Q.B. 253.
[133] *Sotiros Shipping Inc.* v. *Sameiet Solholt* (*supra*, n. 126), at p. 608.
[134] *Bacon* v. *Cooper (Metals) Ltd.* [1982] 1 All E.R. 397.
[135] *The Antaios* [1981] 2 Lloyd's Rep. 284, 299.
[136] *Holden Ltd.* v. *Bostock & Co. Ltd.* (1902) 18 T.L.R. 317.
[137] *Banco de Portugal* v. *Waterlow & Sons Ltd* [1932] A.C. 452, the facts of which are set out *ante*, p. 575.
[138] *British Westinghouse Co.* v. *Underground Electric Rys Co. of London* [1912] A.C. 673. See also *Gardner* v. *Marsh & Parsons* [1997] 1 W.L.R. 489. Cf. *Lavarack* v. *Woods of Colchester* [1967] 1 Q.B. 278; *Hussey* v. *Eels* [1990] 2 Q.B. 227; *Famosa S.S. Co. Ltd.* v. *Armada Bulk Carriers Ltd.* [1994] 1 Lloyd's Rep. 633, at p. 637.
[139] *British Westinghouse Co.* v. *Underground Electric Rys. Co. of London* (*supra*, n. 138).
[140] See generally Law Commission No. 219, *Contributory Negligence as a Defence in Contract* (1993).

reduced unless the plaintiff's conduct breaks the chain of causation[141] or itself amounts to a breach of contract.[142]

Law Reform (Contributory Negligence) Act 1945

Where, however, the defendant is liable in contract for failure to use reasonable skill and care and this liability co-exists with liability in the tort of negligence, as may be the case where services are rendered to a client by professionals such as lawyers, builders, or carriers, the Law Reform (Contributory Negligence) Act 1945 empowers the court to reduce the damages for breach of contract by a proportion commensurate with the plaintiff's blameworthiness.[143] The Act does not apply to breaches of a strict contractual duty[144] or of a duty of care imposed by the contract which does not also give rise to liability in tort.[145] While this position is not entirely logical, particularly in respect of breaches of contractual obligations to exercise reasonable care where the defendant's liability exists solely in contract, it has been argued that permitting apportionment in contract cases would allow courts to vary an agreed allocation of risks. It has also been said that existing contract doctrines, in particular implied terms obliging plaintiffs to take care for their own interests, mitigation, and causation, recognize and give effect to the principle that account should be taken of the fact that it is the plaintiff who is part author of the loss suffered. Those who take this view, while recognizing that these doctrines operate in an 'all or nothing' manner either allowing full recovery or no recovery, believe that apportionment would unduly undermine the certainty which is important in the English law of contract. The Law Commission accepted that this would be so in the case of a breach of a strict contractual duty but recommended that apportionment should be available in cases where the defendant is in breach of a purely contractual obligation to exercise reasonable care.[146]

[141] *Quinn* v. *Burch Bros. (Builders) Ltd.* [1966] 2 Q.B. 370; *Lambert* v. *Lewis* [1982] A.C. 225; *Schering Agrochemicals Ltd.* v. *Reisbel N.V. S.A.* (1992, C.A.), noted by Burrows (1993) 109 L.Q.R. 175; *Beoco Ltd.* v. *Alfa Laval Co. Ltd.* [1995] Q.B. 137; *County Ltd.* v. *Girozentrale Securities* [1996] 3 All E.R. 834.

[142] *Tennant Radiant Heat Ltd.* v. *Warrington Development Corp.* [1988] 1 E.G.L.R. 41; *Harper* v. *Ashton's Circus Pty Ltd.* [1972] 2 N.S.W.L.R. 395.

[143] *Sayers* v. *Harlow U.D.C.* [1958] 1 W.L.R. 623; *Forsikringsaktieselskapet Vesta* v. *Butcher* [1989] A.C. 852; *Gran Gelato* v. *Richcliff (Group)* [1992] Ch. 560. See also *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145, at p. 185. It is not settled whether the 1945 Act applies where the plaintiff has a right of action in tort which is not co-extensive with the one it has in contract: cf. *Vacwell Engineering Co. Ltd.* v. *B.D.H. Chemicals Ltd.* [1971] 1 Q.B. 88 and *Bank of Nova Scotia* v. *Hellenic Mutual War Risks Association (Bermuda) Ltd.* [1988] 1 Lloyd's Rep. 514, at p. 555; [1990] 1 Q.B. 818, rev'd on other grounds [1992] 1 A.C. 233, at p. 266. The Law Commission concluded that the Act does not apply: Law Com. No. 219 (1993) § 3.29.

[144] *Schering Agrochemicals Ltd.* v. *Reisbel N.V. S.A.* (1992, C.A.), noted by Burrows (1993) 109 L.Q.R. 175; *Barclays Bank plc* v. *Fairclough Building Ltd.* [1995] Q.B. 214.

[145] *Forsikringsaktieselskapet Vesta* v. *Butcher* [1989] A.C. 852, at p. 866, aff'd. at p. 880. Cf. *Rowe* v. *Turner Hopkins & Partners* [1982] 1 N.Z.L.R. 178, at p. 181; *Clark Boyce* v. *Mouat* [1992] 2 N.Z.L.R. 559, at p. 564, rev'd. on other grounds [1994] 1 A.C. 428.

[146] Law Com. No. 219 (1993) Parts III and IV.

VIII. The Tax Element in Damages

The tax element in damages

SINCE damages are designed to compensate the plaintiff for the actual loss suffered and no more, any liability to pay tax may have to be taken into account. In *British Transport Commission* v. *Gourley*,[147] where a claim was made for loss of earnings arising out of personal injuries caused by negligence, the House of Lords held that damages awarded to the plaintiff on the basis of his gross earnings before deduction of income tax and surtax (£37,720) should be reduced by the amount which he would have had to pay in tax. The plaintiff was therefore left with a *net* sum of £6,695. This principle has subsequently been applied to contractual claims arising out of the wrongful dismissal of an employee[148] although it has not so far been applied to the assessment of damages in commercial cases or cases of breach of contract generally.[149] Before it can be applied, however, two conditions must be satisfied: first, the earnings or profits in respect of which the claim is made must be subject to tax; secondly, the sum awarded as damages must not be subject to tax in the plaintiff's hands.

The first requirement means that the principle in *Gourley's* case does not apply to a claim in respect of the loss of a capital asset, for this would not have been subject to income tax.[150] The second excludes from its operation most claims for loss of profit, for sums awarded as damages for loss of profit are normally subject to tax in the plaintiff's hands as part of the profits of his business.[151] The case itself has been the subject of considerable criticism, since it is said that the Courts treat damages for loss of earnings arising out of personal injuries as taxable income, whereas the legislature exempts them, in part, from tax as being compensation for the loss of what may be called 'natural capital equipment'.[152] Nevertheless, the Law Reform Committee in 1958[153] recommended no change in the law, although it considered that the practical implications of the case should be kept under review.

[147] [1956] A.C. 185.

[148] *Beach* v. *Reed Corrugated Cases Ltd.* [1956] 1 W.L.R. 807; *Re Houghton Main Colliery Co. Ltd.* [1959] 1 W.L.R. 1219; *Phipps* v. *Orthodox Unit Trusts Ltd.* [1958] 1 Q.B. 314. But under the Income and Corporation Taxes Act 1988, ss. 148 and 188(4) as amended, damages for wrongful dismissal are made taxable in the plaintiff's hands, save that tax is not chargeable on the first £30,000 of such payment and, on the excess over £30,000, relief is given by way of a regressive reduction on the taxpayer's marginal rate. It has been held that the rule in *Gourley's* case nevertheless continues to apply to the exempted amount: *Parsons* v. *B.N.M. Laboratories Ltd.* [1964] 1 Q.B. 95; *Bold* v. *Brough, Nicholson & Hall Ltd.* [1964] 1 W.L.R. 201; *Lyndale Fashion Manufacturers* v. *Rich* [1973] 1 W.L.R. 73; *Stewart* v. *Glentaggart Ltd.* 1963 S.L.T. 119; *Shove* v. *Downs Surgical plc* [1984] I.C.R. 582; *Denny* v. *Gooda Walker Ltd.* 1995 S.L.T. 439.

[149] Cf. *West Suffolk County Council* v. *W. Rought Ltd.* [1957] A.C. 403.

[150] *Hull & Co. Ltd.* v. *Pearlberg* [1956] 1 W.L.R. 244. Capital gains tax is to be disregarded.

[151] *Diamond* v. *Campbell-Jones* [1961] Ch. 22; *Dickman* v. *Jones Alexander* (1989) [1993] 2 F.L.R. 521.

[152] See Baxter (1956) 19 M.L.R. 373; Hall (1957) 73 L.Q.R. 212; Jolowicz [1959] C.L.J. 85; Tucker, *ibid.*, at p. 185; Bishop and Kay (1987) 103 L.Q.R. 211; Kerridge (1992) 108 L.Q.R. 433, 442–5.

[153] 7th Report, Cmd. 501.

IX. Interest

Interest

At common law a debtor who fails to pay any sum due and owing on the date fixed for payment, is under no contractual obligation to pay interest in the absence of an express stipulation in the contract to that effect or unless such a stipulation can be implied from a previous course of dealing between the parties,[154] or from trade usage.[155] But since 1934 the Courts have been empowered to award interest on debts and damages by statute.[156] The statutory provisions enable the High Court or a county court to include in any sum for which judgment is given simple (but not compound) interest at such rate as the Court thinks fit or as rules of court may provide, on all or part of any part of the debt or damages for which judgment is given for all or any part of the period between the date when the cause of action arose and the date of the judgment. Further, if the debtor pays the debt after the institution of proceedings but before judgment, the Court has a similar power to award interest in respect of the period between the date when the cause of action arose and the date of payment.

Interest not generally available as damages for late payment

There is, however, no general statutory power to award interest on a debt which is paid late but before proceedings to recover it were brought. Although in the case of commercial debts this may change,[156a] the *common law* position is still of importance. The basic rule laid down reluctantly by the House of Lords in 1893 and recently, equally reluctantly, confirmed is that, at common law, interest cannot be awarded as damages for the late payment of money.[157] Given the compensatory aims of damages for breach of contract the general rule cannot be justified in principle.[158] In one respect, however, the common law rule has been relaxed. If by reason of the late payment the creditor has actually incurred interest charges in obtaining finance from an alternative source, the amount so paid may be recoverable as special damages, provided that it was in the reasonable contemplation of the parties at the time the contract was made that such charges would be incurred.[159]

Where the relationship between the creditor and the debtor is not purely contractual but also gives rise to equitable duties, for example where the parties are in a fiduciary relationship, interest, including not only simple interest but also compound interest, may be recoverable in certain circumstances in the absence of any agreement or custom to that effect.[160]

[154] *Re Marquis of Angelsey* [1901] 2 Ch. 548. [155] e.g., as in the case of bank deposits.
[156] Law Reform (Miscellaneous Provisions) Act 1934, s.3. See now the Supreme Court Act 1981, s. 35A and the County Courts Act 1959, s. 97A.
[156a] Late Payment of Commercial Debts (Interest) Bill 1997.
[157] *London, Chatham and Dover Railway Co.* v. *South Eastern Railway Co.* [1893] A.C. 429; *President of India* v. *La Pintada Co. Nav.* [1985] A.C. 104.
[158] *President of India* v. *La Pintada Co. Nav.* [1985] A.C. 104, 111, 112, 129–31; Law Commission No. 88, *Report on Interest* (1978); Mann (1985) 101 L.Q.R. 30. On the case for compound interest, see *Westdeutsche Landesbank Girozentrale* v. *Islington L.B.C.* [1996] A.C. 669, *per* Lord Goff and Lord Woolf (*dissente*) at pp. 695–6, 719–21, and 735–6.
[159] *The Lips* [1988] A.C. 395; *Wadsworth* v. *Lydall* [1981] 1 WLR 598.
[160] *Wallersteiner* v. *Moir (No. 2)* [1975] Q.B. 373, at p. 388; *Re Fox, Walker & Co.* (1880) 15 Ch. D. 400 (surety); *Mathew* v. *T.M. Sutton Ltd.* [1994] 1 W.L.R.1453 (pawnbroker). For a wider view of the equitable jurisdiction, see *Westdeutsche Landesbank Girozentrale* v. *Islington L.B.C.* (*supra*, n. 158)

X. Agreed Damages Clauses

(a) Liquidated Damages and Penalties

Liquidated damages and penalties

The parties to a contract not infrequently make provision in the contract for the damages to be paid on a breach of contract. Such provision does not exclude the application of the rule that damages for breach are intended to compensate for the actual loss sustained by the plaintiff, and it is a question of the proper construction of the contract to decide whether a sum fixed in this way, however the parties may have described it, is a 'penalty', in which case it cannot be recovered, or a genuine attempt to 'liquidate', that is to say, to reduce to certainty, prospective damages of an uncertain amount, in which case the sum will be recoverable.

The rule against penalties originates in equity which would relieve against penalties, cutting them down to the actual damage suffered, but was taken up and applied by the common law, and reinforced by statute.[161] The Court will accept as liquidated damages the sum fixed by the parties if it is a genuine pre-estimate of the damage which seems likely to be caused if the breach provided for should occur. The question is one of construction, to be decided upon the terms and inherent circumstances of each particular contract, judged as at the time of making the contract, not as at the time of breach.[162] Or, again, if, although it is not an estimate of the probable damage, the parties had fixed that sum because they were agreed in limiting the damages recoverable to an amount less than that which a breach would probably cause, it will similarly be accepted by the Court.[163] On the other hand, if the sum was fixed *in terrorem*, the provision will be considered to be a penalty. It will be unenforceable.

In construing the terms 'penalty' and 'liquidated damages' when inserted in a contract, the Courts will not be bound by the phraseology used, but will look to the substance rather than to the form. The parties may call the sum specified 'liquidated damages' if they wish, but if the Court finds it to be a penalty, it will be treated as such. Conversely, if the parties had described the sum fixed as a 'penalty', but it turns out to be a genuine pre-estimate of the loss, it will be treated as liquidated damages.[164]

per Lord Goff and Lord Woolf (dissenting) at pp. 695–6, 719–21, 735–6. Cf. the majority, *ibid.*, at pp. 717, 718–19, 737–41.

[161] 8 & 9 Will. III, c. 11 (an Act for the better preventing frivolous and vexatious Suits), s. 8. For history, see *Wall* v. *Rederiaktiebolaget Luggude* [1915] 3 K.B. 66, at pp. 72–3; Simpson (1966) 82 L.Q.R. 392.

[162] *Dunlop Pneumatic Tyre Co. Ltd.* v. *New Garage and Motor Co. Ltd.* [1915] A.C. 79; *Phillips Hong Kong Ltd.* v. *Att.-Gen of Hong Kong* (1993) 61 Build. L.R. 41 (P.C.).

[163] *Cellulose Acetate Silk Co. Ltd.* v. *Widnes Foundry (1925) Ltd.* [1933] A.C. 20, for facts see *post*, p. 591.

[164] *Ibid.* See also *Union Eagle Ltd.* v. *Golden Achievement Ltd.* [1997] 2 W.L.R. 341.

(b) Rules of Construction

Rules of construction

The leading case on penalties is that of *Dunlop Pneumatic Tyre Co. Ltd.* v. *New Garage and Motor Co. Ltd.*:[165]

The appellant sold motor tyre-covers, tyres, and tubes to the respondent which contracted not to resell them, or offer them for sale, at a price below the appellant's list prices and to pay the sum of £5 by way of liquidated damages for every breach of this agreement. The respondent sold a tyre-cover at less than the list price, and was sued by the appellant for damages for breach.

The House of Lords held that the sum fixed by the parties was a genuine pre-estimate of the damage which might ensue and not a penalty. In the course of his speech Lord Dunedin laid down the following rules:[166]

(i) 'It will be held to be a penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.'

An illustration was provided by the Earl of Halsbury in an earlier case, where he said:[167]

For instance, if you agreed to build a house in a year, and agreed that if you did not build the house for £50, you were to pay a million of money as penalty, the extravagance of that would be at once apparent.

We shall see that there is considerable doubt as to how far this principle extends to the forfeiture of a sum already paid.[168] But in other situations the question is one of fact in each particular case. The purpose of such clauses is to promote certainty and, especially in commercial contracts, where the parties are able to protect themselves, the Court is likely to take the view that what the parties have agreed should normally be upheld and to take care not to set too stringent a standard which could defeat that purpose.[169] In the case of consumer contracts for the supply of goods or services, the common law rule has been embodied in a legislative presumption that a term requiring a consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation is unfair and not binding.[170]

(ii) 'It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid.'

[165] [1915] A.C. 79. [166] At p. 87.

[167] *Clydebank Engineering and Shipbuilding Co. Ltd.* v. *Don Jose Ramos Yzquierdo y Castaneda* [1905] A.C. 6, at p. 10.

[168] *Post*, p. 609.

[169] *Phillips Hong Kong Ltd.* v. *Attorney-General of Hong Kong* (1993) 61 Build. L.R. 41 (P.C.) For the economic advantages of such clauses, including avoiding difficulties of measuring loss (on which see *ante*, p. 565) and the inability of the penalty rule accurately to identify unfairness, see Scott and Goetz (1977) 77 Col. L. Rev. 554; Rea (1984) 13 J.L.S. 147. But cf. Fenton (1975/6) 51 Ind. L.Rev. 189, at pp. 191–2.

[170] Unfair Terms in Consumer Contracts Regulations 1994 (S.I. 1994 No. 3159), reg. 4(1) and Sched. 3, para. 1(e). See generally, *ante*, pp. 196, 291.

In *Kemble* v. *Farren*:[171]

The defendant agreed to perform at the Covent Garden Theatre for four seasons at £3 6*s*. 8*d*. a night. The contract provided that if either party refused to fulfil the agreement or any part thereof, such party should pay to the other the sum of £1,000 as 'liquidated damages'. The defendant refused to perform during the second season.

It was held that the stipulation was penal. The obligation to pay £1,000 might have arisen upon a failure to pay £3 6*s*. 8*d*. and was therefore quite obviously a penalty. The most obvious example of this presumption is where a borrower of money promises to pay the lender an additional sum if the money is not repaid by a fixed day. Such 'accelerated payment' clauses are common in sales by instalments and leasing arrangements. However, a distinction is drawn between contracts which accelerate an *existing* liability to pay on default and those which create or increase the liability to pay. The penalty rules do not apply to the former.[172] The distinction is, however, open to criticism on the ground that it is commercially unrealistic to hold that a debt which can only be recovered by instalments over a period is to be equated with one which can be recovered immediately and as permitting the circumvention of this rule of construction by contractual stipulation for discount if payment is made by a given date.

But even where the penalty rules apply, the presumption may be rebutted if the increase is, in the circumstances, commercially justifiable and the dominant purpose of the provision is not to deter the borrower from breach. Thus, it has been held that a provision increasing by one per cent the interest chargeable on a loan from the time a borrower defaulted reflected the increased credit risk of having such a debtor, and was not therefore a penalty.[173]

(iii) 'There is a presumption (but no more) that it is a penalty when a single lump sum is made payable by way of compensation, on the occurrence of one or more of all of several events, some of which may occasion serious and others but trifling damage.'

An illustration is offered by *Ford Motor Co.* v. *Armstrong*:[174]

A retailer of motor-cars agreed with a manufacturer *inter alia* not to sell any one of the manufacturer's cars, or any part, below the listed price. For every breach of this agreement he was to pay £250, as 'agreed damages'.

A majority of the Court of Appeal held that this was a penalty. The defendant might have become bound to pay the sum of £250 for the breach of some term which would cause only trifling damage. Similarly in *Kemble* v. *Farren*, the same factor provided an additional reason for the Court to hold that the £1,000 was a penalty because that very large sum was to become immediately payable if 'the defendant had refused to conform to any usual regulation of the theatre, however minute or unimportant'.[175]

[171] (1829) 6 Bing. 141.
[172] *Protector Loan Co.* v. *Grice* (1880) 5 Q.B.D. 529; *O'Dea* v. *All States Leasing System Pty Ltd.* (1983) 152 C.L.R. 359; *The Angelic Star* [1988] 1 Lloyd's Rep. 122.
[173] *Lordsvale Finance plc* v. *Bank of Zambia* [1996] Q.B. 752.
[174] (1915) 31 T.L.R. 267.
[175] (1829) 6 Bing. 141, at p. 148.

A single sum, as opposed to a sum proportioned to the seriousness of the breach (for example per week for delay or per item for items sold in breach of covenant), is presumed to be penal because one tests it against the least serious breach possible. The presumption does not apply where the sum is payable for breach of a single obligation which can be broken in a number of ways, for example non-completion of a building contract.[176] Where it is difficult to estimate the loss and it is therefore uncertain that losses from one breach would be greater than those from another, a court may hold that the presumption is rebutted. It may also be rebutted where it is clear that the contractual provision has sought to average out the probable losses from all the breaches provided, however, that the disparity is not too great.[177]

On the other hand:

(iv) 'It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility.'

For example, in the *Dunlop Tyre* case itself, the stipulated sum of £5 could only, at the most, be a very rough and ready estimate of the possible damage which might be suffered if a trader undercut the manufacturer's listed price. In public works contracts, such as those for the construction of roads or tunnels, the nature of the loss may in part be non-financial and therefore be particularly difficult to evaluate, but in *Phillips Hong Kong Ltd.* v. *Attorney-General of Hong Kong* it was said that a clause using a formula based on estimates of the loss of return on the capital at a daily rate, the effect of the delay on related contracts, and increased costs, was said to be sensible.[178]

But these rules are no more than presumptions as to the intention of the parties; they may be rebutted by evidence of a contrary intention, appearing from a consideration of the contract as a whole.[179]

(c) Necessity for Breach

Necessity for breach

At common law the question whether the sum of money or other performance[180] stipulated for is a penalty or liquidated damages can only arise when the event upon which it becomes payable is a *breach of the contract between the parties.*[181] It does not arise where the obligation to pay exists on entering the contract as an advance payment or deposit,[182] or is a true alternative mode of performing the

[176] *Law* v. *Local Board of Redditch* [1892] 1 Q.B. 127.
[177] *Dunlop Pneumatic Tyre Co. Ltd.* v. *New Garage and Motor Co. Ltd.* [1915] A.C. 79, at p. 99; *English Hop Growers* v. *Dering* [1928] 2 K.B. 174.
[178] (1993) 61 Build. L.R. 41 (P.C.).
[179] *Pye* v. *British Automobile Commercial Syndicate Ltd.* [1906] 1 K.B. 425.
[180] *Jobson* v. *Johnson* [1989] 1 W.L.R. 1026 (transfer of shares).
[181] *Export Credits Guarantee Department* v. *Universal Oil Products Co.* [1983] 1 W.L.R. 399 (H.L.) See also *Nutting* v. *Baldwin* [1995] 1 W.L.R. 201. The law on penalties does not apply to claims in debt: see *post*, p. 593.
[182] See *post*, p. 609.

contract.[183] The distinction has given rise to litigation in the context of hire-purchase agreements. Finance companies sometimes provide that, in the event of termination of the agreement, not only shall they be entitled to take possession of the goods hired and to forfeit instalments already paid, but that the hirer shall also pay a certain sum as compensation for 'loss of profit on the transaction'. If the hiring is terminated as a result of a breach of the agreement by the hirer, the Courts may hold this payment to be a penalty *in terrorem*.[184] But if it is terminated voluntarily by the hirer, or by his death or bankruptcy, so that there is no breach of the agreement, the question of a penalty or liquidated damages cannot arise.[185] This produces the anomaly that it may be more expensive for a hirer to behave honourably and terminate the agreement voluntarily than to repudiate and break the contract—a situation which has now been mitigated by the Consumer Credit Act 1974 in respect of credits not exceeding £15,000 to individuals[186] and by the Unfair Terms in Consumer Contracts Regulations 1994 in respect of terms in sale and supply contracts with consumers.[187] The courts have, however, been unwilling to extend the common law rule.[188]

(d) Amounts Recoverable

Amounts recoverable

Where the clause is a liquidated damages clause the plaintiff will recover the stipulated sum without being required to prove damage and irrespective of any actual damage, even where this is demonstrably smaller than the stipulated sum.[189] However, where the actual loss is greater, the plaintiff is limited to the stipulated sum. In *Cellulose Acetate Silk Co. Ltd.* v. *Widnes Foundry Ltd.* (1925):

> The appellant agreed to pay 'by way of penalty the sum of £20 per week for every week we exceed 18 weeks' in the delivery of certain machinery. Calculated on this basis, the damages recoverable by the respondent on breach amounted to some £600, but its actual loss amounted to £5,850. It therefore claimed that it was entitled to disregard the penalty and to sue for the damages actually suffered.

It was, however, clear from the circumstances that the parties must have known that the damage which would be incurred might greatly exceed the stipulated sum. The House of Lords therefore held that the sum was not a penalty, but was

[183] *Alder* v. *Moore* [1961] 2 Q.B. 57. See also *Golden Bay Realty* v. *Orchard Investment* [1991] 1 W.L.R. 981 (penalty rules not applicable to contract in statutory form).
[184] *Bridge* v. *Campbell Discount Co. Ltd.* [1962] A.C. 600; *Cooden Engineering Co. Ltd.* v. *Stanford* [1953] 1 Q.B. 86; *Financings Ltd.* v. *Baldock* [1963] 1 Q.B. 887; *Lombard North Central plc.* v. *Butterworth* [1987] Q.B. 527.
[185] *Bridge* v. *Campbell Discount Co. Ltd.* (*supra*, n. 184), at pp. 613, 614, 625; cf. Lord Denning at p. 631; *Goulston Discount Co.* v. *Harman* (1962) 106 S.J. 369 (C.A.). See also *Alder* v. *Moore* [1961] 2 Q.B. 57; *Richco* v. *A.C. Toepfer* [1991] 1 Lloyd's Rep. 136.
[186] Consumer Credit Act 1974, ss. 99, 100. See also Hire-Purchase Act 1965, ss. 27, 28.
[187] S.I. 1994 No. 3159, Sched. 3, para. 1(e) (any 'failure to fulfil . . . obligation').
[188] *Else (1982) Ltd.* v. *Parkland Holdings Ltd.* [1994] 1 B.C.L.C. 130, at p. 138 *per* Evans L.J. See also *Phillips Hong Kong Ltd.* v. *Attorney-General of Hong Kong* (1993) 61 Build. L.R. 41.
[189] *Wallis* v. *Smith* (1882) 20 Ch.D. 243, 267.

merely the amount which the appellant had agreed to pay by way of compensation for delay, and that the damages must be limited to this agreed amount.[190]

Where a clause is held to be penal the damages incurred must be assessed in the usual way. In such circumstances the plaintiff might be able to recover a sum greater than the stipulated sum[191] even though it cannot be said that the clause has a penal effect in such circumstances and although this means that a plaintiff who has acted unfairly by inserting a penal clause would be treated more favourably than one whose clause is a genuine attempt to 'liquidate' prospective damages. However, this result can be seen as following from the principle that the validity of a clause is determined by reference to the time at which the contract is made.

[190] [1933] A.C. 20. See also *Diestal* v. *Stevenson* [1906] 2 K.B. 345. Cf. *AKT Reidar* v. *Arcos* [1927] 1 K.B. 352 (unliquidated damages available in respect of breaches outside ambit of clause).

[191] *Wall* v. *Rederiaktiebolaget Luggude* [1915] 3 K.B. 66; *Watts, Watts & Co.* v. *Mitsui* [1917] AC 227; *AMEV-UDC Finance Ltd.* v. *Austin* (1986) 162 C.L.R. 344 (Australia). For criticism see *Robophone Facilities* v. *Blank* [1966] 1 W.L.R. 1428, at p. 1446; Law Commission W.P. No. 61 (1975), paras. 46–8; Hudson (1974) 90 L.Q.R. 25 (1985) 101 L.Q.R. 480; Gordon (1974) 90 L.Q.R. 25.

18

Specific Remedies

UNDER certain circumstances, a contractual promise may be enforced directly. This may be by an action for the agreed sum, for instance the price it has been agreed would be paid for goods or some other performance, by an order for specific performance of the obligation, or by an injunction to restrain the breach of a negative stipulation in a contract, or to require the defendant to take positive steps to undo a breach of contract. These remedies have different historical roots, the claim for an agreed sum being a common law remedy whereas specific performance and injunctions are equitable remedies which were once exclusively administered by the Court of Chancery. At common law the breach of a contract was regarded as the breach of a purely personal obligation but equity would sometimes regard a contract as conferring a proprietary interest on the person to whom property was to be transferred, and even where this was not the case, would come to the aid of the injured party where damages would be, for that party, an inadequate redress. The specific remedies are not subject to the limits imposed on damages by, for instance, rules of remoteness and mitigation and a plaintiff may therefore prefer specific relief where these would limit the damages recoverable.

I. Actions for the Agreed Sum[1]

A liquidated claim for the precise sum

WHERE, for example, it is agreed to sell goods for a certain price, the seller may seek payment of the agreed price. The claim, a liquidated claim for the precise sum, is for the payment of a debt. The law of contract draws a clear distinction between such a claim and a claim for damages for breach of contract. The plaintiff need prove no loss where the claim is for the payment of a debt; 'the rules as to remoteness of damage and mitigation of loss are irrelevant; and unless the event on which payment is due is a breach of some other contractual obligation . . . the law on penalties does not apply to the agreed sum'.[2] However, a seller who suffers loss over and above the sum due may recover both the agreed sum and damages.[3] An action for an agreed sum will not be available until the contractual duty to pay has arisen, whether expressly or impliedly.[4] Subject to any provision in the

[1] Burrows, *Remedies for Torts and Breach of Contract*, 2nd edn. (1994), ch. 7.
[2] *Jervis* v. *Harris* [1996] Ch. 195, at p. 202.
[3] *Overstone Ltd.* v. *Shipway* [1962] 1 W.L.R. 117.
[4] *Mount* v. *Oldham Corporation* [1973] Q.B. 309 (implied term that school fees be paid in advance).

contract, in sale of goods, by section 49(1) and (2) of the Sale of Goods Act 1979 the seller is not entitled to the price unless the property in the goods has passed to the buyer or payment is due 'on a day certain irrespective of delivery'.[5] Where the goods have not been delivered, the seller's claim for the price depends on it being ready and willing to do so.[6] The contractual duty to pay and the correlative right to payment may arise on entering the contract, as in the case of the deposits required in contracts for the sale of land[7] or during the course of performance, as in the case of hire in charterparties,[8] or progress payments in building contracts.[9] By the Apportionment Act 1870, all rents, annuities (including salaries and pensions), dividends and other periodic payments in the nature of income shall be considered as accruing from day to day and are, subject to express contrary stipulation, apportionable in respect of time.[10]

Sum due in advance of performance

Where the sum due is simply an advance payment of the price and was not required as security for due performance, the right to it is conditional upon subsequent completion of the contract. Where the contract is discharged before completion, the payment ceases to be due and the innocent party is relegated to its claim for damages.[11] Where the sum due is a deposit or other sum required as security for due performance of the contract, as a general rule it remains payable where the contract has been discharged.[12] It makes no difference whether the accrued obligation is one in favour of the innocent or the guilty party although a claim by the guilty party may be off-set by the innocent party's claim for damages. Thus, an employee who repudiates a contract of employment, can nevertheless sue for wages earned before that time.[13] There is, however, a limited jurisdiction in the Courts to provide equitable relief where it would be unconscionable for the innocent party to recover the payment.[14] Similar principles, considered *infra*, apply where the payment has been made but the payer wishes to recover it.[15]

Effect of repudiatory breach before agreed sum has fallen due

The effect of a repudiatory breach by the party who will become liable to pay the agreed sum but before the agreed sum has fallen due has been considered in the context of discharge.[16] Although *White and Carter (Councils) Ltd.* v.

[5] *Stein Forbes & Co. Ltd.* v. *County Tailoring & Co. Ltd.* (1916) 86 L.J.K.B. 448 (provision for payment in cash 'against documents on arrival of steamer' means an action for the price can be brought before delivery).

[6] *Maclean* v. *Dunn & Watkins* (1828) 6 L.J. (O.S.) C.P. 184.

[7] *Howe* v. *Smith* (1884) 27 Ch. D. 87.

[8] *Leslie Shipping Co.* v. *Welstead* [1921] 3 K.B. 420.

[9] *Hyundai Heavy Industries Co. Ltd.* v. *Papadopoulos* [1980] 1 W.L.R. 1129; *Stocznia Gdanska S.A.* v. *Latvian Shipping Co.* (*infra*. n. 20) (ship-building contracts).

[10] By the Apportionment Act 1870, ss. 2, 7.

[11] *Dies* v. *British and International Mining and Finance Co. Ltd.* [1939] 1 K.B. 724, *post*, p. 607; *McDonald* v. *Dennys Lascelles* (1933) 218 C.L.R. 457, at p. 447; *Chinery* v. *Viall* (1860) 5 H. & N. 288. On the position where the payment has been made, see *post*, p. 604.

[12] *Ibid.* See also *Hinton* v. *Sparkes* (1868) L.R. 3 C.P. 161, at p. 166; *Damon Compania Naveria* v. *Hapag Lloyd* [1985] 1 W.L.R. 435, at p. 451; *Rover International Ltd.* v. *Cannon Film Sales Ltd. (No. 3)* [1989] 1 W.L.R. 912, at pp. 924–5. See further, *ante*, p. 550 (consequences of discharge).

[13] *Taylor* v. *Laird* (1856) 25 L.J. Ex. 329 (*ante*, p. 37); Apportionment Act 1870, s. 2. Cf. *Boston Deep Sea Fishing and Ice Co.* v. *Ansell* (1888) 39 Ch.D. 339. Note the difference of opinion in *Moriarty* v. *Regent's Garage & Engineering Co.* [1921] 1 K.B. 423. Cf. *ibid.*, *per* Lush J. at p. 434, and *per* McCardie J. at pp. 448–9.

[14] *Post*, p. 609.

[15] *Post*, p. 608.

[16] *Ante*, p. 535.

McGregor[17] suggests that an injured party who can perform without the co-operation of the contract-breaker has an unfettered option to hold the contract open, to perform and to recover the sum once it becomes due, this has been criticized.[18] It is said to encourage wasteful performance and to be inconsistent with the mitigation rule (which it is said should apply to actions for an agreed sum) as well as giving what amounts to indirect specific performance of contracts which are not specifically enforceable. It has not been followed in a number of other common law jurisdictions,[19] and it does not apply where the innocent party has no legitimate interest, financial or otherwise, in completing performance,[20] although this fetter on the innocent party's right to perform and create an entitlement to the agreed sum has been stated only to apply in extreme cases.[21] Supporters of an unfettered right on the part of the innocent party point to the inconsistency of a requirement of legitimate interest with the rejection in English law, affirmed by Lord Reid,[22] of a rule that contract remedies must be exercised reasonably and to the uncertainty of the concept of legitimate interest.[23] But it is submitted that these arguments neglect a number of ways in which the law of remedies limits the possibility of abuse by the innocent party of its rights[24] and the discretionary nature of the specific remedies which have their origin in equity, to which we now turn.

II. Specific Performance

Specific performance

An order for specific performance is one by which the Courts direct the defendant to perform the contract, and in accordance with its terms.[25]

[17] [1962] A.C. 413.

[18] Nienabar [1962] C.L.J. 213; Goodhart (1962) 78 L.Q.R. 263; Stoljar (1974) 9 Melb U.L.R. 355, at p. 368; Priestley (1990–91) 3 J.C.L. 218. But cf. (1962–66) 2 Adelaide L.R. 103; Tabachnik [1972] C.L.P. 149, at p. 164 ff.

[19] *Rockingham County* v. *Luten Bridge Co.* 35 F2d 301 (1929); *Restatement of Contracts* 2d, §253 (USA); *Asamera Oil Cpn.* v. *Sea Oil Cpn.* [1979] 1 S.C.R. 633 (Canada).

[20] *White and Carter (Councils) Ltd.* v. *McGregor* [1962] A.C. 413, *per* Lord Reid at p. 431. See also *Stocznia Gdanska S.A.* v. *Latvian Shipping Co* [1996] 2 Lloyd's Rep. 132 but point not considered in H.L.: [1998] 1 W.L.R. 514.

[21] *Gator Shipping Cpn.* v. *Trans-Asiatic Oil Ltd. S.A.* [1978] 2 Lloyd's Rep. 357, at p. 374 (interest may be legitimate where the court would have great difficulty in assessing the damages); *Clea Shipping Corp.* v. *Bulk Oil International Ltd. (The Alaskan Trader)* [1984] 1 All E.R. 129, at p. 137. Cf. *Attica Sea Carriers Corp.* v. *Ferrostaal Poseidon Bulk Reederei GmbH (The Puerto Buitrago)* [1976] 1 Lloyd's Rep. 250 (interest not legitimate where cost of repairing ship exceeds the value of the ship when repaired).

[22] *White and Carter (Councils) Ltd.* v. *McGregor* [1962] A.C. 413, at p. 430.

[23] Lord Hodson [1962] A.C. 413, at p. 445, stated that such a requirement would make an action in debt a discretionary remedy.

[24] Friedmann, in Beatson and Friedmann, eds., *Good Faith and Fault in Contract Law* (1995), ch. 16, lists the rules concerning penalties (*ante*, p. 587), limitation of the right to recover the cost of cure (*ante*, p. 566) and restriction of the right to recover the defendant's gain (*post*, p. 614).

[25] Since Lord Cairns' Act 1858 there has been jurisdiction to grant damages either in addition to or in substitution for specific performance or an injunction. See now the Supreme Court Act 1981, ss. 49, 50. Such damages are governed by the same principles as are damages at common law: *Johnson* v. *Agnew* [1980] A.C. 367, at p. 400 (*contra Wroth* v. *Tyler* [1974] Ch. 30); they can be awarded where

(a) Inadequacy of Damages

Inadequacy of damages

Since the jurisdiction to order specific performance was supplementary to the common law remedy of damages, it has traditionally been said that specific performance will not normally be granted where damages provide adequate relief.[26] In the modern law, however, there is no absolute rule to this effect, and the scope of specific performance is wider: it may now be ordered if that remedy will 'do more perfect and complete justice than an award of damages'.[27] This may be the case where the contract provided for a series of regular payments but damages could only be sought as each payment fell due,[28] or where the loss is suffered by a person who is not a party to the contract.[29] Nevertheless, in exercising its discretion whether or not to order specific performance, the Court will be disposed to refuse the remedy if, in the particular case before it, damages will fully compensate and will put the plaintiff in as beneficial a position as if the contract had been specifically performed.[30] It is submitted that although Courts are taking a more flexible and liberal approach to the availability of specific performance, two factors indicate that it should remain a secondary remedy to damages. First, specific performance, unlike damages, does not take account of the desirability of a plaintiff taking reasonable steps to mitigate its loss and granting it avoids the policy of the mitigation rule. Secondly, there have been many improvements in the techniques for identifying and quantifying loss recoverable by damages.[31]

Sale of goods

Where personal property is concerned, damages can usually be adjusted so as to compensate for (let us say) a failure to supply goods. Section 52 of the Sale of Goods Act 1979 provides that, in any action for breach of contract to deliver specific or ascertained goods, the Court may, if it thinks fit, direct that the contract shall be performed specifically, without giving the defendant the option of retaining the goods on payment of damages. The Court of Chancery was accustomed to decree specific performance only where the goods sold were of unique value to the buyer or possessed special beauty, rarity, or interest.[32] The power conferred by the Sale of Goods Act will similarly not be exercised where the chattel is 'an ordinary article of commerce' such as a piano or even a set of Hepplewhite chairs, as

an order for specific performance has been made and not complied with (*Biggin* v. *Minton* [1977] 1 W.L.R. 701; *Johnson* v. *Agnew* (*supra*).

[26] *Harnett* v. *Yielding* (1805) 2 Sch. & Lef. 549, at p. 553; *Ryan* v. *Mutual Tontine Westminster Chambers Association* [1893] 1 Ch. 116, at p. 126.

[27] *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, *per* Megarry V.-C. at p. 322. See also *Beswick* v. *Beswick* [1968] A.C. 58, at pp. 77, 83, 88; *The Stena Nautica (No. 2)* [1982] 2 Lloyd's Rep. 336, at pp. 346–7.

[28] *Beswick* v. *Beswick* [1968] A.C. 58.

[29] *Beswick* v. *Beswick* [1968] A.C. 58, *ante*, p. 409. But not always, see *Co-operative Insurance Society Ltd.* v. *Argyll Stores (Holdings) Ltd.* [1997] 2 W.L.R. 898, at p. 909 (H.L.), *post*, p. 600, wrongful closure of 'anchor' supermarket in shopping centre caused losses to other tenants.

[30] *South African Territories Ltd.* v. *Wallington* [1898] A.C. 309; *Beswick* v. *Beswick* [1968] A.C. 58, at pp. 88, 90–1, 102.

[31] Burrows, *Remedies for Torts and Breach of Contract*, 2nd edn. (1994), pp. 350–3.

[32] *Holroyd* v. *Marshall* (1862) 10 H.L. Cas. 191, at p. 209; *Falcke* v. *Gray* (1859) 4 Drew. 651, at p. 658.

substitute goods can be obtained and damages are normally a sufficient remedy.[33] Even in the case of generic goods, such as petrol or steel, however, a contract falling outside section 52 of the Sale of Goods Act 1979 may be specifically enforced where scarcity of supplies means that substitutes are not available.[34]

Sale of land

On the other hand, as a general rule, either party to a contract for the sale of land is entitled to sue for specific performance of the agreement. Traditionally it is said that damages are an inadequate remedy for the breach of a contract for the sale of land; but a more convincing reason is that the purchaser acquires by the contract an equitable interest in the land sold and that the vendor is entitled to a reciprocal remedy. The power of the Court to grant specific performance is not limited to those situations in which at law damages would be recoverable. Thus, specific performance may be ordered in respect of an anticipatory breach of contract in circumstances where the plaintiff, having elected to affirm the agreement, would have no immediate right of action for damages.[35]

(b) Discretionary Remedy

Discretionary remedy

Specific performance is a discretionary remedy. It does not follow that specific performance will necessarily be granted because damages are not an adequate compensation. The Court has a choice in the matter, and, although this does not mean that the choice will be exercised in an arbitrary or capricious manner, the Court can consider whether it would be fair to grant the remedy[36] and refuse it in circumstances which would not justify a refusal of the common law remedy of damages. 'He who comes to Equity must come with clean hands.' Thus the Court can take into account the fact that the plaintiff's conduct has been tricky or unfair,[37] or that the plaintiff has tried to take advantage of a mistake on the part of the defendant.[38] It can also take account of the conduct of the defendant,[39] and it can refuse specific performance if, to grant it, great hardship would be caused to the defendant.[40] So, where the potential loss to the defendant was 'enormous, unquantifiable and unlimited, as well as being out of all proportion to any uncompensatable loss' suffered by the plaintiff, specific performance will not be granted.[41] The defendant's bad conduct may also induce the Court to grant the

[33] *Whiteley Ltd.* v. *Hilt* [1918] 2 K.B. 808, at p. 819; *Cohen* v. *Roche* [1927] 1 K.B. 169. Cf. *The Oro Chief* [1983] 2 Lloyd's Rep. 509 (ship); *Record* v. *Bell* [1991] 1 W.L.R. 853, at p. 862 (furniture in house separately sold to plaintiff).

[34] *Sky Petroleum Ltd.* v. *VIP Petroleum Ltd.* [1974] 1 W.L.R. 576 (scarcity due to oil embargo); *Howard E. Perry* v. *British Railways Board* [1980] 1 W.L.R. 1375 (steel strike).

[35] *Hasham* v. *Zenab* [1960] A.C. 316; and see *ante*, p. 541.

[36] *Shell U.K. Ltd.* v. *Lostock Garages Ltd.* [1976] 1 W.L.R. 1187.

[37] *Mortlock* v. *Buller* (1804) Ves. 292; *Walters* v. *Morgan* (1861) 3 De G.F. & J. 718; *Sang Lee Investment Co.* v. *Wing Kwai Investment Co.* (1983) 127 Sol. Jo. 410.

[38] *Webster* v. *Cecil* (1861) 30 Beav. 62; *ante*, p. 324.

[39] *Sang Lee Investment Co.* v. *Wing Kwai Investment Co.* (*supra*, n. 37).

[40] *Malins* v. *Freeman* (1837) 2 Keen 25; *Denne* v. *Light* (1857) 8 De G.M. & G. 774; *Handley Page Ltd.* v. *Commissioners of Customs and Excise* [1970] 2 Lloyd's Rep. 459; *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at p. 326. But cf. *Mountford* v. *Scott* [1975] Ch. 258; *Howard E. Perry & Co.* v. *British Railways Board* [1980] 1 W.L.R. 1375.

[41] *Co-operative Insurance Society Ltd.* v. *Argyll Stores (Holdings) Ltd.* [1996] 3 W.L.R. 27, *per* Millett L.J., at p. 43. Cf. Lord Hoffmann's formulation: [1997] 2 W.L.R. 898, at p. 909.

remedy where there has been a gross breach of personal faith or an attempt to use the threat of non-performance as blackmail.[42] But where the parties' interests are purely financial, acting 'with gross commercial cynicism' will not suffice.[43] These considerations are, of course, generally considered to be irrelevant at common law.[44]

(c) Want of Mutuality

Want of mutuality

In considering whether or not to entertain a claim for specific performance, the Court will take into account whether 'mutuality' exists between the parties. If one party were compelled to perform its obligations in accordance with the terms of the contract while the obligations of the other party under the contract, or some of them, remained unperformed, it might be unfair that the former party should be left to its remedy in damages if the latter party failed to perform any of its unperformed obligations.[45] At one time it was supposed that the Court would not grant specific performance to one party unless, at the time the contract was entered into, it could not have been enforced against that party by the other.[46] But this supposed rule was subject to a number of exceptions[47] and has since been exploded.[48] Lack of mutuality is now only relevant if, at the date of the hearing, the plaintiff has not performed its obligations under the contract and could not be compelled for some reason to perform its unperformed obligations specifically.[49] Even where mutuality in this sense does not exist, the Court may possibly, in the exercise of its discretion, order specific performance if damages would be an adequate remedy to the defendant for any default on the plaintiff's part.[50]

(d) Contracts of Personal Service

Contracts of personal service

The Court will not, in general, compel the performance of contracts which involve personal service.[51] In the case of contracts of employment, this principle is now embodied in legislation which provides that an employee shall not be compelled to perform a contract of employment.[52] The basis of the Courts' approach seems to be that to make one person serve or employ another against the will of the other would be improper and could 'turn contracts of service into contracts of

[42] *Co-operative Insurance Society Ltd.* v. *Argyll Stores (Holdings) Ltd.* [1997] 2 W.L.R. 898, *per* Lord Hoffmann., at p. 909.

[43] *Ibid.*

[44] But see Friedmann, in Beatson and Friedmann, eds., *Good Faith and Fault in Contract Law* (1995), ch. 16, and *ante*, pp. 587 (the rules concerning penalties), 566 (limitation of the right to recover the cost of cure), and *post*, p. 614 (restriction of the right to recover the defendant's gain).

[45] *Price* v. *Strange* [1978] Ch. 337, at p. 361.

[46] Fry, *Specific Performance*, 6th edn., p. 219.

[47] Ames, *Lectures on Legal History* (1913), p. 370.

[48] *Price* v. *Strange* [1978] Ch. 337.

[49] *Ibid.*; *Sutton* v. *Sutton* [1984] Ch. 184.

[50] *Ibid.*, at p. 368.

[51] *Rigby* v. *Connol* (1880) 14 Ch. D. 482, at p. 487; *Scott* v. *Rayment* (1868) L.R. 7 Eq. 112 (partnership).

[52] Trade Union and Labour Relations (Consolidation) Act 1992, s. 236. Cf. *Stevenson* v. *United Road Transport Union* [1977] I.C.R. 893.

slavery'.[53] But this is difficult to reconcile with the less personal nature of modern employment, and the fact that, by declaration, a public official[54] and a university lecturer[55] may in effect be reinstated. Certain statutes now enable a tribunal to make an order for re-engagement or reinstatement of an employee.[56] Furthermore, in exceptional circumstances, an injunction may be granted to restrain an employer from dismissing an employee and this may indirectly amount to specific enforcement of the contract of employment.[57]

(e) Unsuitability

Ill-defined

The obligations in an agreement which it is sought to enforce may be so ill-defined, or what has to be done in order to comply with the order of the Court may not be capable of sufficient definition, that specific performance would in the circumstances be an unsuitable remedy. Thus a covenant to 'lay out £1,000 in building'[58] and a contract to construct 'a railway station' with nothing to indicate the nature, materials, style, dimensions, or anything else[59] have been held not to be specifically enforceable.

Constant supervision by the Court

At one time it was said that an order for specific performance would not be granted if the court would be required constantly to supervise the execution of the contract. Thus, in *Ryan* v. *Mutual Tontine Westminster Chambers Association*[60] the Court held that it could not grant specific performance of a covenant to maintain a resident porter in constant attendance at a block of flats for the benefit of the tenants as it was a contract which would require such supervision as the Court was not prepared to undertake. However, the impossibility for the Court to supervise the doing of the work has more recently been rejected as a ground for denying relief[61] and in *Posner* v. *Scott-Lewis*[62] a covenant to employ a resident porter was specifically enforced. In the case of contracts which involve continuing or complex obligations, difficulties may arise in formulating with sufficient precision (having regard to the terms of the contract) what it is that the defendant must do to comply with the order for specific performance, any breach of which is

[53] *De Francesco* v. *Barnum* (1890) 45 Ch. D. 430, at p. 438.

[54] *Ridge* v. *Baldwin* [1964] A.C. 40; *R.* v. *B.B.C., ex parte Lavelle* [1983] 1 W.L.R. 23. But cf. *Chief Constable of North Wales Police* v. *Evans* [1982] 1 W.L.R. 1155, at pp. 1175–6; *R.* v. *East Berkshire H.A., ex parte Walsh* [1985] Q.B. 152; *McLaren* v. *Home Office* [1990] I.C.R. 808. And cf. *Hill* v. *C. A. Parsons Ltd.* [1972] Ch. 305 (injunction).

[55] *Thomas* v. *University of Bradford* [1987] A.C. 795, at p. 824; *Pearce* v. *University of Aston (No. 2)* [1991] 2 All E.R. 469.

[56] Employment Rights Act 1996, ss. 114–15, 130. See also Race Relations Act 1976, s. 56.

[57] *Hill* v. *C. A. Parsons & Co. Ltd.* [1972] Ch. 305; *Irani* v. *Southampton and S.W. Hampshire Health Authority* [1985] I.C.R. 590; *Powell* v. *Brent L.B.C.* [1988] I.C.R. 176; *Robb* v. *Hammersmith and Fulham L.B.C.* [1991] I.R.L.R. 72. Cf. *Chappell* v. *Times Newspapers Ltd.* [1975] 1 W.L.R. 482. See also *post*, p. 603.

[58] *Moseley* v. *Virgin* (1796) 3 Ves. 184.

[59] *Wilson* v. *Northampton and Banbury Ry. Co.* (1874) 9 Ch. App. 279.

[60] [1893] 1 Ch. 116.

[61] *Shiloh Spinners Ltd.* v. *Harding* [1973] A.C. 691, *per* Lord Wilberforce, at p. 724. See also the statements of Megarry V.-C cited *post*, n. 64.

[62] [1987] Ch. 25. See also *Rainbow Estates* v. *Tokenhold Ltd.*, *The Times*, 12 March 1998 (repairing covenant).

punishable as a contempt of court. If those difficulties can be overcome, there is no reason why such a contract cannot be specifically enforced if damages would be an inadequate remedy.

Achieving a result and carrying on an activity

A narrower approach was, however, taken by the House of Lords in *Co-operative Insurance Society Ltd.* v. *Argyll Stores (Holdings) Ltd.*[63] Their Lordships refused to order the specific performance of an undertaking in a lease (which had 19 years to run) to keep a supermarket 'open for retail trade during the usual hours of business'. A distinction was drawn between cases in which the order would require the party to achieve a result, for instance building or repairing a house, and those in which it would require the party to carry on an activity, such as to run a business over an extended period of time. The more liberal approach was said to apply only to the first type of case[64] since, in the second type of case, there was a greater possibility of repeated applications to the Court to rule on whether the order would be breached. This puts the decision in *Posner* v. *Scott-Lewis*[65] into question. In the *Co-operative Insurance Society Ltd.* case it was also said to be contrary to the long-standing and settled practice of the Court to order a person specifically to perform a contract to run a business,[66] and that the contract in that case did not define the obligation sufficiently precisely to make it capable of specific performance because it said nothing about the level of trade, the areas of trade, or the kind of trade.[67]

In addition to these instances, the Court will also refuse specific performance where the interest to be transferred is merely transitory,[68] or where an entire obligation is specifically enforceable in part only.[69] Also contracts to appoint an arbitrator,[70] to convey the goodwill of a business without the business premises,[71] and to exercise a testamentary power of appointment[72] will not be specifically enforced.

III. Injunction

Injunction

INJUNCTIONS are either prohibitory or mandatory.[73] A prohibitory injunction may be granted to restrain the breach of a negative contract or of a negative stipu-

[63] [1997] 2 W.L.R. 898.

[64] *Ibid.*, at pp. 904–6. Lord Wilberforce's rejection of the nineteenth century authorities in *Shiloh Spinners Ltd.* v. *Harding* (*supra*, n. 61) at p. 724., was made in that context and Megarry V.-C's statements in *C. H. Giles & Co. Ltd.* v. *Morris* [1972] 1 W.L.R. 307, at p. 318 and *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at p. 321 were said to be based on incomplete analysis.

[65] See *supra*, n. 62.

[66] *Ibid.* See also *ante*, p. 597 (hardship to defendant).

[67] *Ibid.*, at p. 907.

[68] *Lavery* v. *Pursell* (1888) 39 Ch. D. 508, at p. 519 (tenancy for a year).

[69] *Ryan* v. *Mutual Tontine Westminster Chambers Association* [1893] 1 Ch. 116.

[70] *Re Smith & Service and Nelson & Sons* (1890) 25 Q.B.D. 545.

[71] *Baxter* v. *Connelly* (1820) 1 J. & W. 576. But see *Beswick* v. *Beswick* [1968] A.C. 58, at pp. 89, 97.

[72] *Re Parkin* [1892] 3 Ch. 510.

[73] On damages in lieu of an injunction, see *ante*, p. 595, n. 25 and *Jaggard* v. *Sawyer* [1995] 1 W.L.R. 269.

lation in a contract. A mandatory injunction compels the positive performance of an act and may be used to restore the situation to what it was before the breach of contract.

(a) Prohibitory Injunctions

Prohibitory injunctions

Although the grant of an injunction is normally discretionary, an injunction will normally be granted, without reference to 'the balance of convenience', to restrain the breach of a negative contract or stipulation.[74] A negative contract or stipulation is one whereby a promisor covenants not to do something, for example, not to carry on a certain trade,[75] or to build on land,[76] or not to ring church bells early in the morning.[77] A negative stipulation, though not express, may be implied, for example, in the case of an exclusive dealing agreement relating to a particular product,[78] or an agreement to charter a ship to a particular person,[79] the injunction being granted to restrain the promisor from buying (or selling) the product elsewhere or chartering the ship to another.

An injunction may be granted to restrain the breach of a negative stipulation in a contract even though the Court would not order specific performance of the positive stipulations contained in the same contract.[80] Also it may be used in a case where its effect will be to enforce performance of the contract, even though the contract is one which the Court might not normally specifically enforce. Thus in *Metropolitan Electric Supply Co. Ltd.* v. *Ginder*,[81] an express promise by the defendant to take the whole of his supply of electricity from the Company was held to import a negative promise that he would take none from elsewhere, and an injunction was accordingly granted.

Contracts of personal service

Contracts of personal service cannot, of course, be specifically enforced, but it is possible by means of an injunction to encourage performance in an oblique manner. In *Lumley* v. *Wagner*,[82] for instance:

> The defendant agreed to sing at the plaintiff's theatre, and during a certain period to sing nowhere else. Afterwards, she made a contract with another person to sing at another theatre, and refused to perform her contract with the plaintiff.

[74] *Doherty* v. *Allman* (1878) 3 App. Cas. 709, at p. 720. But the grant of an *interlocutory* injunction is not obligatory: *Texaco Ltd.* v. *Mulberry Filling Station Ltd.* [1972] 1 W.L.R. 814. Cf. *Hampstead and Suburban Properties Ltd.* v. *Diomedous* [1969] 1 Ch. 248. And see generally *American Cyanamid Co.* v. *Ethicon Ltd.* [1975] A.C. 396.

[75] *Nordenfelt* v. *Maxim Nordenfelt Guns and Ammunition Co. Ltd.* [1894] A.C. 535.

[76] *Wrotham Park Estate Co.* v. *Parkside Homes Ltd.* [1974] 1 W.L.R. 798 (in relation to building that had been undertaken before the decision, see *post*, p. 614).

[77] *Martin* v. *Nutkin* (1724) 2 Peere Wms. 266.

[78] *Catt* v. *Tourle* (1869) L.R. 4 Ch. App. 654; *Evans Marshall & Co. Ltd.* v. *Bertola S.A.* [1973] 1 W.L.R. 349.

[79] *Lord Strathcona SS Co.* v. *Dominion Coal Co.* [1926] A.C. 108 (*ante*, p. 435); *Associated Portland Cement Manufacturers Ltd.* v. *Teigland Shipping A/S* [1975] 1 Lloyd's Rep. 581.

[80] *Lumley* v. *Wagner* (1852) De G.M. & G. 604; *Sky Petroleum Ltd.* v. *VIP Petroleum Ltd.* [1974] 1 W.L.R. 576; *Hill* v. *C.A. Parsons & Co. Ltd.* [1972] Ch. 305.

[81] [1901] 2 Ch. 799.

[82] (1852) 1 De G.M. & G. 604.

The Court refused to order specific performance of her positive engagement to sing at the plaintiff's theatre, but granted an injunction to restrain the breach of her promise not to sing elsewhere.

The scope of the principle in *Lumley* v. *Wagner* has, however, been confined by two restrictions:

Implication of negative undertaking

In the first place, although in certain instances an express positive promise implies a negative undertaking not to do anything which would interfere with the performance of this promise, the Courts have normally refused in contracts of personal service to enforce by injunction anything but an express stipulation not to do some specific thing. There must have been inserted in the contract itself an express negative stipulation, and the defendant must have acted in breach of that stipulation. Thus in *Mortimer* v. *Beckett*,[83] a boxer, Joe Beckett, agreed with the plaintiff that he should have 'the sole arrangements of matching me for all my boxing contests and engagements during the period of the next seven years': afterwards he refused to be managed by the plaintiff. In terms, the contract contained no negative covenant, and so the Court held that an injunction could not be granted.

No compulsion to choose between performance and starvation

Secondly, an injunction will not be granted if its effect will be to compel the defendant to fulfil a contract for personal service or to abstain from any business whatsoever, for this would be to compel a contract-breaker to choose between specific performance and starvation. In *Ehrman* v. *Bartholomew*,[84] therefore, where a traveller promised that he would serve a firm for 10 years and would not, during that period, 'engage or employ himself in any other business', an injunction was refused, among other grounds, because to have granted it would have given him no real choice but to work for the firm. But if the employment is of a special kind, an injunction may be granted to restrain the defendant from doing similar work of that kind. So in *Warner Brothers Pictures Incorporated* v. *Nelson*:[85]

> A film actress, Mrs Nelson (professionally known as Bette Davis), agreed that she would render her exclusive services as an actress to the plaintiffs for a certain period, and would not during that period render any similar services to any other person *or engage in any other occupation*. In breach of these stipulations, she entered into an agreement to appear for another film company. The plaintiffs claimed an injunction to restrain her.

Branson J. held that, although it was impossible to grant an injunction to prevent her from engaging in any other occupation as this would amount to specific performance, an injunction should be granted to restrain her from working as an actress for any other person for a period of up to 3 years. There were other spheres of activity which, if not so remunerative, would still be open to her, so that she would not be driven, although she might be encouraged, to perform the contract.[86] This has been criticized as implying that nothing short of idleness or starvation is compulsive and it has been said that Branson J.'s view that 'an actress of her then youth and soaring talent' might employ herself usefully and remunera-

[83] [1920] 1 Ch. 571. See also *Whitwood Chemical Co.* v. *Hardman* [1891] 2 Ch. 416. Cf. *Hivac Ltd.* v. *Park Royal Scientific Instruments Ltd.* [1946] Ch. 169.

[84] [1898] 1 Ch. 671.

[85] [1937] 1 K.B. 209.

[86] At p. 217.

tively in other spheres of activity for a period of up to 3 years appeared 'extraordinarily unrealistic'.[87] More recent cases have examined the practical realities of granting an injunction and have been more willing to infer compulsion where a longer term injunction was being sought and less willing to grant an injunction where the contract contained obligations of mutual trust or confidence.[88] Where there is no question of starvation, as where the employer is willing to pay wages throughout a period of notice whether or not the employee performs the contractual duties,[89] or of the employee's skills atrophying, as where the period of notice is short,[90] the Court is more willing to grant an injunction if satisfied that breach of the negative obligation, for instance to work for a third party during the contractual period of notice, will seriously prejudice the employer.

We have noted that in exceptional circumstances, however, an injunction may be granted to restrain an employer from dismissing an employee.[91]

(b) Mandatory Injunctions

Mandatory injunctions

An injunction may also be granted to restore the situation which would have prevailed but for the defendant's breach of contract, e.g. to put back a tenant wrongfully evicted by a landlord.[92] Mandatory injunctions are always discretionary[93] and the Court will not intervene in this way unless it is shown that the defendant has deliberately ridden roughshod over the plaintiff's rights[94] or that the plaintiff would be gravely prejudiced if the remedy were withheld.[95]

[87] *Warren* v. *Mendy* [1989] 1 W.L.R. 853, *per* Nicholls L.J. at p. 865.
[88] *Ibid.*; *Page One Records Ltd.* v. *Britton* [1968] 1 W.L.R. 157 (injunction not granted to restrain breach of management contracts by boxer and pop group).
[89] *Evening Standard Ltd.* v. *Henderson* [1987] I.C.R. 588 (injunction granted; employer offered to permit employee to work through notice period). See also *Robb* v. *Hammersmith & Fulham LBC* [1991] I.R.L.R. 72.
[90] *Provident Financial Group plc* v. *Hayward* [1989] I.C.R. 160 (no injunction because no prejudice to employer).
[91] *Ante*, p. 599.
[92] *Luganda* v. *Service Hotels Ltd.* [1969] 2 Ch. 209.
[93] *Sharp* v. *Harrison* [1922] 1 Ch. 502, at p. 512; *Shepherd Homes Ltd.* v. *Sandham* [1971] Ch. 340.
[94] *Luganda* v. *Service Hotels Ltd.* (*supra*, n. 92).
[95] *Durell* v. *Pritchard* (1865) L.R. 1 Ch. App. 244, at p. 250; *Shepherd Homes Ltd.* v. *Sandham* (*supra*, n. 93); *Wrotham Park Estate Co.* v. *Parkside Homes Ltd.* [1974] 1 W.L.R. 798.

19

Restitutionary Awards

A PERSON who pays money or supplies goods or services to the defendant pursuant to a contract which is discharged by breach may be entitled to recover the money paid or to recompense in the form of a reasonable price or remuneration for the goods or services; *quantum valebat* and *quantum meruit*. These remedies may also be available in respect of money paid or services rendered under other ineffective agreements including those that are void, illegal, discharged for frustration, or too uncertain to amount to contracts. Such claims, which are strictly outside the scope of this part of the book, since they are not for breach of contract, have been briefly considered in the chapters on ineffective contracts.[1] Furthermore, in certain circumstances, the plaintiff may, by way of exception to the normal compensatory measure, be able to claim the profits the contract-breaker is alleged to have made from the breach. Wherever the innocent party has made a bad bargain,[2] where damages are limited or irrecoverable (perhaps because of the rules of remoteness or the mitigation principle), or where for some reason the innocent party finds it difficult to prove the loss suffered,[3] one of these two types of restitutionary claim may be advantageous. The first type of claim, the recovery of money paid or recompense in respect of goods or services, may also be available to a contract-breaker in certain situations.

I. The Recovery of Money Paid

(a) Recovery by the Innocent Party

Recovery of money paid

If one party is entitled to be treated as discharged from further performance of the contract by reason of the other party's breach, and does so, any money paid by that party to the other party under the contract can be recovered provided that the consideration for the payment has failed. Although the principle is not confined to contracts,[4] many of the cases are concerned with ineffective contracts.

[1] *Ante*, pp. 64, 86, 203, 388, 528. See further Goff and Jones, *The Law of Restitution*, 4th edn. (1993), chs. 17–25; Beatson, *The Use and Abuse of Unjust Enrichment* (1991), pp. 1–11; ch. 3.

[2] *B.P. Exploration Co. (Libya) Ltd.* v. *Hunt (No. 2)* [1979] 1 W.L.R. 783, at p. 800, aff'd [1983] 2 A.C. 352; *Bush* v. *Canfield* 2 Conn. 485 (1818) (Connecticut). For other advantages, see *post*, pp. 606, 612–13.

[3] *Ante*, p. 567.

[4] *Chillingworth* v. *Esche* [1924] 1 Ch. 97 (deposit paid in transaction 'subject to contract').

Strictly, the rule requires that the failure be *total*, but several factors indicate that the requirement of totality may be 'on the turn'. We shall first consider total failure, and then the recent developments.

Total failure of consideration

In *Kwei Tek Chao* v. *British Traders and Shippers Ltd.*,[5] a case concerned with a c.i.f. contract for the sale of goods, Devlin J. said:

> If goods have been properly rejected, and the price has already been paid in advance, the proper way of recovering the money back is by an action for money paid on a consideration which has wholly failed, i.e. money had and received.

As well as the requirement that the failure of consideration be total, the party seeking repayment must have elected to accept the breach as discharging the contract. If the contract has been partly performed and the innocent party who is claiming repayment has either derived some benefit under it, as where goods or services have been received, or has elected to treat the contract as still continuing,[6] the money cannot be recovered unless that benefit can be and is returned to the payee. The need for a total failure of consideration is illustrated by *Hunt* v. *Silk*:[7]

> The plaintiff paid £10 to the defendant in return for a promise by the defendant to give him immediate possession of certain premises, to put them into repair, and to execute a lease of them in his favour within 10 days. The plaintiff obtained possession, but left soon afterwards when the defendant failed to carry out the rest of his promise; he also sued to recover the £10.

His action failed. It was held that, the contract having been in part performed, no part of the consideration could be recovered.

Reason for the rule

The common law requires the failure of consideration to be total for two main reasons.[8] First, the common law has set its face against apportionment, partly because one cannot assume that all parts of the payee's performance are equally valuable and that the contract price is earned incrementally. Secondly, in many cases the benefit the payer has received from the payee's part-performance cannot easily be valued in money. This is particularly so where it consists of services.

Bargained-for benefit

Failure of consideration occurs where one party has not enjoyed the benefit of any part of what it bargained for.[9] It is judged from the payer's point of view and consideration in this context refers to performance by the payee of the contractual promise.[10] This means that any performance of the actual thing promised, as determined by the contract, is fatal to recovery. The consequence of this is that the concept of total failure of consideration is somewhat arbitrary, and can ignore real benefits received by the payer and significant detrimental reliance by the payee. For instance, in the case of a contract for the sale of goods,[11] or of hire

[5] [1954] 2 Q.B. 459, at p. 475. [6] *Ibid.* [7] (1804) 5 East 449.

[8] *Whincup* v. *Hughes* (1871) L.R 6 CP 78, at p. 81 (Bovill C.J.). Birks, *An Introduction to the Law of Restitution* (1985) pp. 242–4. For other justifications, see Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), §§ 3.8–3.10.

[9] *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.* [1943] A.C. 32; *Rover International* v. *Cannon Film Sales Ltd. (No. 3)* [1989] 1 W.L.R. 912; *Stocznia Gdanska S.A.* v. *Latvian S.S. Co.* [1998] 1 W.L.R. 574.

[10] *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbur Ltd.* [1943] A.C. 32, at p. 48.

[11] *Hudson* v. *Robinson* (1816) 4 M. & S. 475; *Rowland* v. *Divall* [1923] 2 K.B. 500.

purchase,[12] a failure by the seller to convey a good title to the goods in breach of the condition implied by section 12(1) of the Sale of Goods Act 1979[13] will constitute a total failure of consideration. Thus, in *Rowland* v. *Divall*:

> R bought a motor-car from D for £334, repainted it and sold it on to a third party. It then turned out that the car had been stolen, although D had dealt with it in good faith. The police took possession of it on behalf of the true owner and R brought an action to recover from D the £334.

The Court of Appeal held that, since R 'had not received any part of that which he had contracted to receive—namely, the property and right to possession' of the car, there had been a total failure of consideration. He was entitled to recover the whole purchase price, notwithstanding that he and his sub-purchaser had had 4 months' use and enjoyment of the vehicle and that he could not restore the car to D.[14] In an action for damages, account would be taken of the benefit received by R.[15] Similarly, there will be a total failure of consideration even though a buyer or hirer has incurred substantial reliance expenditure for the purpose of the contract[16] or where, although there has been partial performance by the payee, the Court is able to divide the contract and hold that there has been a total failure in relation to the parts not performed,[17] or can find that the parties have impliedly acknowledged that the consideration can be 'broken up' or apportioned.[18]

Partial failure of consideration

The willingness of the Court so to divide the contract may indicate dissatisfaction with the requirement of totality. We have seen that the requirement of totality can produce fine and sometimes arbitrary distinctions, and in an earlier chapter that, in the case of frustrated contracts, it has been removed by statute so that money paid can be recovered even though there has only been a partial failure of

[12] *Karflex Ltd.* v. *Poole* [1933] 2 K.B. 251; *Warman* v. *Southern Counties Car Finance Corporation Ltd.* [1949] 2 K.B. 576.

[13] *Ante*, p. 150.

[14] [1923] 2 K.B. 500, at pp. 504, 506–7. See also *Butterworth* v. *Kingsway Motors* [1954] 1 W.L.R. 1286 where the purchase price of a car (£1,275) was recovered although it had been used for nearly a year and by the time the car was returned it was worth only £800. The principle has been both criticized and defended; see Law Reform Committee, Twelfth Report, (Cmnd. 2958, 1966); Law Commissions' Report on Exemption Clauses in Contracts, (Law Com. No. 24, 1969); Law Commissions' Report on Sale and Supply of Goods (Law Com. No. 160, 1987), §§ 6.1–6.5, the last of which recommended no reform of the rule by requiring a buyer seeking to recover the price to make a money allowance in favour of the seller in respect of the use. Cf. Torts (Interference with Goods) Act 1977, s. 6(3).

[15] *Harling* v. *Eddy* [1951] 2 K.B. 739, and *ante*, p. 583. But where a buyer has spent money on the goods while they are in its possession, damages may be the preferable remedy because this can be recovered in such an action but not in an action for the return of the price: *Mason* v. *Burningham* [1949] 2 K.B. 545.

[16] *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.* [1943] A.C. 32, *ante*, p. 528 (work done by payees in manufacturing machines); *Rover International* v. *Cannon Film Sales Ltd. (No. 3)* [1989] 1 W.L.R. 912, at pp. 932, 936, 937 (expenditure in buying back films to fulfil terms of distributorship contract).

[17] *D.O. Ferguson* v. *Sohl* (1992) 62 Build. L.R. 92 (building contract; total failure of consideration in respect of sum paid in excess of value of work done); *White Arrow Express Ltd.* v. *Lamey's Distribution Ltd.* (1995) 15 Tr. L.R. 69, noted Beale (1996) 112 L.Q.R. 205; *Baltic Shipping Co.* v. *Dillon* (1993) 176 C.L.R. 344, at p. 375 (High Court of Australia).

[18] *David Securities Pty. Ltd.* v. *Commonwealth Bank of Australia* (1992) 175 C.L.R. 353, at p. 383.

consideration.[19] We shall also see that where a *quantum meruit* claim is made in respect of services rendered, the difficulty of valuing the work done is not regarded as an insurmountable bar to relief. It may, moreover, be difficult to maintain the requirement that the failure be *total* now that the principle of unjust enrichment and the defence of change of position have been recognized in English law.[20] It has been said that 'if counter-restitution is relatively simple . . ., insistance on total failure of consideration can be misleading and confusing',[21] and recently, in *Goss* v. *Chilcott*,[22] the Judicial Committee of the Privy Council relaxed the requirement that the failure be total by the use of apportionment. It was held that a loan could be apportioned between the principal sum lent and the interest, so that the receipt by the lender of interest did not prevent the lender recovering the principal sum lent, and the court indicated that it would have been willing to apportion the principal sum itself so that partial repayment of the principal sum would not have prevented a restitutionary claim, but would have merely reduced such a claim to the unpaid balance of the loan. Moreover, support has been expressed in the House of Lords for the reformulation of the total failure of consideration rule.[23] Although these cases all concerned loans or other transactions in which the part-performance received by the payer consisted of money so that the problems of valuing non-monetary performance did not arise, it is submitted that in principle restitution should be available in all cases in which it is relatively simple for the payer to return any benefits received.

(b) Recovery by the Party in Breach

Advance payments of the contract price

It is similarly possible for the party who has broken the contract to recover from the innocent party money pre-paid by it. The recoverability of such payments depends on the construction of the contract and is primarily a function of the purpose for which the payment is required. A distinction is drawn between deposits and other payments required as security for due performance on the one hand and advance payments of the price on the other. Where the payment was not a deposit or otherwise required as security for due performance and where recovery was not otherwise expressly or impliedly precluded by the terms of the agreement (e.g. by express provision that it be forfeited) it may be recoverable. Thus, in *Dies* v. *British and International Mining and Finance Corporation Ltd.*:[24]

The defendant contracted to sell rifles and ammunition to one Quintana at a total price of £270,000 of which £100,000 was paid before the agreed delivery date. Subsequently, in

[19] *Ante*, p. 529 (Law Reform (Frustrated Contracts) Act 1943, s. 1(2)).

[20] *Lipkin Gorman* v. *Karpnale Ltd.* [1991] 2 A.C. 548.

[21] *David Securities Pty. Ltd.* v. *Commonwealth Bank of Australia* (*supra*, n. 18) at p. 383 (High Court of Australia).

[22] [1996] A.C. 788, at p. 798.

[23] *Westdeutsche Landesbank Girozentrale* v. *Islington L.B.C.* [1996] A.C. 669, at pp. 682–3. See also Birks, *An Introduction to the Law of Restitution* (1985), pp. 259–64; Goff and Jones, (*supra*, n. 1), pp. 401–3, 419, but cf. Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983), §§ 3.8–3.9 and *Stocznia Gdanska S.A.* v. *Latvian S.S. Co.* (*supra* n. 9) at p. 590.

[24] [1939] 1 K.B. 724. See also *McDonald* v. *Dennys Lascelles Ltd.* (1933) 48 C.L.R. 457 (sale of land); *Rover International Ltd.* v. *Cannon Film Sales Ltd. (No. 3)* [1989] 1 W.L.R. 912; Beatson, *The Use and Abuse of Unjust Enrichment* (1991), ch. 3 (updating (1981) 97 L.Q.R. 389).

breach of contract, the purchaser failed to take delivery or to pay the balance. The defendant elected to treat the contract as discharged but refused to return the £100,000. Quintana assigned his rights to the plaintiff, who brought an action to recover the money.

Stable J. held that the plaintiff might recover it, less the amount of any damages suffered by the defendant through Quintana's breach of contract. It might seem strange, at first sight, that the party in breach should have succeeded. But as the learned Judge pointed out, the defendant was 'amply protected', since it could set off its claim for damages against the sum sought to be recovered. Again, however, in the present state of the law, the consideration for the payment must have totally failed. If the party in default has received any benefit from the subject-matter of the sale before the discharge, it cannot, subject to any equitable relief,[25] recover any part-payment made. Thus, where a contract for work and materials provides for payment of the purchase price by instalments, a contractor who is bound to incur expense as the work proceeds, will be entitled to retain any instalment paid if the other party repudiates the contract before completion of the work because, subject to a *de minimis* rule, the services rendered by the innocent party are to be regarded as part of the bargained-for performance and there is thus no total failure of consideration in such a contract once performance has commenced.[26]

Deposits and other payments as security for due performance

It is settled law that a sum paid by way of 'deposit' for the purchase of goods or land is security for completion of the contract by the buyer and cannot as a general rule be recovered if the buyer fails to perform its side of the contract.[27] Similarly, where the contract provides that on default instalments of the price already paid shall be forfeited, there will generally be no recovery.

The general rule that deposits and other payments required as security or subject to forfeiture clauses are irrecoverable is, however, subject to statutory and equitable exceptions. By section 49(2) of the Law of Property Act 1925 the Court has an unqualified discretion to order repayment of a deposit paid under a contract for the sale of land where the justice of the case requires it.[28] Another legislative exception can be found in the Unfair Terms in Consumer Contracts Regulations 1994 which provide that a term which permits the seller or supplier 'to retain sums paid by the consumer where the latter decides not to conclude or perform the contract, without providing for the consumer to receive compensation from the seller or supplier where the latter is the party cancelling the contract' is presumptively unfair.[29] Secondly, where the provision for the forfeiture of the sum paid is penal and it is unconscionable for the payee to retain the money,

[25] See *post*, p. 609.

[26] *Hyundai Heavy Industries Co. Ltd.* v. *Papadopoulos* [1980] 1 W.L.R. 1129. The case for relaxing the rule requiring that the failure of consideration be *total* is much weaker where the person seeking recovery is a contract-breaker: see *ante*, p. 484, in the context of the rule precluding recovery for part performance of an entire obligation.

[27] *Howe* v. *Smith* (1884) 27 Ch. D 89. See generally Harpum [1984] C.L.J. 134; Beatson, *The Use and Abuse of Unjust Enrichment* (1991), pp. 46–50, 76–7, 90–4.

[28] *Universal Corporation* v. *Five Ways Properties Ltd.* [1979] 1 All E.R. 552. Cf. *Macara (James) Ltd.* v. *Barclay* [1945] 1 K.B. 148 for a narrower approach to the discretion and the view that repayment could only be ordered where the vendor's conduct was open to criticism.

[29] S.I. 1994 No. 3159, Sched. 3, para. (d). See generally *ante*, pp. 196, 291.

equitable relief may be available.[30] Thus a person who purchases goods or land by instalments, or who hires goods in return for payment of rent, may be entitled to equitable relief against forfeiture of the property or purchase money if he defaults in prompt payment of the instalments or rent when due.[31] The principle is similar to that governing penalty clauses and liquidated damages clauses[32] but the law has treated the two situations as entirely separate.[33] The 'genuine pre-estimate of damage' test does not apply to stipulations for security for due performance; 'the forfeiture rule looks at the position after the breach when the innocent party is enforcing the forfeiture'.[34] The scope of the jurisdiction to relieve against forfeiture is somewhat uncertain and it probably does not apply to those commercial contracts where speed and certainty are of paramount importance.[35] Although not entirely logical, it also appears that the Courts may only relieve against the forfeiture of proprietary or possessory interests as opposed to the forfeiture of 'mere contractual rights'.[36] This may, however, leave open the possibility of seeking relief where a contract is specifically enforceable and thus creates equitable rights, although in the case of breach of an essential condition as to time relief by way of specific performance is less likely to be given than relief by way of restitution, for example by repayment of retained money.[37] Apart from the uncertainty as to the scope of the equitable jurisdiction it is also possible, though unlikely, that the only form of relief available is to give the contract-breaker more time to perform the contract so that no relief will be possible if it is clear that the contract-breaker will not be able to pay after such extension of time.[38]

[30] See *Workers Trust & Merchant Bank Ltd.* v. *Dojap Investments Ltd.* [1993] A.C. 573 (the amount of the deposit had to be reasonable, and while long usage established the reasonableness of a 10% deposit in sales of land, a larger deposit would, unless justified, be penal). Similar principles apply where the money has not been paid and an action for the agreed sum is brought; *ante*, p. 594.

[31] *Stockloser* v. *Johnson* [1954] 1 Q.B. 476; *Shiloh Spinners Ltd.* v. *Harding* [1973] A.C. 691, *per* Lord Simon at pp. 726–7. Cf. Lord Wilberforce, *ibid.*, at pp. 723–4.

[32] *Ante*, p. 587. See *Public Works Commissioners* v. *Hills* [1906] A.C. 368.

[33] *Linggi Plantations Ltd.* v. *Jagatheesan* (1972) 1 M.L.J. 89, *per* Lord Hailsham L.C at p. 91; *Workers Trust & Merchant Bank Ltd.* v. *Dojap Investments Ltd.* [1993] A.C. 573. It may sometimes be hard to say whether a contract is providing for forfeiture of money paid absolutely or for a penal liability: *Else (1982) Ltd.* v. *Parkland Holdings Ltd.* [1994] 1 B.C.L.C. 130, at p. 146.

[34] *Else (1982) Ltd.* v. *Parkland Holdings Ltd.* [1994] 1 B.C.L.C. 130, *per* Hoffmann L.J., at p. 144. His Lordship also described the penalty rule as 'mechanical', *ibid.*, p. 145. See also *ibid.*, pp. 139, 143.

[35] *The Laconia* [1977] A.C. 850; *Scandinavian Trading Tanker Co. A.B.* v. *Flota Petrolera Ecuatoriana* [1983] 2 A.C. 694; *Sport International Bussum BV* v. *Inter-Footwear Ltd.* [1984] 1 W.L.R. 776; *Union Eagle Ltd.* v. *Golden Achievement Ltd.* [1997] A.C. 514. Cf. the broader approach of the High Court of Australia: *Legione* v. *Hateley* (1983) 152 C.L.R. 406; *Stern* v. *McArthur* (1988) 165 C.L.R. 489.

[36] *BICC plc* v. *Burndy Corporation* [1985] Ch. 232, at pp. 251–2; *Nutting* v. *Baldwin* [1995] 1 W.L.R. 201; *Transag Haulage Ltd.* v. *Leyland DAF Finance plc* [1994] 2 B.C.L.C. 88, at p. 99 (contingent interest sufficient). Cf. the broader *dictum* in *Workers Trust & Merchant Bank Ltd.* v. *Dojap Investments Ltd.* [1993] A.C. 573, at p. 578.

[37] *Union Eagle Ltd.* v. *Golden Achievement Ltd.* [1997] A.C. 514; *Steedman* v. *Drinkle* [1916] 1 A.C. 275. Cf. *Re Dagenham (Thames) Dock Co., ex parte Hulse* (1873) L.R. 8 Ch. App. 1022 and the broader Australian approach: *Legione* v. *Hateley*; *Stern* v. *McArthur* (*supra*, n. 35).

[38] *Stockloser* v. *Johnson* [1954] 1 Q.B. 476, *per* Romer L.J. (cf. Denning and Somervell L.JJ.); *Galbraith* v. *Mitchenall Estates Ltd.* [1965] 2 Q.B. 473; *Starside Properties Ltd.* v. *Mustapha* [1974] 1 W.L.R. 816; *BICC plc* v. *Burndy Corporation* [1985] Ch. 232; *Workers Trust and Merchant Bank Ltd.* v. *Dojap Investments Ltd.* [1993] A.C. 573. See also *Jobson* v. *Johnson* [1989] 1 All E.R. 621.

In the exercise of the equitable jurisdiction account has been taken of whether the sum to be forfeited is much greater than the damage caused by the breach,[39] whether the party seeking relief had received a substantial part of the consideration for the payment,[40] whether there has been any fraud or sharp practice,[41] whether it is reasonable to require the party who is *prima facie* entitled to forfeiture to accept an alternative to the property it is sought to forfeit,[42] and whether relief would permit the evasion of a contractual obligation simply because the contract has turned out to be an unwise one.[43]

II. Recompense for Goods and Services

Quantum meruit

A *QUANTUM MERUIT* claim arises where goods are supplied or services rendered by one person to another in circumstances which entitle the former to be recompensed by the latter by receiving a reasonable price or remuneration.

Such a claim may arise in a number of different situations. Some of the situations are really contractual, the remedy being based on an implied promise or agreement.[44] In others, however, the law imposes a duty upon one party to recompense the other for a benefit received by the defendant or in respect of the plaintiff's reasonable reliance on the defendant's words or conduct,[45] without any promise or agreement so to do.

(a) Contractual Claims

Contractual claims

There are two main situations where a claim for a contractual *quantum meruit* may arise. First, where one person has rendered a service to another in circumstances which indicate an understanding between them that it is to be paid for, although no particular remuneration has been specified, the law will infer a promise to pay *quantum meruit*, i.e. as much as the party doing the service has deserved, or, as it is generally described, a 'reasonable' sum.[46] The principle is precisely the same when goods are bought and sold or services rendered under a contract without an express agreement as to the price, in which case the Sale of Goods Act 1979, section 8(2) and the Supply of Goods and Services Act 1982, section 15(1) provide

[39] *Stockloser* v. *Johnson* [1954] 1 Q.B. 476, at pp. 484, 490; *Transag Haulage Ltd.* v. *Leyland DAF Finance plc* [1994] 2 B.C.L.C. 88, at pp. 101–2.

[40] *Ibid.*, at pp. 484, 492.

[41] *Ibid.*, *per* Romer L.J. at pp. 495–6.

[42] *Shiloh Spinners Ltd.* v. *Harding* [1973] A.C. 691, at pp. 726–7; *Transag Haulage Ltd.* v. *Leyland DAF Finance plc* [1994] 2 B.C.L.C. 88, at pp. 101–2.

[43] *Galbraith* v. *Mitchenall Estates Ltd.* [1965] 2 Q.B. 473; *Hyundai Ship Building and Heavy Industries Co. Ltd.* v. *Pournaras* [1978] 2 Lloyd's Rep. 502, at pp. 508–9.

[44] Winfield, *The Province of the Law of Tort* (1931), p. 157; (1947) 63 L.Q.R. 35; Birks, *An Introduction to the Law of Restitution* (1985), p. 275.

[45] Goff and Jones (*supra*, n. 1), pp. 18–23, 424–8 and ch. 25; Beatson, (*supra*, n. 1), ch. 2. Cf. Birks, (*supra*, n. 44), pp. 265–76.

[46] *Paynter* v. *Williams* (1833) 1 C. & M. 810; *The 'Batis'* [1990] 1 Lloyd's Rep. 345, at p. 352.

that the buyer and the recipient of the services must pay a reasonable price or charge.

Secondly, a *quantum meruit* claim may arise when the conduct of the parties to an express contract leads to the inference that they have agreed to substitute for it a new contract. In *Steven* v. *Bromley and Son*,[47] for example, the tender and acceptance of a completely different type of cargo from that envisaged by the original contract was held to give rise to the inference that the parties had entered into a new and substituted agreement. If no quantified remuneration can be spelled out for the new contract, then the law will imply a promise to pay a reasonable sum. It must be remembered, however, that for such a contract to arise, each party must have had the option of accepting or rejecting the substituted agreement.[48] A new and different contract cannot be forced by one party on the other against its will.

The same principle is also applied where one party has, in breach of contract, only partially performed the agreement, or performed it in a manner different from that contemplated by its terms. In such a case, if the party not in default elects to accept the partial or substituted performance, that party will have to pay *quantum meruit* the value of the benefit received. So if A plc agrees to buy from B plc certain goods, and B delivers the goods it contracted to sell mixed with goods of a different description not included in the contract, or delivers a lesser quantity of the contracted goods, if A accepts those goods,[49] it must pay a reasonable price for them.[50] By its acceptance A impliedly promises to pay a reasonable sum but again, if the party not in default has no option but to accept, then it will not be liable to a *quantum meruit* or any other action.[51]

So far we have considered claims by the innocent party. Where, however, the contractual obligation is divisible or severable so that the right to payment accrues incrementally as the services are rendered, the guilty party will also be entitled to claim in respect of performance completed, but subject to a counterclaim for damages by the innocent party in respect of loss suffered by the breach.[52]

(b) Restitutionary Claims by the Innocent Party

Restitutionary claims by the innocent party

Where the claim is in restitution, the obligation is imposed on the parties by the law without reference to any promise or agreement. Where a contract has been

[47] [1919] 2 K.B. 722 (for facts see *ante*, p. 30). See also *Sir Lindsay Parkinson & Co. Ltd.* v. *Commissioners of Works* [1949] 2 K.B. 632.

[48] *Taylor* v. *Laird* (1856) 25 L.J. Ex. 329 (for facts see *ante*, p. 37); *Foreman and Co. Pty Ltd.* v. *Ship 'Liddesdale'* [1900] A.C. 190, at p. 202.

[49] It is not obliged to: Sale of Goods Act 1979, s. 30(4).

[50] *Steven* v. *Bromley and Son* (*supra*, n. 47), at p. 728 (Atkin L.J.); Sale of Goods Act 1979, s. 30(1), *ante*, p. 488.

[51] *Munro* v. *Butt* (1858) 8 E. & B. 738; *Sumpter* v. *Hedges* [1898] 1 Q.B. 673 (for facts see *ante*, p. 488); *Bookmakers Afternoon Greyhound Services Ltd.* v. *Wilfred Gilbert Staffordshire Ltd.* [1994] F.S.R. 723.

[52] *Taylor* v. *Laird* (1956) 25 L.J. Ex 328 (in respect of services rendered before throwing up his command); *Button* v. *Thompson* (1869) L.R. 4 C.P. 330. On entire and divisible obligations see *ante*, p. 485; on the action for the price, see *ante*, p. 594; on acceptance of part performance of an entire obligation, see *post*, p. 488.

broken in such a way as to entitle the innocent party to be treated as discharged, and it has elected to be so treated, it may sue on a *quantum meruit* for the value of the work done under the contract, as an alternative to bringing an action on the contract for damages. In such a case the claim to recompense arises in restitution. Two cases provide useful illustrations of this remedy. In *Planché* v. *Colburn*:[53]

The plaintiff had contracted to write a book on custom and ancient armour for a periodical publication, called the *Juvenile Library* to be published by the defendant. For this he was to receive the sum of £100 on completion. When he had completed half, but not the whole, of his volume, the defendant abandoned the publication.

The plaintiff was held entitled to retain a verdict for £50 which the jury had awarded him. Tindal C.J. said:[54]

I agree that when a special contract is in existence and open, the plaintiff cannot sue on a *quantum meruit*: part of the question here, therefore, was whether the contract did exist or not. It distinctly appeared that the work was finally abandoned; and the jury found that no new contract had been entered into. Under these circumstances, the plaintiff ought not to lose the fruit of his labour.

Again, in *De Bernardy* v. *Harding*[55]

The defendant appointed the plaintiff his agent to advertise and sell tickets for seats to view the funeral of the Duke of Wellington, the plaintiff to receive a commission on the ticket sold. The defendant wrongfully revoked the plaintiff's authority after he had already incurred certain expenses in carrying out the contract.

It was held that the plaintiff was entitled to recover *quantum meruit* for the expenses so incurred.

Comparison with damages

If the contract has not been discharged, the innocent party cannot use the *quantum meruit* remedy, but can only sue for damages. However, if the restitutionary remedy is available and the injured party chooses to sue on a *quantum meruit*, the principle of assessment differs from that which is applied in assessing damages for breach of contract and the sum which the innocent party is entitled to recover may differ from that which is recoverable as damages:[56]

Suppose that by the terms of a contract A plc is to do a certain piece of work for B plc for £10,000, payable on its completion. B repudiates the contract when A has done half of the work and A accepts that repudiation as discharging it from further performance of its obligations under the contract.

It is clear that A cannot claim the stipulated sum since the work has not been completed.[57] Should it claim damages, however, it will receive £10,000 less any saving on labour and materials. If, however, a *quantum meruit* is sought, A is asking to be paid the reasonable value of the work done. Ordinarily, damages will be the more favourable remedy since the profit element in the transaction can then be

[53] (1831) 8 Bing. 14.

[54] *Ibid.*, at p. 16.

[55] (1853) 8 Ex. Ch. 822. See also *Prickett* v. *Badger* (1856) 1 C.B.N.S. 296.

[56] *Heyman* v. *Darwins Ltd.* [1942] A.C. 356, at p. 398 (Lord Porter). See also *The Batis* [1990] 1 Lloyd's Rep. 345, at p. 353.

[57] See *ante*, p. 484 (entire contracts). Cf. *ante*, p. 535 (repudiation not accepted).

recovered. But there might be special circumstances where, for instance, the contract price had been underestimated, or the costs of doing the work had risen considerably since the contract was made. In these circumstances a plaintiff may secure a greater measure of compensation by suing on a *quantum meruit* instead of for damages. Thus it has been held that relief by way of *quantum meruit* is not limited to a pro-ration of the contract price[58] (in our example £5,000) or the contract price itself (in our example, £10,000).[59] Although this can be criticized as inconsistent with the contract and as reallocating contractual risks, pro-ration is difficult in a complex contract and may be unfair because it takes no account of fixed costs which may be incurred at the early stages of a contract or of economies of scale which may have affected the determination of the contract price but be lost on part performance. Restriction to the contract price, while more attractive[60] on pragmatic grounds, would give the contract-breaker a proportion of the profits expected under the contract even though the contract has been discharged. It would also produce disequilibrium between the position of an innocent party who has only done a small proportion of the work before the contract is discharged, where the contract price limit would rarely apply, and a person who has done the bulk of the work, where the limit would be more likely to apply. So, in the example above, if the market value of half the work is in fact £20,000, the limit would not apply, and A would recover the true value of the work, £10,000, but if A has completed three-quarters of the job, it would apply and A would only recover £10,000 as the *quantum meruit*.

(c) Restitutionary Claims by the Party in Breach

Restitutionary claims by the party in breach

We have mentioned the contractual *quantum meruit* that is available to the party in breach who has part performed a contractual obligation which is divisible or severable. Where the contractual obligations are entire the party in breach will, however, generally obtain no recompense unless the other party freely accepted the work or otherwise waived the need for complete performance. In *Sumpter* v. *Hedges*[61] the party in breach was accordingly entitled to recover the value of materials left on the building site and used by the defendant who had a choice whether or not to use them to complete the building but not in respect of the partially completed building. This rule can work harshly where substantial benefits are conferred on an innocent party who has suffered no loss whatsoever from the breach of contract.[62] In one case it was suggested that a shipowner who deviated but delivered the goods at the port of discharge without injury or substantial delay

[58] *Newton Woodhouse* v. *Trevor Toys Ltd.* (20 December 1991, C.A.) Cf. *Noyes* v. *Pugin* 27 P. 548, at p. 549 (1891) (Washington).

[59] *Lodder* v. *Slowey* (1900) 20 N.Z.L.R. 321, 358; [1904] A.C. 442; *Rover International Ltd.* v. *Cannon Films Sales Ltd. (No. 3)* [1989] 1 W.L.R. 912.

[60] See Goff and Jones, (*supra*, n. 1), pp. 426–8, citing *Wuchter* v. *Fitzgerald* 163 P. 819 (1917) (Oregon).

[61] [1898] 1 Q.B. 673 (for facts see *ante*, p. 488); *Bolton* v. *Mahadeva* [1972] 1 W.L.R. 1009.

[62] Law Com. No. 121, *Pecuniary Restitution on Breach of Contract* (1983) proposed reform but this was rejected by the Lord Chancellor; Law Com. No. 140, § 2.11 (19th Annual Report).

would be entitled to reasonable remuneration.[63] Perhaps the best explanation of this is that it was not really a case of part-performance but one in which the goods owner, in the end, got everything he had contracted for. Where, however, the innocent party has made it clear that anything other than full and precise performance is not wanted a *quantum meruit* will not be awarded.[64]

III. Restitutionary Damages[65]

Restitutionary damages

A DEFENDANT may make a gain from a breach of contract as where a financier broke his contract to invest £15,000 in the plaintiff's timber business but instead invested it in a distillery which proved much more profitable.[66] Alternatively a defendant may gain by saving expense from its breach as where remedial work, for instance replacing soil or planting trees on the plaintiff's land, is not done.[67] A restitutionary award will be attractive to a plaintiff who suffers a smaller loss than the defendant's gain as where the diminution in the value of the plaintiff's land is less than the cost of the remedial work, an expense saved by the defendant. It will also be attractive where the interest harmed by the breach of contract is a non-pecuniary interest such as confidentiality.[68] In general, the gain to a defendant from a breach of contract is irrelevant to the quantification of damages.[69]

The defendant's gain will, however, be relevant in sales of land because the effect of the contract is that the purchaser has an equitable interest in the land and is accordingly entitled to the proceeds of any wrongful sale to a third party.[70] It will also be relevant where there has been a breach of a contractual duty of confidence[71] or a fiduciary duty,[72] or where the breach of contract involves the use of or interference with the plaintiff's property.[73] These are all cases of specifically

[63] *Hain S.S. Co. Ltd.* v. *Tate and Lyle Ltd.* (1936) 41 Com. Cas. 350 (H.L.).

[64] *Wilusznynski* v. *Tower Hamlets L.B.C.* [1989] I.C.R. 493. See also *British Telecommunications plc* v. *Ticehurst* [1992] I.C.R. 383. Cf. *Miles* v. *Wakefield M.B.C.* [1987] A.C. 539. See also *ante*, p. 486.

[65] Jones (1983) 99 L.Q.R. 442; Burrows, *Remedies for Torts and Breach of Contract*, 2nd edn. (1994), pp. 308–14; Birks [1987] L.M.C.L.Q. 421; Law Commission No. 247, *Aggravated, Exemplary and Restitutionary Damages* (1998), Part III. Cf. *Co-operative Insurance Society Ltd.* v. *Argyll (Holdings) Ltd.* [1996] 3 W.L.R. 27, *per* Millett L.J. at p. 44, disapproving of this term.

[66] *Teacher* v. *Calder* (1899) 1 F. 39 (H.L.).

[67] *Tito* v. *Waddell (No. 2)* [1977] Ch. 106 (for the reasons why 'cost of cure' damages were not available, see *ante*, p. 566).

[68] *Snepp* v. *United States* 100 Sup. Ct. 763 (1980); *Attorney General* v. *Guardian Newspapers Ltd. (No. 2)* [1990] 1 A.C. 109. For other non-pecuniary interests, see *ante*, p. 562.

[69] *The Siboen* [1976] 1 Lloyd's Rep. 293, at p. 337 (profits from alternative charter irrelevant); *Tito* v. *Waddell (No. 2)* [1977] Ch. 106, at p. 332; *Surrey CC* v. *Bredero Homes Ltd.* [1993] 1 W.L.R. 1361. But see *Attorney-General* v. *Blake*, [1988] 1 All E.R. 833; Goodhart [1995] R.L. Rev. 3; *Jaggard* v. *Sawyer* [1995] 1 W.L.R. 269, at p. 281. See further Birks, ed., *Wrongs and Remedies in the Twenty-First Century* (1996), chs. 9, 10 and 13.

[70] *Lake* v. *Bayliss* [1974] 1 W.L.R. 1073; *Tito* v. *Waddell (No. 2)* (*supra*, n. 69), at p. 332.

[71] *Peter Pan Manufacturing Corporation* v. *Corsets Silhouette Ltd.* [1964] 1 W.L.R. 96.

[72] See *Reading* v. *Attorney-General* [1951] A.C. 507. See also *Hospital Products Ltd.* v. *U.S. Surgical Corp.* (1984) 156 C.L.R. 41 (Australia).

[73] *Penarth Dock Engineering Co. Ltd.* v. *Pound* [1963] 1 Lloyd's Rep. 359; *Wrotham Park Estate Co* v. *Parkside Homes Ltd.* [1974] 1 W.L.R. 798; *Jaggard* v. *Sawyer* (*supra*, n. 69).

enforceable contracts and it is arguable that the defendant's gains should be relevant in all such cases.

The suggestion has been made that gains should be recovered in all cases of cynical exploitation of breach for the purpose of making a gain so as to deter breaches of contract.[74] This, however, has the capacity to revolutionize contract remedies since in many cases, particularly commercial cases, the breach is in fact deliberate in the sense that it is knowingly done for commercial reasons. For instance, a seller of goods may choose to breach its contract and sell to a third party who is willing to pay a premium over and above the market price. Restitutionary awards made on this basis might also permit a plaintiff to evade the requirements of the mitigation rule. But it has been suggested that, apart from contracts which are specifically enforceable, there are two situations in which restitutionary damages for breach of contract may be awarded where compensatory damages would be inadequate. The first is the case of skimped performance where the defendant fails to provide the full extent of the services it contracted to provide and for which the plaintiff has paid. So, a security firm which has agreed to guard premises using a stipulated number of guards but used a much smaller number might be liable to pay the sum it had saved by its breach.[75] The second is where the defendant has obtained its profit by doing the very thing which it contracted not to do. So, a member of the security services who contracted not to disclose official information but did so for profit might be required to pay such profit to the other party to the contract.[76]

In these cases, the profits are occasioned directly by the breach and are attributable to the interest infringed. In other cases where the defendant makes a profit in excess of that which the plaintiff might have made there may be difficulties in so attributing that profit to the breach of contract as opposed to the defendant's skill and initiative so that it is difficult to say that the enrichment is 'at the expense' of the plaintiff.[77]

[74] Birks [1987] L.M.C.L.Q. 421. But this was rejected in *Attorney-General* v. *Blake* (*supra*, n. 69).
[75] *Attorney-General* v. *Blake* (*supra*, n. 69). See *City of New Orleans* v. *Firemen's Charitable Association* 9 So. 486 (1891). See also *White Arrow Express Ltd* v. *Lamey's Distribution Ltd*, (1995) 15 Tr.L.R. 69; Beale (1996) 112 L.Q.R. 205.
[76] *Attorney-General* v. *Blake* (*supra*, n. 69).
[77] Farnsworth (1985) 94 Yale L.J. 1339.

20

Limitation of Actions

At common law, lapse of time does not affect contractual rights. But it is the policy of the law to discourage stale claims, because after a long period a defendant may not have the evidence to rebut such claims and should be in a position to know that after a given time an incident which might have led to a claim is finally closed. Accordingly, in the Limitation Act 1980, the legislature has laid down certain periods of limitation after the expiry of which no action can be maintained. Equity has developed a doctrine of laches, under which a plaintiff who has not shown reasonable diligence in prosecuting the claim may be barred from equitable relief.

I. Limitation Act 1980[1]

(a) The General Rule

The general rule

The Act provides that an action founded on a simple contract must be commenced within 6 years, and one created or secured by a deed, within 12 years, from the date on which the cause of action accrued.[2] In contract, the cause of action normally accrues, not, as in tort, when the damage is suffered, but when the breach of contract takes place[3] or, in the case of an anticipatory breach, when the innocent party elects to treat the contract as terminated.[4] In the case of certain loans, however, the 6-year period does not start to run unless and until a demand in writing for the repayment of the debt is made by or on behalf of the creditor.[5]

[1] For proposals for reform see Law Com. C.P. No. 151, *Limitation of Actions* (1998).

[2] Limitation Act 1980, ss. 5, 8. But in the case of personal injuries arising from a breach of contract, ss. 11 and 14 of the Act provide that the limitation period is to be 3 years from the date on which the cause of action accrued or the date of the plaintiff's knowledge (if later) of certain relevant facts. See also ss. 12, 13, 14 (fatal accidents).

[3] *Battley* v. *Faulkner* (1820) 3 B. & Ald. 288; *Short* v. *M'Carthy* (1820) 3 B. & Ald. 626; *Howell* v. *Young* (1826) 5 B. & C. 259. But if the plaintiff can establish an action in tort for negligence, the cause of action accrues when the damage is suffered: *Midland Bank Trust Co. Ltd.* v. *Hett, Stubbs & Kemp* [1979] Ch. 384; *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145; *First National Commercial Bank* v. *Humberts* [1995] 2 All E.R. 673. Cf. *Forster* v. *Outred & Co.* [1982] 1 W.L.R. 86; *Pirelli General Cable Works Ltd.* v. *Oscar Faber & Partners* [1983] 2 A.C. 1; *Bell* v. *Peter Browne & Co.* [1990] 2 Q.B. 495.

[4] *Reeves* v. *Butcher* [1891] 2 Q.B. 509.

[5] Limitation Act 1980, s. 6.

A distinction is, however, drawn between a 'once and for all' breach and a 'continuing' breach. In the case of a continuing breach, such as of an obligation to repair a building, the promisor's duty is considered as persisting and as being for ever renewed until that which has been promised has been done; 'a further breach arises in every successive moment of time during which the state or condition is not as promised, during which . . . the building is out of repair'.[6] In cases of continuing breaches the plaintiff will be able to recover in respect of that part of the breach which occured within the 6 or, in the case of an obligation created or secured by a deed, 12 years before the action was brought.

It is no answer to a plea of limitation that the plaintiff was unaware or could not have been aware of the existence of the cause of action for breach of contract until after the expiry of the limitation period. The 'discoverability' rule in the Latent Damage Act 1986 does not apply to a breach of contract.[7]

Where the action is in restitution, the plaintiff's cause of action normally accrues when the defendant is unjustly enriched whether by the receipt of money or otherwise.[8]

(b) Persons Under a Diability

Plaintiff under a disability

If on the date on which the cause of action accrued the person to whom it accrued was under a disability, i.e. was a minor or person of unsound mind,[9] the action may be brought within 6 years from the date when he or she ceased to be under the disability, or dies.[10] This enlargement of time does not apply when the disability supervenes after the right of action has already accrued, or where the same person is afflicted by successive disabilities (e.g. minority followed by insanity) separated by an interval in which he or she is under no disability. Again, no extension is allowed when the right of action first accrues to a person not under a disability through whom the person under a disability claims.

(c) Effect of Fraud, Concealment and Mistake

Fraud, concealment, & mistake

Where an action is based on the fraud of the defendant, or where any fact relevant to the right of action has been deliberately concealed from the plaintiff by the defendant, whether before or after the cause of action has accrued,[11] or where an action is for relief from the consequences of a mistake, the period does not begin to run until the plaintiff has discovered the fraud, concealment, or mistake, or

[6] *Larking* v. *Great Western (Nepean) Gravel Ltd.* (1940) 64 C.L.R. 221, *per* Dixon J. at 236 (High Court of Australia). See also the facts of *Midland Bank Trust Co. Ltd.* v. *Hett, Stubbs & Kemp* (*supra*, n. 3).

[7] *Iron Trades Mutual Insurance Co. Ltd.* v. *J. K. Buckenham Ltd.* [1990] 1 All E.R. 808. But it will apply if the plaintiff can establish an action in tort for negligence. See also Consumer Protection Act 1987, s. 5(5).

[8] McLean [1989] C.L.J. 472; *Armontilla* v. *Telefusion* (1987) 9 Con. L.R. 139.

[9] Limitation Act 1980, s. 38(2).

[10] *Ibid.*, s. 28.

[11] *Sheldon* v. *R.H.M. Outhwaite (Underwriting Agencies) Ltd.* [1996] A.C. 102.

could with reasonable diligence have discovered it.[12] The 1980 Act further provides that a deliberate breach of duty in circumstances in which it is unlikely to be discovered for some time amounts to deliberate concealment of the facts involved in that breach of duty.[13] So, for example, if a builder fails to disclose the deliberate breach of a building contract by using defective bricks[14] or putting in inadequate foundations,[15] or if the vendors of a house knowingly fail to warn the purchaser of the risk of subsidence, when they are aware that the house has been built on a disused rubbish tip,[16] the running of the limitation period will be postponed until such time as the plaintiff discovers the concealment or could with reasonable diligence discover it.[17]

(d) Acknowledgement and Part Payment

Acknowledgement and part payment

An acknowledgement of a debt or part payment of a debt may extend the period of limitation. The 1980 Act provides[18] that in such a case the right shall be treated as having accrued on and not before the date of the acknowledgement or payment. Thus where A owes B the sum of £500, say, as the price of goods sold and delivered, B's remedy is barred after the passing of 6 years from the date on which payment became due. But if A, during that period, either acknowledges the debt and its legal liability to pay it[19] or makes a part payment on account of the debt, time begins to run afresh from the date of the acknowledgement or part payment. The limitation period may thus be repeatedly extended. Once, however, it has expired, the right of action cannot subsequently be revived.[20] To be effective, an acknowledgement must be in writing and signed by the person making it or that person's agent, and either an acknowledgement or part payment must be made to the person or to the agent of the person whose claim is acknowledged or in respect of whose claim the payment is made.[21]

(e) Statute Bars Remedy Not Right

Statute bars remedy not right

The Act operates merely to bar the contractual remedy, but not to extinguish the right. It is procedural and not substantive. Accordingly, a debtor who pays a statute-barred debt, cannot recover the money as money not due.[22] And if the debtor owes to the creditor certain debts some of which are, and some of which

[12] Limitation Act 1980, s. 32. But this provision is not to affect the rights of third parties taking *bona fide* and for value. *Sed quaere* whether an action under the Misrepresentation Act 1967, s. 2(1) falls within s. 32 of the 1980 Act because of the statutory fiction of fraud: *ante*, p. 245.

[13] *Ibid.*, s. 32(2).

[14] *Clark* v. *Woor* [1965] 1 W.L.R. 650.

[15] *Applegate* v. *Moss* [1971] 1 Q.B. 406.

[16] *King* v. *Victor Parsons & Co.* [1973] 1 W.L.R. 29.

[17] Note, however, these cases were decided on the wording of the Limitation Act 1939, s. 26(b), now repealed.

[18] s. 29(5).

[19] *Surrendra Overseas Ltd.* v. *Government of Sri Lanka* [1977] 1 W.L.R. 565; *Kamouh* v. *Associated Electrical Industries International Ltd.* [1980] Q.B. 199.

[20] Limitation Act 1980, s. 29(7).

[21] *Ibid.*, s. 30.

[22] *Bize* v. *Dickason* (1786) 1 Term R. 286, at p. 287.

are not, statute-barred, the creditor is entitled to appropriate any payment made by the debtor to those debts which are statute-barred, unless the debtor at the time expressly indicates that he is discharging a debt which is still actionable.[23]

II. Bars to Equitable Relief: Laches

(a) The Statute Applied by Analogy

Statute applied by analogy

The statutory periods of limitation do not apply to claims for specific performance or an injunction or other equitable relief, except in so far as the Court may apply them by analogy.[24] The situations to which the statute will be applied by analogy are relatively few, but, for example, the right to a final injunction will not be barred so long as the substantive legal right which it seeks to protect has not become barred.[25]

(b) Laches

Laches

Equitable claims or remedies to which the statute does not apply expressly or by analogy are subject to the equitable doctrine of laches. Equity has always refused its aid to stale claims. Delay which is sufficient to deprive a person of the right to claim specific performance or injunction is known technically as 'laches'. This doctrine has been described in a well-known passage in the advice of the Privy Council in *Lindsay Petroleum Co.* v. *Hurd*,[26] as follows:

> The doctrine of laches in Courts of Equity is not an arbitrary or a technical doctrine. Where it would be practically unjust to give a remedy, either because the party has, by his conduct, done that which might fairly be regarded as equivalent to a waiver of it, or where by his conduct and neglect he has, though perhaps not waiving that remedy, yet put the other party in a situation in which it would not be reasonable to place him if the remedy were afterwards to be asserted, in either of these cases lapse of time and delay are most material. But in every case, if an argument against relief, which otherwise would be just, is founded upon mere delay, that delay of course not amounting to a bar by any statute of limitations, the validity of that defence must be tried upon principles substantially equitable. Two circumstances, always important in such cases, are, the length of the delay and the nature of the acts done during the interval.

Delay may therefore bar equitable remedies such as claims for rescission,[27] rectification,[28] specific performance,[29] or for an interim or interlocutory

[23] *Mills* v. *Fowkes* (1830) 5 Bing. N.C. 455.
[24] Limitation Act 1980, s. 36(1).
[25] *Fullwood* v. *Fullwood* (1878) 9 Ch. D. 176.
[26] (1874) L.R. 5 P.C. 221, *per* Lord Selborne at p. 239.
[27] *Lindsay Petroleum Co.* v. *Hurd* (*supra*, n. 26).
[28] *Beale* v. *Kyte* [1907] 1 Ch. 564.
[29] *Mills* v. *Haywood* (1877) 6 Ch. D. 196. But cf. *Lazard Bros. & Co. Ltd.* v. *Fairfield Properties Co. (Mayfair) Ltd.* (1977) 121 Sol. J. 793 (2-year delay insufficient to bar specific performance of contract for sale of land); *H. P. Bulmer Ltd.* v. *J. Bollinger S.A* [1977] 2 C.M.L.R. 625.

injunction.[30] The plaintiff must show itself to be 'ready, desirous, prompt and eager' to assert its rights, and even a short lapse of time may, in certain circumstances,[31] be fatal. But in exceptional circumstances, as where the parties have been negotiating, a lapse of time longer than the common law limitation period will not be fatal.[32]

[30] *Great Western Ry.* v. *Oxford, Worcester and Wolverhampton Ry.* (1853) 3 De G.M. & G. 341; *Shepherd Homes Ltd.* v. *Sandham* [1971] Ch. 340 (4-month delay).

[31] *Lehmann* v. *McArthur* (1868) L.R. 3 Ch. App. 496 (short leasehold interest); *First National Reinsurance Co. Ltd.* v. *Greenfield* [1921] 2 K.B. 260 (shares). See also *Nelson* v. *Rye* [1996] 2 All E.R. 187.

[32] *Southcomb* v. *Bishop of Exeter* (1847) 6 Hare 213. See also *Tito* v. *Waddell* [1977] Ch. 106, at pp. 244–52 (specific performance refused 17 years after the breach of contract not because of delay; but because of futility).

PART 6

Agency

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21

Creation of Agency

Nature of agency

ALTHOUGH as a general rule A cannot by contract with B confer rights or impose liabilities upon a third party, yet A may represent or act on behalf of B, with B's authority, for the purpose of bringing B into legal relations with a third party. The relationship thus constituted is called agency.[1]

Capacity

Full contractual capacity is not necessary to enable a person to represent another as agent. Minors can be agents,[2] although their incapacity may shield them from liability to their principals.[3] But it is not possible to enter into a contract through an agent which is outside the principal's contractual capacity.[4]

I. Modes of Creation

Creation of agency

AGENCY may be created in any one of five ways:

(a) by an actual authority to contract given by the principal to the agent;
(b) by the principal's ratification of a contract entered into by the agent on the principal's behalf but without its authority;
(c) by an ostensible authority conferred by the principal on the agent even though no actual authority has been given;
(d) by an implication of law in cases of necessity.

In the first two cases, the principal can sue and be sued by the third party and rights and duties also arise between the principal and the agent. In the last three cases, the principal can be sued but cannot always sue. We shall deal with each of these in turn, and also consider the authority which is vested in different kinds of agents.

[1] The leading textbooks on this subject are *Bowstead and Reynolds on Agency*, 16th edn. (1996); Powell, *The Law of Agency*, 2nd edn.

[2] *Foreman* v. *G.W. Ry.* (1878) 38 L.T. 851; *Re D'Angibau* (1880) 15 Ch. D. 228, at p. 246.

[3] *Ante*, p. 211 ff. But note the Minors' Contracts Act 1987, s. 3 (Court empowered to order a minor to transfer to the plaintiff any property acquired by the minor under the contract).

[4] *Daily Telegraph Newspaper Co.* v. *M'Laughlin* [1904] A.C. 776. The statement of Denning L.J. in *Re Shephard* [1953] Ch. 728 (reversed on other grounds *sub nom. Shephard* v. *Cartwright* [1955] A.C. 431) that a minor cannot appoint an agent seems too wide. Although it would appear that a minor cannot give a valid power of attorney (*Zouch* v. *Parsons* (1765) 3 Burr. 1794), a minor can contract through an agent to the same extent as that minor could personally: see *G.(A.)* v. *G.(T.)* [1970] 2 Q.B. 643, at pp. 651–2.

(a) Actual Authority

Actual authority

Express authority

Actual authority to contract may be express or implied.

Normally the authority given by a principal to its agent is an express authority enabling the latter to bind the former by acts done within the scope of that authority. Such authority may, in general, be given orally. But in some cases it is necessary that the authority should be given in a special form. First, in order that an agent may make a binding contract under seal, it is necessary that authority should be received under seal. Certain transactions, for example, conveyances of land, must still be made by deed.[5] Secondly, the Law of Property Act 1925,[6] which requires the creation or disposition of any equitable interest, or interest in land, to be in writing, signed by the grantor or the grantor's agent, lays down that in such case the agent shall be authorized in writing.

Implied authority

The authority of an agent may also be implied. In most cases such implied authority is said to be *incidental* to an express authority or *required* due to the circumstances of the case. The category of implied authority also includes *usual* and *customary* authority. Generally, agents have the authority *usually* possessed by agents in their position. Therefore if an agent is authorized to conduct a particular trade or business, or to perform certain duties, that agent has implied authority to do such acts as are usual in the trade or business, or ordinarily incidental to the due performance of the duties. In addition, every agent has implied authority to act in accordance with the reasonable customs and usages of the particular place, trade, or market where the agent is employed, for example, the London Stock Exchange.[7]

(b) Ratification

Ratification

Even if the agent enters into a contract without the authority of the principal, the principal may subsequently ratify, that is to say, adopt the benefit and liabilities of a contract made on the principal's behalf.

Relation back to time of contract

This may occur in one of two ways. First, when A, though contracting as P's agent, and having P in contemplation as the principal, was not at the time of the contract P's agent in fact, as no precedent authority had been received. Secondly, when A was in fact P's agent at the time of making the contract, but exceeded the authority which P had given. In either case a ratification duly made places the parties in exactly the same position in which they would have been if A had P's authority at the time the contract was made. It is said to 'relate back' to the time of contracting and to have a retrospective effect.[8] An unauthorized acceptance

[5] On formalities for the creation of powers of attorney, see Powers of Attorney Act 1971, s. 1 (as amended by the Law of Property (Miscellaneous Provisions) Act 1989); Enduring Powers of Attorney Act 1985, s. 2.

[6] ss. 53(1), 54.

[7] *Pollock* v. *Stables* (1848) 12 Q.B. 765.

[8] *Wilson* v. *Tumman* (1843) 6 M. & G. 236, *per* Tindal C.J. at p. 242. The Latin maxim is *omnis ratihabitio retrotrahitur et priori mandato aequiparatur.*

may therefore be ratified even though the offer has in the meantime been withdrawn. So in *Bolton Partners* v. *Lambert*:[9]

The managing director of a company, purporting to act as agent on the company's behalf, but without its authority, accepted an offer by the defendant for the purchase of some sugar works belonging to them. The defendant then withdrew his offer, but the company ratified the manager's acceptance.

It was held that the defendant was bound. The ratification related back to the time of the agent's acceptance and so prevented the defendant subsequently revoking the offer. But there can be no true ratification where an agent purports to accept an offer 'subject to ratification', or where the other contracting party has intimation of the limitation of the agent's authority. In such a case the so-called ratification would merely be an acceptance of the offer of the other party, which may be withdrawn at any time before the so-called ratification takes place.[10]

The rules which govern ratification may be summarized as follows: 'The agent must contract as agent, for a principal who is in contemplation, and who must also be in existence at the time, for such things as the principal can and lawfully may do'.

(i) The agent must purport to act as an agent for a named or identifiable principal

Principal must b named or identifiable

An individual may not incur a personal liability and then assign it to someone else under colour of ratification. The individual must contract as agent at the time of the contract, and the principal, if not named, must at any rate be identifiable. It is not possible for an undisclosed principal, that is, a principal who is not disclosed by the agent to the third party at the time of contracting, to step in and ratify acts done by the agent in excess of what had previously been authorized.[11] In *Keighley, Maxsted & Co.* v. *Durant*:[12]

A corn merchant was authorised to buy wheat at a certain price on a joint account for himself and the appellants. Acting in excess of his authority, he purchased wheat at a higher price from the respondents, but in his own name. The appellants next day ratified the transaction, but later failed to take delivery of the wheat. The respondents brought an action against them for breach.

The action failed. The corn merchant had contracted in his own name without mentioning that the appellants were his principals. Any purported ratification by them was therefore ineffective, and they were consequently under no contractual obligation to the respondents.

On the other hand, if this requirement is satisfied, it makes no difference that the agent's act was a fraud on the principal. So where an agent, without

[9] (1888) 41 Ch. D. 295, doubted in *Fleming* v. *Bank of New Zealand* [1900] A.C. 577, at p. 587, but followed in *Presentaciones Musicales S.A.* v. *Secunda* [1994] Ch. 271.

[10] *Watson* v. *Davies* [1931] 1 Ch. 455; *Warehousing & Forwarding Co. of East Africa Ltd.* v. *Jafferali & Sons Ltd.* [1964] A.C. 1.

[11] Cf. *Welsh Development Agency* v. *Export Finance Co. Ltd.* [1992] B.C.L.C. 148 at pp. 159, 173, 182 (this principle is qualified by the maxim *id certum est quod certum reddi potest*, i.e. that which is capable of being made certain is to be treated as certain).

[12] [1901] A.C. 240.

authority, and fraudulently, entered into a contract for the sale of wheat in the principal's name, but intending to take the benefit of it, the principal could nevertheless ratify and adopt the contract and hold the buyers to their bargain.[13] But a forged signature cannot be ratified, for one who forges the signature of another is not an agent, actually or in contemplation. The forger does not act for another; but rather personates the person whose signature has been forged.[14]

(ii) The principal must be in existence

rincipal must be in existence at time of contract

To ratify the contract, the intended principal must have been in existence, and ascertainable, at the time that the contract was made. It is not necessary for the principal to be named as long as he or she is ascertainable.[15]

This rule is important in its bearing on the liabilities of companies for the contracts made by the promoters on their behalf before they are formed. In *Kelner* v. *Baxter*:[16]

The promoters of an unformed company entered into a contract on its behalf, which the company when duly incorporated, ratified. It went into liquidation, and the promoters, who had contracted as agents, were sued upon the contract. They pleaded that the liability had passed, by ratification, to the company, and no longer attached to them.

The Court rejected this argument. Willes J. said:[17]

Could the company become liable by a mere ratification? Clearly not. Ratification can only be by a person ascertained at the time of the act done,—by a person in existence either actually or in contemplation of law; as in the case of assignees of bankrupts and administrators, whose title, for the protection of the estate, vests by relation.

This limitation is likely to work hardship to solicitors and others who are called in to do the preliminary work leading to the formation of a company. They will have no right of action against the company when formed, although, as we shall see,[18] they will normally be able to assert a right of action against the promoters in such cases, since the promoters will be considered to have incurred personal liability on the contract.[19]

(iii) Capacity of the principal to contract

Principal must have capacity at time of contract

The agent must contract for such things as the principal can, and lawfully may, do, both at the time of contracting and at the time of ratification. 'At the time the act was done the agent must have had a competent principal.'[20] Thus, if an agent enters into a contract on behalf of a principal who is, at the time, incapable of making it, no ratification is possible.[21]

[13] *Re Tiedemann and Ledermann Frères* [1899] 2 Q.B. 66.
[14] *Brook* v. *Hook* (1871) L.R. 6 Ex. 89.
[15] *National Oilwell (U.K.) Ltd.* v. *Davy Offshore Ltd.* [1993] 2 Lloyd's Rep 582, at pp. 592–7.
[16] (1866) L.R. 2 C.P. 174. See also *Natal Land and Colonization Co. Ltd.* v. *Pauline Colliery and Development Syndicate Ltd.* [1904] A.C. 120.
[17] At p. 184.
[18] *Post*, p. 650.
[19] Companies Act 1985, s 36C(1), inserted by Companies Act 1989, s 130(4).
[20] *Firth* v. *Staines* [1897] 2 Q.B. 70, at p. 75, *per* Wright J.
[21] *Ashbury Railway Carriage and Iron Co.* v. *Riche* (1875) L.R. 7 H.L. 653 (*ultra vires* contract); *Boston Deep Sea Fishing and Ice Co. Ltd.* v. *Farnham* [1957] 1 W.L.R. 1051 (alien enemy).

and at time of ratification

Further, the principal can only ratify the act of the agent if at the time of the purported ratification, the principal could personally do the act in question.[22] So, for example, a contract of insurance made by an agent without the principal's authority cannot be ratified after the principal has become aware that the event insured against has in fact occurred. The principal could not insure in such circumstances, and is not permitted to take advantage of the agent's unauthorized act.[23]

(iv) Manner of ratification

Mode in which ratification may be made

The principal who accepts the contract made by a person whom the principal thereby undertakes to regard as its agent, may accept by words or conduct. The principal may avow responsibility for the act of the agent, or take the benefit of the contract, or otherwise by acquiescence in what is done create a presumption of authority. In the absence of an express avowal, however, the ratification must be founded on a full knowledge of the facts,[24] and the principal must have had the option whether to accept or to refuse the contract.[25] Otherwise it will be unenforceable against the principal. It is not, however, necessary for the ratification to be communicated to the third party.[26]

(v) Time of ratification

Ratification may come too late to be effective. Thus, it has been said that 'an estate once vested cannot be divested, nor can an act lawful at the time of its performance be rendered unlawful by the doctrine of ratification'. Although the basis of this limit to the ability to ratify has been said to be wider than that property rights should not be divested retrospectively, it is not easy to discern the principle upon which ratification will be denied.[27]

(c) Ostensible Authority

Ostensible authority

The principal may, by words or conduct, create an inference that an agent has authority to act on behalf of the principal even though no authority exists in fact. In such a case, if the agent contracts within the limits of the apparent authority, although without any actual authority, the principal will be bound to third parties by the agent's acts.

and estoppel

This doctrine of apparent authority, or ostensible authority as it is usually called, is really an application of the principle of estoppel, for estoppel means only

[22] *Presentaciones Musicales S.A.* v. *Secunda* [1994] Ch. 271, *per* Dillon L.J. at p. 277.

[23] An exception is created by the Marine Insurance Act 1906, s. 86, but this is an anomaly which the Courts have refused to extend, see *Grover & Grover* v. *Matthews* [1910] 2 K.B. 401.

[24] *La Banque Jacques-Cartier* v. *La Banque d'Epargne de Montréal* (1887) 13 App. Cas. 111.

[25] *Forman & Co. Pty. Ltd.* v. *Ship 'Liddesdale'* [1900] A.C. 190, *ante*, p. 488.

[26] See *Shell Co. of Australia Ltd.* v. *Nat Shipping Bagging Services Ltd. (The Kilmun)* [1988] 2 Lloyd's Rep. 1 at p. 11 citing *Harrisons & Crossfield Ltd.* v. *L.N.W. Railway* [1917] 2 K.B. 755 at p. 758 *per* Rowlatt J. See also *Pagnan SpA* v. *Feed Products Ltd.* [1987] 2 Lloyd's Rep. 601.

[27] *Presentaciones Musicales S.A.* v. *Secunda* [1994] Ch. 271, at p. 280. See also *Ainsworth* v. *Crecke* (1868) L.R. 4 C.P. 476; *Bolton Partners* v. *Lambert* (1888) 41 Ch. D. 295.

that a person is not permitted to resist an inference which can reasonably be drawn from the principal's words or conduct. Thus, where one person expressly or impliedly represents another to have authority to act as agent, so that a third party reasonably believes the person who is so held out to possess that authority and deals with that person in reliance on the representation so made, the person making the representation will be bound to the same extent as if actual authority had in fact been conferred.[28] The person making the representation is estopped from denying the ostensible authority which was thus created.

It is, however, important to note three things. First, the representation must be made by or with the authority of *the principal*.[29] Ostensible authority cannot be created simply by a representation by the agent.[30] Secondly, subject to certain exceptions which will be discussed *infra*,[31] the third party must rely on a representation of the agent's authority to act *as agent*; the doctrine cannot apply where the third party does not know or believe that person to be an agent, for example, if the existence of the principal is unknown to the third party.[32] Thirdly, the agent's want of authority must be *unknown* to the third party.[33]

Absence of authority

These limitations mean that there will seldom be ostensible authority where a person has never at any time had authority to contract. But in *Freeman & Lockyer* v. *Buckhurst Park Properties (Mangal) Ltd.*:[34]

> The articles of a company contained power to appoint a managing director. With the knowledge and approval of the board of directors, K acted as managing director, although he was never appointed to this post. K instructed the plaintiffs, a firm of architects, to do certain work for the company. The company disclaimed liability for payment for this work on the ground that K had no authority to contract on the company's behalf.
>
> The Court of Appeal held that, although K had no actual authority to employ the plaintiffs, the company had created an ostensible authority by its conduct in permitting him to act as managing director to the knowledge of the board. Any act done within the usual ambit of that ostensible authority was therefore binding on the company.

Limited or evoked authority

The doctrine of ostensible authority is more likely to apply where an authorized agent goes beyond the limits of his actual authority, yet acts within an authority

[28] For examples of factual situations in which ostensible authority may exist, see *Egyptian Intl. Foreign Trade Co.* v. *Soplex Wholesale Supplies Ltd. (The Raffaella)* [1985] 2 Lloyd's Rep. 36; *Shearson Lehman Hutton. Inc.* v. *MacLaine, Watson & Co. Ltd. (No. 2)* [1988] 1 W.L.R.16; *Polish SS. Co.* v. *A.J. Williams Fuels (Overseas Sales) Ltd. (The Suwalki)* [1989] 1 Lloyd's Rep. 511.

[29] *First Sport Ltd.* v. *Barclays Bank plc.* [1993] 1 W.L.R. 1229.

[30] *Att.-Gen. for Ceylon* v. *Silva* [1953] A.C. 461, at p. 479; *Freeman & Lockyer* v. *Buckhurst Park Properties (Mangal) Ltd.* [1964] 2 Q.B. 480, at p. 505; *British Bank of the Middle East* v. *Sun Life Assurance Co. of Canada (U.K.) Ltd.* [1983] 2 Lloyd's Rep. 9 (H.L.). See also *First Energy (U.K.) Ltd.* v. *Hungarian Int'll Bank Ltd.* [1993] 2 Lloyd's Rep. 194.

[31] See *post*, pp. 629–30.

[32] *Farquharson Bros.* v. *King & Co.* [1902] A.C. 325; *Freeman & Lockyer* v. *Buckhurst Park Properties (Mangal) Ltd.*(*supra*, n. 30), at p. 503.

[33] See *Armagas Ltd.* v. *Mundogas SA* [1986] 1 A.C. 717 at pp. 777–9.

[34] [1964] 2 Q.B. 480. But see now Companies Act 1985, s. 35(1), inserted by Companies Act 1989, and *ante*, p. 227 (*ultra vires* contracts).

which he is made to appear to possess.[35] In particular, where a principal has publicly allowed the agent to assume an authority, that authority cannot be revoked privately. The principal will be bound by the acts of the agent if the principal has given other persons reason to suppose that they are done with authority.

Employer and employee

Thus if an employer allows its employee habitually to purchase goods for it on credit from X, so that X becomes accustomed to look to the employer for payment for such things as are supplied in the usual course of dealing, the employer cannot privately revoke the employee's authority and claim, when sued by X, that the agency thereupon immediately determined. The employer's 'holding out' of the employee as its agent estops it from denying that the authority was not still in existence.[36]

Husband and wife

Similarly if a husband recognizes, and takes upon himself the liability in respect of, his wife's past dealings with suppliers of goods and servies, he holds her out to be his agent and to have his authority to contract on his behalf even for articles of luxury. He will be liable on such contracts as she may make with any supplier, unless and until he actually makes known to the supplier the fact that her agency has been determined.[37]

Partnership

Partnership also provides a further example of ostensible authority. Every partner is an agent of the firm and of the other partners for the business of the partnership; this is simply a case of implied authority. But any act done by a partner for carrying on in the usual way business of a kind carried on by the firm binds the firm and the other partners, even if the partner so acting has in fact no authority to act for the firm in the particular matter, unless the person with whom the partner is dealing either knows that person has no authority, or does not know or believe that person to be a partner.[38] Moreover, a partner who retires from a firm may still be liable for partnership debts contracted after retirement. A person dealing with a firm after a change in its constitution is entitled to treat all apparent members of the old firm as still being members of the firm until that person has notice of the change.[39] The retiring partner will be estopped from denying the continuation of that authority,[40] except where he was not known to be a partner by the person dealing with the firm.[41]

Liability of undisclosed principal for a usual in or incidental to business

These examples of ostensible authority are all consistent with the principle of estoppel previously mentioned. But there are a number of cases which establish that, in certain circumstances, a principal may be liable for the unauthorized acts of an agent, even though the third party did not rely upon any representation by the principal of the agent's authority to act *as agent*. In these cases, the existence

[35] *Todd* v. *Robinson* (1825) 1 Ry. & M. 217; *Summers* v. *Solomon* (1857) 7 E. & B. 879; *Manchester Trust* v. *Furness* [1895] 2 Q.B. 539.

[36] *Summers* v. *Solomon* (*supra*, n. 35).

[37] *Drew* v. *Nunn* (1879) 4 Q.B.D. 661; *Jetley* v. *Hill* (1884) Cab. & El. 239. See also *Ryan* v. *Sams* (1848) 12 Q.B. 460 (mistress).

[38] Partnership Act 1890, s. 5. See also s. 8. See further, *United Bank of Kuwait Ltd.* v. *Hammoud* [1988] 1 W.L.R. 1051.

[39] Partnership Act 1890, s. 36(1). Under s. 36(2), notice in the *London Gazette* is sufficient notice as to persons who had no dealings with the firm before the change; otherwise express notice is required.

[40] *Scarfe* v. *Jardine* (1882) 7 App. Cas. 345, at p. 349.

[41] Partnership Act 1890, s. 36(3).

of the principal was unknown to the third party, so that it could not be said that the principal held out the agent to have authority to act as agent, but as principal. The rule to be extracted from them is as follows: An undisclosed principal who employs an agent to conduct business is liable for any act of the agent which is incidental to or usual in that business, although such act may have been forbidden by the principal. For example, in *Watteau* v. *Fenwick*:[42]

The defendants, a firm of brewers, bought a beer-house from one Humble, but kept him on as manager, and his name appeared above the door. They instructed Humble not to buy cigars on credit, although it was usual for such a business to deal in cigars. Humble bought some cigars on credit from the plaintiff, who thought he was the owner of the business and gave credit to him personally. On discovering that he was employed by the defendants, the plaintiff sued them for the price of the cigars.

It was held that the defendants were liable. Wills J. rejected the argument that a principal could only be bound where there had been a holding out of authority—which could not be said of this case where the person supplying the goods knew nothing of the existence of the principal. 'The principal', he said,[43] 'is liable for all the acts of the agent which are within the authority usually confided to an agent of that character, notwithstanding limitations as between the principal and the agent, put upon that authority'.

This case is anomalous, and has been criticized as such.[44] An attempt has been made to explain it and similar cases on the grounds that they are cases of 'usual authority'. As we have seen,[45] the usual authority of an agent is merely an example of implied authority, which could be negatived by an express limitation. If this and similar cases[46] are rightly decided, they are better regarded as examples of the operation of a quasi-tortious principle whereby an employer is rendered vicariously liable for the acts of an agent if done in the course of the agent's employment.

Cohabitees

Another, somewhat archaic, category of agency in which there is no ostensible authority created by a holding out arises where two people are cohabiting. In such cases there is a rebuttable presumption that one has implied authority to pledge the credit of the other for necessaries in all domestic matters normally entrusted to the cohabitee who deals with the supplier.[47] The vast majority of the cases concern the liability of the husband for obligations incurred by his wife but the presumption is not confined to such cases.[48]

(d) Agency of Necessity

Agency of necessity

In certain circumstances the law confers an authority on one person to act as agent for another without any regard to the consent of the principal. Such an agency is

[42] [1893] 1 Q.B. 346.

[43] At p. 348.

[44] *Rhodian River Shipping S.A.* v. *Halla Maritime Corporation* [1984] 1 Lloyd's Rep. 373, *per* Bingham L.J. at pp. 378–9. See also Hornby [1961] C.L.J. 239.

[45] *Ante*, p. 624.

[46] It is not unique: see *Edmunds* v. *Bushell and Jones* (1865) L.R. 1 QB. 97. For further examples, see Powell, *The Law of Agency*, 2nd edn., pp. 72 ff., and *post*, p. 633.

[47] See generally *Bowstead and Reynolds on Agency*, 16th edn. (1996), §3-040A ff.

[48] *Debenham* v. *Mellon* (1680) 6 App. Cas. 24, at p. 33.

called an agency of necessity.[49] At common law the paradigm illustration of an agency of necessity was provided by the right of a wife, at common law, to supply the needs of herself and her children by pledging her husband's credit for necessaries. It was, however, abolished by legislation which gave the courts power to make financial provision in the event of a husband's wilful neglect to maintain his wife or children.[50]

Ship-masters and carriers

An agency of necessity can arise in the case of a carrier of goods or a master of a ship who, under certain circumstances of necessity, is empowered on behalf of the shipowner or the owner of the goods carried to dispose of the goods or to enter into such other contract as may be necessary, and will be considered to have their authority to do so.[51] In order that this agency of necessity should arise, it must be shown that the carrier or master:

(1) took action which was the only practicable action in the circumstances;[52] thus a master of a ship who finds that the cargo is perishing rapidly is entitled to put into the nearest port and to sell the goods for the best price there obtainable;[53]
(2) had no opportunity in the time available of communicating with the principal;[54]
(3) acted honestly in the interests of the principal.

In the situations mentioned above, the acts of the agent bind the principal, and it has been suggested that the expression 'agency of necessity' should properly be confined to such situations.[55] But the expression is frequently used also to describe cases where one person, in an emergency, performs services or incurs expenditure to preserve the property or rights of another and seeks reimbursement,[56] or where a person claims to be protected against an action for wrongful interference with the property of another by pleading necessity.[57]

Negotiorum gestio not recognized

In principle, a person who voluntarily incurs expense by performing work or services which are 'necessary' to another cannot recover in the absence of some legal authority to incur the expense.[58] Our law does not recognize the *negotiorum gestor* of Roman law—the person who voluntarily spends money upon the necessary protection of another.[59] So a person who finds a dog and spends money on

[49] See Treitel (1954) 3 U.W. Aust. L.R. 1; Birks [1971] C.L.P. 110; Rose (1989) 9 O.J.L.S. 167.
[50] Matrimonial Proceedings and Property Act 1970, s. 41 (on which see Cartwright-Sharp (1974) 37 M.L.R. 480). The repeal of this provision by the Matrimonial Causes Act 1973, s. 54 and Sched. 3 did not revive the doctrine.
[51] See e.g., *The Choko Star* [1990] 1 Lloyd's Rep. 516. By the Merchant Shipping Act 1995, s. 224(1) the master of a ship has authority to conclude salvage agreements on behalf of the shipowner.
[52] *Prager* v. *Blatspiel, Stamp & Heacock Ltd.* [1924] 1 K.B. 566.
[53] *Couturier* v. *Hastie* (1852) 8 Exch. 40, reversed on a different point (1856) 5 H.L.C. 673.
[54] *Springer* v. *Great Western Ry.* [1921] 1 K.B. 257. See also *In re F* [1990] 2 A.C. 1, at p. 75.
[55] *China-Pacific S.A.* v. *Food Cpn. of India* [1982] A.C. 939.
[56] *Exall* v. *Partridge* (1799) 8 T.R. 308.
[57] See *Elvin & Powell Ltd.* v. *Plummer Roddis Ltd.* (1933) 50 T.L.R. 158; *Sachs* v. *Miklos* [1948] 2 K.B. 23; and now the Torts (Interference with Goods) Act 1977, s. 12.
[58] *Macclesfield Cpn.* v. *G. C. Ry.* [1911] 2 K.B. 528.
[59] *Falcke* v. *Scottish Imperial Insurance Co.* (1886) 34 Ch. D. 234, *per* Bowen L.J. at p. 248.

its keep,[60] or a local authority which repairs a bridge which it is not bound to repair,[61] cannot recover from the owner of the property benefited.

Exceptions

Clear exceptions, however, exist in the case of salvage at sea (the owner of the cargo salvaged being bound to compensate the rescuer),[62] the supply of necessaries to mental patients,[63] and bills of exchange under section 65 of the Bills of Exchange Act 1882.[64] Any person, not being a party already liable on a bill of exchange, may, with the holder's consent, intervene and accept a bill *supra protest* for the honour of any party liable thereon, after it has been 'protested' for dishonour by non-acceptance. The acceptor for honour thereby makes himself liable to pay the bill, and succeeds to the rights and duties of the holder as regards the party for whose honour he pays, and all parties liable to that party. Outside of these recognized exceptions, there may yet be other cases where, after some legal relationship has been created between the parties, one party reasonably incurs expenses in safeguarding the other's goods in a situation of necessity, and is entitled to reimbursement. Thus a carrier has recovered the expense of stabling an uncollected horse,[65] a salvor the expense of warehousing cargo after the salvage services had come to an end,[66] and statute enables a doctor who has given emergency treatment to the victim of a road accident to a fee.[67] These cases may be regarded either as an extension of the principle that an agent is entitled to be reimbursed expenses reasonably incurred on behalf of the principal[68] or as an example of a claim in restitution.[69]

II. Different Kinds of Agents

Types of agent

We may note here the authority with which certain kinds of agents are invested in the ordinary course of their employment.

(a) Auctioneers

Auctioneers

An auctioneer is an agent to sell property at a public auction. Although primarily an agent for the seller, upon the property being knocked down, it has been held that the auctioneer becomes the agent of the buyer, but only for the purpose of signing a memorandum sufficient to satisfy the statutory formalities.[70] Auctioneers have authority to sell, but not to give warranties as to the property

[60] *Binstead* v. *Buck* (1776) 2 W. Bl. 1117 (no lien on dog for expenses).
[61] *Macclesfield Corporation* v. *Great Central Ry.* [1911] 2 K.B. 528.
[62] *The Five Steel Barges* (1890) 15 P.D. 142, at p. 146. See also Merchant Shipping Act 1995, s. 224(1).
[63] *Ante*, p. 231.
[64] See also Bills of Exchange Act 1882, s. 68 (payment for honour).
[65] *G.N. Ry.* v. *Swaffield* (1874) L.R. 9 Ex. 132.
[66] *China-Pacific S.A.* v. *Food Cpn. of India* [1982] A.C. 939.
[67] Road Traffic Act 1988, ss. 158–9. [68] See *post*, p. 641. [69] See *ante*, p. 9.
[70] See *Chaney* v. *Maclow* [1929] 1 Ch. 461, and *ante*, p. 78.

sold, unless expressly authorized by the seller.[71] Any deposit paid by the buyer is normally held by the auctioneer, not as agent of the seller, but as stakeholder.[72]

The seller will be bound if the auctioneer acts within his ostensible authority, even though disobeying instructions privately given. So, if an auctioneer through inadvertence, and contrary to instructions, puts up an article for sale without reserve, the seller will be bound by the sale.[73] But where there is a sale by auction with *notice* that it is subject to a reserve, the auctioneer cannot reasonably be supposed to have authority to accept a bid at less than the reserve fixed, and so cannot bind the seller by doing so.[74]

An auctioneer has a lien on goods sold until the whole price is paid, and, if not paid, can sue in his own name for the price.[75]

(b) Factors

Factors

A factor is an agent to whom goods are consigned for the purpose of sale.

The factor has possession of the goods, authority to sell them in its own name, and a general discretion as to their sale. The factor may sell on the usual terms of credit, may receive the price, and give a good discharge to the buyer. Its authority to dispose of the goods cannot, even at common law, be restricted as against third parties by instructions privately communicated by the principal, for a factor has ostensible authority to do such things as are usual in the conduct of its business.[76]

Factors Act 1889

This ostensible authority has been extended by a series of Factors Acts which were consolidated by the Factors Act 1889. The Act applies not only to factors, but also to any mercantile agent 'having in the customary course of his business as such agent authority either to sell goods, or to consign goods for the purpose of sale, or to buy goods, or to raise money on the security of goods'.[77] Such a person is deemed also to have power to pledge the goods, and section 2 of the Act in effect provides that where a mercantile agent is, with the consent of the owner, in possession of goods[78] or of the documents of title to goods, any sale, pledge, or other disposition of the goods, made when acting in the ordinary course of business of a mercantile agent, is as valid as if it were expressly authorized by the owner of the goods.

Persons, therefore, who, in good faith, take the goods under such a disposition, and who have not at the time notice that the agent has not the authority to dispose of them, acquire a good title to them. And so long as the agent is left in possession of the goods, revocation of authority by the principal cannot prejudice the rights of such persons to them.

[71] *Payne* v. *Lord Leconfield* (1881) 51 L.J.Q.B. 642.
[72] *Skinner* v. *Trustee of Reed* [1967] Ch. 1194.
[73] *Rainbow* v. *Howkins* [1904] 2 K.B. 322, at p. 326.
[74] *McManus* v. *Fortescue* [1907] 2 K.B. 1, at p. 6.
[75] *Chelmsford Auctions Ltd.* v. *Poole* [1973] Q.B. 542. Cf. *Cherry* v. *Anderson* (1876) I.R. 10 C.L. 204 (land).
[76] *Pickering* v. *Busk* (1812) 15 East. 38; see *ante*, p. 630.
[77] Factors Act 1889, s. 1(1).
[78] Provided that the possession is in the capacity of mercantile agent, and not e.g. solely as bailee: *Astley Industrial Trust Ltd.* v. *Miller* [1968] 2 All E.R. 386.

(c) Brokers

Brokers

A broker is an agent primarily employed to negotiate a contract between two parties.[79] A broker for sale, has not got possession of the goods to be sold, and so has not got the authority which a factor enjoys. Nor has a broker the authority to sue in its own name on contracts made by it.

(d) Estate Agents[80]

House agents

An estate agent, who is employed to find a purchaser for property, has implied authority to make representations or to give warranties relating to the property.[81] An estate agent has no authority to effect an actual contract for the sale of the property unless expressly authorized so to do[82] and does not have implied authority to receive a deposit from an intending purchaser as agent of the vendor.[83]

(e) Solicitors

Solicitors

When undertaking litigation on behalf of a client, a solicitor has implied authority to accept process and appear for a client, but is not entitled to commence an action without express authority.[84] As against third parties, a solicitor has an ostensible authority to effect a compromise in all matters connected with an action and not merely collateral to it.[85] In certain circumstances solicitors have authority to receive payment on behalf of a client.[86]

(f) Commercial Agents

Commercial Agents

This and the following two chapters are primarily concerned with the basic principles of agency as developed by the common law. Brief mention is, however, also made of a new form of agency, unknown to the common law, which, as a result of the EC Directive on Commercial Agents, is now part of English law.[87] A commercial agent is a self employed intermediary with continuing authority to negotiate the sale or purchase of goods on behalf of the principal, or to negotiate and conclude the sale or purchase of goods on behalf of and in the name of the principal. Where the Regulations implementing the Directive apply, the freedom to terminate a commercial agency, at least without compensation, is restricted.

[79] A broker should be distinguished from a commission agent. A commission agent is employed not to establish privity of contract between the principal and third parties, but to sell or buy goods for the principal at the most favourable price available. The commission agent receives a commission or reward, but the purchase or sale is made with the third party by the commission agent alone. See *Armstrong* v. *Stokes* (1872) L.R. 7 Q.B. 598; *post*, pp. 647–48 and Hill (1968) 31 M.L.R. 623.

[80] See Estate Agents Act 1979 and Property Misdescriptions Act 1991.

[81] *Mullens* v. *Miller* (1882) 22 Ch. D. 194.

[82] *Hamer* v. *Sharp* (1874) L.R. 19 Eq. 108; *Law* v. *Robert Roberts & Co.* [1964] I.R. 292.

[83] *Sorrell* v. *Finch* [1977] A.C. 728.

[84] *Wright* v. *Castle* (1817) 3 Mer. 12.

[85] *Strauss* v. *Francis* (1866) L.R. 1 Q.B. 379; *Waugh* v. *H. B. Clifford & Sons Ltd.* [1982] Ch. 374.

[86] Law of Property Act 1925, s. 69; *Yates* v. *Freckleton* (1781) 2 Doug. K.B. 623.

[87] The Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053) as amended by S.I. 1993 No. 3173 came into force on 1 January 1994.

22

Effect of Agency

THE effects of agency, when created as described above, may thus be arranged:

(1) the relations between the principal and agent;
(2) the relations between the principal and third parties;
(3) the relations between the agent and third parties.

I. The Relations Between the Principal and Agent

Relations between principal and agent

THE rights and duties of the principal and agent depend upon the terms of the contract, whether express or implied, which exists between them. But in addition to these specific provisions, the mere existence of the relationship raises certain duties on both sides. In particular, an agent owes fiduciary duties to its principal. It is with these general duties that we are here mainly concerned, and it is convenient, first to consider the duties of the agent, and then the duties of the principal.

(a) Duties of the Agent

Duties of agent: (i) to account

The agent is bound to account for such property of the principal as comes into its hands in the course of the employment. The agent must keep accurate accounts of the transactions which are entered into on the principal's behalf,[1] and produce them on demand to the principal.[2]

(ii) to use care and skill

The agent must also use ordinary diligence in the discharge of its duties, displaying any special skill or capacity which it may profess in relation to the work in hand.[3] Where the agency is gratuitous, the agent is only liable in tort, the standard of care is that which might reasonably be expected in the circumstances.[4]

If the agent fails in its duty, the normal remedy of the principal is to bring an action for damages; but where the breach consists of a failure to pay across money

[1] *White* v. *Lincoln* (1803) 8 Ves. Jun. 363. [2] *Pearse* v. *Green* (1819) 1 Jac. & W. 135.
[3] *Lee* v. *Walker* (1872) L.R. 7 C.P. 121. See also *Luxmoore May* v. *Messenger May Baverstock* [1990] 1 W.L.R. 1009.
[4] *Chaudhry* v. *Prabhakar* [1989] 1 W.L.R. 29. Cf. the older formulation in *Giblin* v. *McMullen* (1868) L.R. 2 P.C. 317, at p. 336: only as much skill as agent actually possesses and such care as it would exercise in the conduct of its own affairs.

received on behalf of the principal, an action for money had and received or an action for an account may also be brought by the principal.

Fiduciary nature of agency

There are, besides these ordinary duties, certain other duties owed by the agent to the principal which arise from the fiduciary nature of the relationship between them. Although it has been said that 'the essence of a fiduciary obligation is that it creates obligations of a different character from those deriving from the contract itself',[5] where the agency is based on a contract between the principal and the agent, the fiduciary duties may in certain cases be varied by the terms of the contract.[6]

(i) Agent must not make secret profit from agency

First, the agent must not, except with the knowledge and assent of the principal, make any profit from the transactions into which the agent enters on behalf of the principal[7] or from confidential information acquired in the capacity of agent.[8] It is immaterial that the principal has suffered no injury, or that the agent has acted throughout in good faith.[9] Any such profit made must be paid over to the principal. In *Hippisley* v. *Knee Brothers*:[10]

H employed K Brothers, auctioneers, to sell certain property for him, and undertook to pay them a commission on the sale and their out-of-pocket expenses, including those of printing and advertising. K received discounts from printers and advertisers, but charged H with the full amount in the honest belief that they were entitled to keep the discounts for themselves.

It was held that K were bound to account to H for the money. In this case, however, they did not forfeit their commission; but commission will not be payable to an agent who has acted dishonestly,[11] and, if paid in ignorance of the breach of duty, will be recoverable by the principal.

or take a bribe

Where an agent is promised a bribe or secret commission which might induce the agent to act disloyally to the principal or which might diminish his interest in the affairs of the principal, the agent cannot recover the amount of the bribe from the person who promised it, since the transaction is a corrupt one and cannot be enforced.[12] If the agent has received the bribe, it can be claimed by the principal from both the agent[13] and the briber[14] on a restitutionary basis; the agent cannot recover or retain any remuneration from the principal in respect of the transaction.[15] Moreover, since the the agent is a fiduciary, if property or investments

[5] *Re Goldcorp Exchange Ltd.* [1995] 1 A.C. 74, *per* Lord Mustill, at p. 98.

[6] *Clark Boyce* v. *Mouat* [1994] 1 A.C. 428; *Kelly* v. *Cooper* [1993] A.C. 205 (implied term of contract permitted estate agent to have conflict of interests). See also Law Com. No. 236, *Fiduciary Duties and Regulatory Rules* (1995), §§ 3.24 ff., but cf. *Bowstead and Reynolds on Agency*, 16th edn. (1996), p. 217; Brown (1993) 109 L.Q.R. 206.

[7] *Parker* v. *M'Kenna* (1874) L.R. 10 Ch. App. 96; *Cook* v. *Deeks* [1916] A.C. 554; *English* v. *Dedham Vale Properties Ltd.* [1978] 1 W.L.R. 93; *Clark Boyce* v. *Mouat* [1994] 1 A.C. 428. See also *post*, p. 637.

[8] *Phipps* v. *Boardman* [1967] 2 A.C. 46; *Guinness plc* v. *Saunders* [1990] 2 A.C. 663.

[9] *Ibid.*

[10] [1905] 1 K.B. 1.

[11] *Andrews* v. *Ramsay & Co.* [1903] 2 K.B. 635. See also *Kelly* v. *Cooper* [1993] A.C. 205, at p. 216.

[12] *Harrington* v. *Victoria Graving Dock Co.* (1878) 3 Q.B.D. 549.

[13] *Boston Deep Sea Fishing and Ice Co.* v. *Ansell* (1888) 39 Ch. D. 339; *Logicrose Ltd.* v. *Southend United Football Club* [1988] 1 W.L.R. 1256.

[14] *Arab Monetary Fund* v. *Hashim* [1993] 1 Lloyd's Rep. 543.

[15] *Andrews* v. *Ramsay & Co.* [1903] 2 K.B. 635.

acquired with the bribe have increased in value, the principal has an equitable proprietary interest in the profits and is entitled to them.[16] Alternatively, it is open to a principal who discovers that its agent has been paid a bribe for bringing about a contract to recover from the agent and the person who paid the bribe, jointly and severally, damages in tort for any loss which the principal may have sustained by entering into the contract in respect of which the bribe was given. But the principal is bound to elect, at the time judgment is entered, between the claim for the amount of the bribe and the claim for damages. In *T. H. Mahesan s/o Thambiah* v. *Malaysia Government Officers' Co-operative Housing Society Ltd.*:[17]

A director and employee of a housing society in Malaysia dishonestly agreed with M that M should purchase certain land in Penang at a low price and sell it to the housing society at a profit, and that the director would not inform the housing society of the price at which the land was available nor the fact that M was selling the land to the housing society at more than double the price which he had paid for it. M made a gross profit of $488,000 on the transaction, one-quarter of which he passed on to the director as a bribe.

The Federal Court of Malaysia held that the housing society could recover from its director both the amount of the bribe and damages for the whole of the loss suffered by it as a result of the fraudulent transaction.[18] The Judicial Committee of the Privy Council, however, held that the housing society could recover either the amount of the bribe or damages for the loss suffered, but not both. In the result, since the loss suffered was (net) $443,000 and the amount of the bribe was $122,000, it was assumed that the housing society would have elected to claim the former sum, and judgment was entered for that amount.

The Prevention of Corruption Acts 1906 and 1916 also make corrupt transactions of all kinds by or with agents criminal offences punishable by fine and imprisonment.

(ii) Agent must not put itself in position where interest and duty conflict or duties conflict

Secondly, the agent must not put itself in a position where its duty and interest conflict unless full disclosure of the agent's interest (specifying its exact nature) has been made to the principal, and the principal has given its informed consent to the conflict.[19] So, an agent will in general be precluded from acting for two principals whose interests may conflict, unless the principals' assent has been obtained.[20]

Moreover, an agent may not cease to be an agent and become a principal party to the transaction even though this change of attitude does not result in injury to the employer. If a person is employed to buy or sell on behalf of another, that person may not sell to or buy from the principal. Nor, if a person is employed to bring another (the principal) into contractual relations with a third party, may that

[16] *Att-General for Hong Kong* v. *Reid* [1994] 1 A.C. 324.

[17] [1979] A.C. 374. See Beatson and Reynolds (1978) 94 L.Q.R. 344. Cf. Tettenborn (1979) 95 L.Q.R. 68.

[18] Relying on *dicta* of the Court of Appeal in *Mayor of Salford* v. *Lever* [1891] 1 Q.B. 168, which were disapproved by the Judicial Committee.

[19] *Clark Boyce* v. *Mouat* [1994] 1 A.C. 428; *Guinness plc.* v. *Saunders* [1990] 2 A.C. 663. Cf. *Kelly* v. *Cooper* [1993] A.C. 205 (implied term of contract, *ante*, p. 150).

[20] *Ibid.*

person lawfully also act as agent for that third party.[21] Where an agent puts itself in a position where the agent has an interest in direct antagonism to its duty, or where, due to the conflict of duties, the agent's duty to the principal cannot be fully discharged, the principal is entitled to claim an account and payment over of any benefit which the agent has received as a result. The leading case is *De Bussche* v. *Alt*:[22]

The plaintiff consigned a ship to G & Co. in China for sale for a minimum price of $90,000. G & Co. employed the defendant in Japan to sell the ship, and this sub-agency was consented to by the plaintiff. The defendant, having tried in vain to sell the ship at this price, bought her himself for $90,000. Shortly afterwards he resold her to a Japanese prince for $160,000. The $90,000 was remitted through G & Co. to the plaintiff, but he filed a bill to compel the defendant to account for the profit made by the resale.

It was held that, since the defendant was the plaintiff's agent, he was in breach of duty by changing his position without the consent of his principal; he was therefore bound to account for the profit which he had made.

(iii) Agent may not delegate to another

Thirdly, the agent may not, as a general rule, delegate to another person the task undertaken by the contract of agency.[23] The reason for this rule, and its limitations, are outlined by Thesiger L.J. in *De Bussche* v. *Alt*:[24]

As a general rule, no doubt, the maxim '*delegatus non potest delegare*' applies so as to prevent an agent from establishing the relationship of principal and agent between his own principal and a third person; but this maxim when analyzed merely imports that an agent cannot, without authority from his principal, devolve upon another obligations to the principal which he has himself undertaken to personally fulfil; and that, inasmuch as confidence in the particular person employed is at the root of the contract of agency, such authority cannot be implied as an ordinary incident in the contract.

There are, however, a number of occasions when such authority is implied. These occasions arise from the conduct of the parties, the usage of a trade, the nature of a business, or an unforeseen emergency.[25] Also purely ministerial acts, which do not involve any special care and skill, can normally be delegated to another.[26]

Privity

The employment by the agent of a sub-agent does not normally bring into being any privity of contract between the principal and the sub-agent. The sub-agent is responsible to the agent alone and cannot be sued directly in contract by the principal.[27] But where the principal expressly or impliedly authorizes the delegation, or ratifies a delegation which has already taken place, privity of contract is established.[28] The sub-agent becomes responsible to the principal for the due

[21] *Anglo-African Merchants Ltd.* v. *Bayley* [1970] 1 Q.B. 311, at pp. 323–4; *North & South Trust Co.* v. *Berkeley* [1971] 1 W.L.R. 470.
[22] (1878) 8 Ch. D. 286.
[23] See e.g. *John McCann & Co.* v. *Pow* [1974] 1 W.L.R. 1643 (estate agent).
[24] (1878) 8 Ch. D. 286, at p. 310.
[25] *Ibid.*, at p. 310; *Re Newen* [1903] 1 Ch. 812; *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145, at p. 197 (although the agent remained under an obligation that the services would be carried out with reasonable skill and care).
[26] *Allam & Co. Ltd.* v. *Europa Poster Services Ltd.* [1968] 1 W.L.R. 639.
[27] *Kahler* v. *Midland Bank* [1952] A.C. 24. But see *Shamia* v. *Joory* [1958] 1 Q.B. 448.
[28] *Keay* v. *Fenwick* (1876) 1 C.P.D. 745; *De Bussche* v. *Alt* (1878) 8 Ch. D. 286.

discharge of the duties which its employment casts upon it, and a fiduciary relationship arises between them. Where the sub-agent has been negligent, it may also be liable to the principal in tort, provided such liability is not inconsistent with the contractual structure put in place by the principal and agent.[29]

Del credere agents

An agent is not normally responsible for ensuring that the parties with whom the principal is brought into contractual relations will pay the money which may become due under the contract into which they enter. But such a responsibility is assumed by a *del credere* agent. This is an agent employed for the purpose of sale who, in return for extra remuneration, undertakes to be liable to the principal for payment by the buyer.[30] A *del credere* agent does not, however, become responsible to the buyer for the due performance of its contract by the principal.

(b) Duties of the Principal

Duties of principal: to pay agreed remuneration

The principal must pay the agent such commission or reward as may be agreed upon between them. In the absence of any agreement, express or implied, the agent is not entitled to any reward,[31] although there is a presumption that a professional agent is to be remunerated.[32] Indeed, an agreement to pay remuneration will be implied whenever a person is employed to act as agent under circumstances which raise the presumption that the agent would, to the knowledge of the principal, expect to be paid.[33]

Right of agent to remuneration

Before becoming entitled to remuneration, the agent must have carried out the duties, or fulfilled the conditions, stipulated for in the agreement. In particular, if the remuneration takes the form of a commission, the agent is not entitled to the commission until the event on which the commission is payable comes about. This question has frequently arisen in recent years in relation to commission payable to estate agents. The Courts have construed such provisions very strictly, and have said that a claim to commission, if no sale is actually made, must be established by the use of clear and unequivocal language.[34] Thus if the commission is payable 'on finding a purchaser', it has been held that a person found by an agent is not to be considered a 'purchaser' until that person actually purchases by entering into a contract.[35] And if the commission is payable on the introduction of a person

[29] *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145.

[30] Although the agent clearly promises 'to answer for the default of another', no note or memorandum is necessary to satisfy the requirements of the Statute of Frauds 1677, for the undertaking is only incidental to a larger contract. See *ante*, p. 80.

[31] *Reeve* v. *Reeve* (1858) 1 F. & F. 280.

[32] *Turner* v. *Reeve* (1901) 17 T.L.R. 592. See also Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No 3053), reg. 6.

[33] *Way* v. *Latilla* [1937] 3 All E.R. 739 (H.L.). Cf. *Re Richmond Gate and Property Co.* [1965] 1 W.L.R. 335.

[34] *Luxor (Eastbourne) Ltd.* v. *Cooper* [1941] A.C. 108, at p. 129; *Ackroyd & Sons* v. *Hasan* [1960] 2 Q.B. 144, at p. 154; *Jaques* v. *Lloyd D. George & Partners Ltd.* [1968] 1 W.L.R. 625; *Harwood (trading as RSBS Group)* v. *Smith, The Times*, 8 December 1997. Cf. *Scheggia* v. *Gradwell* [1963] 1 W.L.R. 1049; *Christie Owen & Davies Ltd.* v. *Rapacioli* [1974] Q.B. 781. The test is similar where the Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053) apply, see reg. 7.

[35] *Martin* v. *Perry & Daw* [1931] 2 K.B. 310.

'ready, willing and able to purchase', that person is not 'willing' to purchase where the agreement is 'subject to contract' or where the prospective purchaser withdraws before completion;[36] and a prospective purchaser is not 'able' to purchase if any obstacles, whether legal or financial, would prevent the purchase.[37]

Opportunity to earn commission

Where the employment of an agent is on a commission basis, the commission being payable on results, there is no general rule which prevents the principal from taking a step which deprives the agent of the opportunity to earn commission. So, for example, a person who employs an estate agent is not necessarily bound to complete the sale,[38] and can sell the property elsewhere,[39] or simply refuse to sell at all.[40] But there may be an express term of the agreement to the contrary, and in some cases the Courts have been prepared to imply a term in order to give business efficacy to the contract.[41] It is difficult to imply such a term, however, if it means that the principal's business must be kept in existence simply for the agent's benefit. In *Rhodes* v. *Forwood*:[42]

An agreement by the defendant colliery owner with the plaintiffs, a firm of brokers, that for a term of 7 years, or for so long as the plaintiffs should carry on business, the plaintiffs were to be the sole agents for the sale of any of the defendant's coal in Liverpool was not broken when, within 5 years, the defendants sold the colliery and ceased to carry on business.

The House of Lords held that the terms of the agreement did not bind the defendant to send any coal to Liverpool; they merely stipulated that, if coal was sent, the plaintiffs were to be the sole agents for its sale. There could therefore be no implication that the defendant should keep his colliery so that they might earn their commission.

On the other hand, in *Turner* v. *Goldsmith*:[43]

The defendant agreed to employ the plaintiff as his agent, canvasser, and traveller for 5 years. The plaintiff was to do his utmost to obtain orders for, and sell, such various goods *manufactured or sold* by the defendant as should from time to time be forwarded or submitted by sample to him. Within the period of 5 years the defendant's factory was burnt down and he did not resume business. The plaintiff brought an action for breach.

The Court of Appeal gave judgment in his favour. They implied a term that he was to be allowed to earn his commission. *Rhodes* v. *Forwood* was distinguished on the ground that, in that case, there not being any express contract to employ the agent, such a contract could not be implied.[44] The position differed where, as

[36] *Dennis Reed Ltd.* v. *Goody* [1950] 2 K.B. 277.
[37] *Dellafiora* v. *Lester* [1962] 1 W.L.R. 1208.
[38] *Boots* v. *Christopher (E.) & Co.* [1952] 1 K.B. 89.
[39] *McCallum* v. *Hicks* [1950] 2 K.B. 271.
[40] *Luxor (Eastbourne) Ltd.* v. *Cooper* (*supra*, n. 34).
[41] See *ante*, p. 144.
[42] (1876) 1 App. Cas. 256. See also *French & Co. Ltd.* v. *Leeston Shipping Co. Ltd.* [1922] 1 A.C. 451. See also *Orient Overseas Management and Finance Ltd.* v. *File Shipping Co. Ltd. (The Energy Progress)* [1993] 1 Lloyd's Rep. 355.
[43] [1891] 1 Q.B. 544. See also *Warren & Co.* v. *Agdeshman* (1922) 38 T.L.R. 588; *Alpha Trading Ltd.* v. *Dunnshaw-Patten* [1981] Q.B. 290; *George Moundreas & Co. SA* v. *Navimpex Centrala Navala* [1985] 2 Lloyd's Rep. 515.
[44] *Per* Lindley L.J. at p. 549.

Turner v. *Goldsmith*, there is an express contract to employ the agent. Moreover, the Court held that the contract had not been frustrated by the fire, for the plaintiff's employment was not confined to articles manufactured by the defendant, but extended also to articles sold by him without reference to their origin.

Reimbursement and indemnity

Unless otherwise agreed, the agent must also be reimbursed by the principal for all expenses, and indemnified against all liabilities and claims, which the agent has reasonably incurred in the execution of its duties.[45] These rights of reimbursement and indemnity extend to cases where the agent has occasioned liability by an honest mistake,[46] but not where they have arisen from breach of duty or default by the agent.[47]

Lien

The agent is entitled to a lien on the goods of the principal in its possession in respect of any claim by the agent against the principal arising out of the agency.[48] The lien is a possessory and particular lien, i.e. the goods can only be retained by the agent in respect of the particular transaction, unless by agreement or custom a general lien is given in respect of any claim outstanding against the principal, whether connected with the agency or not.[49]

II. The Relations Between the Principal and Third Parties

Qui facit per alium, facit per se

WHEN a principal endows an agent with actual authority to contract, the principal is bound, as regards third parties, by all acts of the agent which are done within the limits of that authority. This rule is often expressed in the maxim, *Qui facit per alium, facit per se*, a person who acts through another acts in person.

Even in cases where only ostensible authority

The same rule applies where the agent, though contracting outside its actual authority, contracts within an authority which it may reasonably be supposed the agent possessed.[50] This doctrine of ostensible authority has been discussed in Chapter 21.

Agent acting in fraud of principal

Once it is established that an agent is acting within its actual or ostensible authority, the principal will nevertheless be liable to third parties even though the agent has acted for its own benefit and in fraud of the principal.[51] Where, however, the third party dealing with the agent is aware that the agent is acting for its own benefit, or where the circumstances of the transaction are such as to put the third party on enquiry, the principal is not bound.[52]

[45] *Adamson* v. *Jarvis* (1827) 4 Bing. 66. See also *Islamic Republic of Iran Shipping Lines* v. *Zannis Cia. Naviera SA (The Tzelepi)* [1991] 2 Lloyd's Rep. 265.

[46] *Pettman* v. *Keble* (1850) 9 C.B. 701.

[47] *Lewis* v. *Samuel* (1846) 8 Q.B. 685.

[48] *Williams* v. *Millington* (1788) 1 H. Bl. 81, at p. 85.

[49] See e.g. *Snook* v. *Davidson* (1809) 2 Camp. 218 (factor); *John D. Hope & Co.* v. *Glendinning* [1911] A.C. 419 (stockbroker); *Barratt* v. *Gough-Thomas* [1951] Ch. 242 (solicitor).

[50] *Maddick* v. *Marshall* (1864) 16 C.B.N.S. 387, *per* Byles J. at p. 393.

[51] *Hambro* v. *Burnand and others* [1904] 2 K.B. 10.

[52] *Reckitt* v. *Burnett, Pembroke & Slater Ltd.* [1929] A.C. 176.

Rights of principal

A principal also acquires rights against a third party under a contract entered into by an agent on its behalf where the agent has acted within the limits of its actual authority. Otherwise it appears that a principal must ratify a contract entered into without authority before it can acquire rights (as opposed to liabilities) against the third party.

(a) Limitations on the Principal's Rights and Liabilities

Limits on principal's capacity to sue and be sued

There are certain situations in which, although the agent contracts within its authority, the principal acquires no rights or liabilities under the contract. It should, however, be stated that these situations are of extremely narrow application and (with one exception) of limited importance at the present day.

(i) Agent party to deed

First, it is still technically the rule that, if an agent is a party to a deed on behalf of another, the principal cannot sue or be sued on the deed unless described in the deed as party to it, and the deed is executed in the principal's name.[53] But in practice this rule is now a dead letter,[54] and cannot in any event be applied in the case of powers of attorney,[55] and contracts into which the agent enters as trustee for the principal.[56]

(ii) Foreign principal

Secondly, it was once thought to be a rule of law that a foreign principal could not sue or be sued on a contract entered into on its behalf, the agent only being liable on the contract.[57] But in modern conditions of trade this rule has no validity.[58] At the most it is but one factor to be taken into account in determining the true intent of the contract, and its weight may be minimal.[59]

(iii) Bills of exchange

Thirdly, a principal is not liable upon any bill of exchange or negotiable instrument unless its name is signed thereon;[60] but if it is signed there by an agent acting with authority, the principal will be liable.[61]

(iv) Undisclosed principal

In fact, the only substantial limitations upon the principal's rights and liabilities are those which are imposed in the case of an 'undisclosed principal', i.e. where the fact of the agency is not disclosed to the other party at the time that the contract is made. Normally, where an agent acts on behalf of a principal whose existence is not, at the time, disclosed, the principal can, when discovered, sue and be sued under the contract. The contractual relationship with the undisclosed principal is not separate from the subsisting contractual relationship between the agent and the other party.[62] This doctrine of the undisclosed principal is peculiar to English law, and has sometimes been criticized as an anomaly, since it runs

[53] *Schack* v. *Anthony* (1813) 1 M. & S. 573.
[54] Law of Property Act 1925, ss. 56(1), 74(3); see *ante*, p. 423.
[55] Powers of Attorney Act 1971, s. 7 as amended by the Law of Property (Miscellaneous Provisions) Act 1989, Scheds. 1 and 2.
[56] *Harmer* v. *Armstrong* [1934] Ch. 65.
[57] *Elbinger Actiengesellschaft* v. *Claye* (1873) LR. 8 Q.B. 313, at p. 317.
[58] *Teheran-Europe Co. Ltd.* v. *S. T. Belton (Tractors) Ltd.* [1968] 2 Q.B. 545.
[59] *Ibid.*, at pp. 553, 558, 562. See also *Tudor Marine Ltd.* v. *Tradax Export S.A.* [1976] 2 Lloyd's Rep. 135.
[60] Bills of Exchange Act 1882, ss. 23, 89. [61] *Ibid.*, s. 91. See also Companies Act 1985, s. 37.
[62] *Welsh Development Agency* v. *Export Finance Co.* [1992] B.C.L.C. 148 at pp. 173, 182.

counter to the generally accepted principles of privity of contract.[63] But it would seem to serve a useful commercial purpose, and is further subject to the qualification that the authority must have been in existence at the time the contract was made. As we have seen, it is not possible to ratify a contract unless the principal is named therein, or is at any rate identifiable. Otherwise it would be open to any stranger to intervene and sue.[64]

Limits of intervention

But the right of the undisclosed principal to intervene as a contracting party is subject to certain limitations.[65]

Agent must not have contracted as principal

First, intervention is excluded if the contract is in terms which import that the agent is the real and only principal, for then the idea of agency is incompatible with the terms of the contract. Thus, in *Humble* v. *Hunter*,[66] where an agent in making a charterparty described himself therein as 'owner' of the ship, it was held that evidence was not admissible to prove that another person was the real owner and that he was merely acting as agent on his behalf. His principal could not intervene, nor, by parity of reasoning, could he be sued. On the other hand, where the agent was described as 'charterer',[67] 'landlord',[68] 'tenant',[69] and even 'disponent owner',[70] evidence has been admitted to show who the real principal was. It may be that in modern law intervention of the principal will only be excluded by descriptive words where such intervention would clearly be inconsistent with the object and intent of the contract.[71]

Personality of agent must be essential

Secondly, where the personality of the agent is of such importance that the contract must be taken to have been made with that person alone, no one else can interpose and adopt the contract.[72] For example, in the case where there is an agreement to write a book,[73] or to underwrite shares in a company,[74] or to purchase goods subject to a right of set-off,[75] if the agent contracts in its own name without disclosure of the agency, the principal cannot intervene. Of course, if the third party subsequently discovers the identity of the principal, and with an

[63] Pollock (1888) 3 L.Q.R. 359; Ames, *Lectures on Legal History*, p. 453. In continental systems the absence of the doctrine of privity of contract makes such a principle commercially unnecessary. Cf. Müller-Freienfels (1953) 16 M.L.R. 299. Arguably, it can, however, be regarded as a form of assignment: see *Siu Yin Kwan* v. *Eastern Insurance Co. Ltd.* [1994] 2 A.C. 199 at p 209.

[64] *Keighley, Maxstead & Co.* v. *Durant* [1901] A.C. 240; *ante*, p. 625.

[65] See Goodhart and Hamson (1932) 4 C.L.J. 320.

[66] (1848) 12 Q.B. 310. See also *Formby* v. *Formby* (1910) 102 L.J. 116 ('proprietor'); *Asty Maritime Co. Ltd. and Panagiotis Stravelakis* v. *Rocco Guiseppe & Figli, S.N.C. (The Astyanax)* [1985] 2 Lloyd's Rep. 109 ('disponent owner').

[67] *Drughorn (Fred.) Ltd.* v. *Rederiaktiebolaget Transatlantic* [1919] A.C. 203.

[68] *Epps* v. *Rothnie* [1945] K.B. 562.

[69] *Danziger* v. *Thompson* [1944] K.B. 654.

[70] *O/Y Wasa S.S. Co.* v. *Newspaper Pulp and Wood Exports* (1949) 82 Ll. L.R. 936. Cf. *Asty Maritime Co. Ltd. and Panagiotis Stravelakis* v. *Rocco Guiseppe & Figli, S.N.C. (The Astyanax)* (*supra*, n. 66).

[71] See e.g., *J. H. Rayner (Mincing Lane) Ltd.* v. *Department of Trade and Industry* [1989] Ch 72 at pp. 190–1 and *Welsh Development Agency* v. *Export Finance Co.* [1992] B.C.L.C. 148 at pp. 159.

[72] But see *Said* v. *Butt* [1920] 3 K.B. 497, *ante*, p. 313. Cf. *Dyster* v. *Randall & Sons* [1926] Ch. 932.

[73] *Boulton* v *Jones* (1857) 2 H. & N. 564, *per* Bramwell B. at p. 566.

[74] *Collins* v. *Associated Greyhound Racecourses Ltd.* [1930] 1 Ch. 1.

[75] *Boulton* v. *Jones* (*supra*, n. 73), *ante*, p. 311; *Greer* v. *Downs Supply Co.* [1927] 2 K.B. 28.

opportunity of affirming or rejecting the contract, elects to affirm it, as, for example, by retaining goods purchased, the third party will be bound to the principal, but not otherwise.[76]

Set-off

In any case, a person who contracts with an agent, honestly and reasonably believing the agent to be the principal party to the transaction, is entitled to set up against the principal, when discovered, any set-off which is available against the agent, and which accrued before the person knew that the party with whom the contract was made was in fact an agent.[77] This rule rests upon the doctrine of estoppel.[78] But a person who has not been misled cannot claim such a set-off. So in a case where a man dealt with brokers whom he knew to be in the habit of selling, sometimes as brokers for principals, and sometimes on their own account, he could not set off his indebtedness to the brokers against his debt to the principal.[79]

Election on discovery

Upon discovering the principal, the other contracting party may elect to sue either the agent or the principal. Any act which unequivocally indicates the adoption of either principal or agent as the party liable determines the election, and the contracting party cannot afterwards sue the other.[80]

Law of Property (Miscellaneous) Provisions) Act 1989, s. 2(3)

A contract for the sale or other disposition of land must be in writing 'signed *by or on behalf* of each party to the contract'.[81] Although, as we have noted, the contract to which the undisclosed principal is a party is generally normally considered not to be separate from the contract between the agent and the other party,[82] the sub-section would seem to preclude an undisclosed or an unnamed principal from suing or being sued on contracts signed by their agents.[83] But the Law Commission's Working Paper stated that 'plainly agents should be permitted to sign on behalf of the parties' and that it was intended to 'let the ordinary principles of agency operate',[84] and the Commission's Report indicates that its recommendations were made on this basis.[85] So, it is arguable that, as was the case before the enactment of the 1989 Act,[86] an agent signs 'on behalf of' the principal whenever the contract is signed with authority and the agent intends to act on behalf of the principal.

(b) Misrepresentation or Non-Disclosure by the Agent

Misrepresentation of agent a ground for rescission

When a contract is made through an agent, a misrepresentation by the agent or, if the contract is one *uberrimae fidei*, the agent's failure to disclose a material fact renders the contract voidable by the other party just as would misrepresentation

[76] *Greer* v. *Downs Supply Co.* [1927] 2 K.B. 28, at p. 33.
[77] *Isberg* v. *Bowden* (1853) 8 Exch. 852, at p. 859; *Montagu* v. *Forwood* [1893] 2 Q.B. 350.
[78] *Cooke* v. *Eshelby* (1887) 12 App. Cas. 271, *per* Lord Watson at p. 278.
[79] *Cooke* v. *Eshelby* (*supra*, n. 78).
[80] *Scarf* v. *Jardine* (1882) 7 App. Cas. 345. Cf. *Clarkson Booker Ltd.* v. *Andjel* [1964] 2 Q.B. 775; *Pyxis Special Shipping Co. Ltd.* v. *Dritsas & Kaglis Bros. Ltd.* [1978] 2 Lloyd's Rep. 380 (institution of legal proceedings not conclusive). See Reynolds (1970) 86 L.Q.R. 318.
[81] *Ante*, p. 81.
[82] *Welsh Development Agency* v. *Export Finance Co.* (*ante*, n. 62).
[83] See *Bowstead and Reynolds on Agency*, 16th edn. (1996), p. 363.
[84] Law Com. W.P. No. 92 (1985), § 5.16.
[85] Law Com. No. 164 (1987), § 4.8.
[86] *Basma* v. *Weekes* [1950] A.C. 441, at p. 454, on the Law of Property Act 1925, s. 40.

or non-disclosure on the part of the principal. The other contracting party may rescind the agreement, or set up the misrepresentation as a defence to an action for specific performance or otherwise. So far as concerns the invalidation of the contract, it makes no difference with what state of mind the representation was made.[87] That question only becomes relevant when the issue arises as to the liability of the principal in damages for deceit or negligence, or under section 2(1) of the Misrepresentation Act 1967.[88]

Liability of principal in deceit

A principal who expressly authorizes an agent to make a statement which the principal knows to be false, or who knows that the agent has made or will make such a statement, yet deliberately does not intervene, will be liable in deceit. So, for example, a landlord who knows of facts which would deter a prospective tenant from taking a lease of a house, and deliberately employs an agent in order that it might be innocently represented that the house is sound, will be liable to an action for damages for fraud.[89] A principal is also responsible for fraudulent misrepresentations made by the agent in the course of its employment under the normal rules of vicarious liability.[90]

Is knowledge of falsity by agent to be attributed to principal?

One of the most difficult problems, however, is to know how far the knowledge of the agent that the representation is false can be attributed to the principal. In general it is true to say that where the state of mind of a party to a contract is material, the law regards the principal and agent as one.[91] Thus in a contract *uberrimae fidei*, if there is a failure to disclose material facts which are known to the agent but not to the principal, or vice versa, the contract may be avoided.[92] But this formula is correct only 'where the employment of the agent is such that in respect of the particular matter in question, he really does represent the principal'.[93] So, if, for example, the agent of an insurance company assists the proposer by filling in the proposal form, and does so in such a way as to mislead the company, the policy is voidable by the company. No knowledge of the inaccuracies will be attributed to the company, for the agent is not employed by them to fill in proposal forms; but knowledge will be attributed to the proposer, for the company's agent became the proposer's agent for the matter in question.[94]

Also in *Blackburn, Low & Co.* v. *Vigors*:[95]

A principal effected a policy of insurance on a ship through a broker, X, neither of them being aware of any material fact not disclosed to the insurers. The principal had, however, previously employed another broker, Y, to negotiate a policy on the same ship, and Y had accidentally, and before effecting the insurance, learnt of a material fact which he had not

[87] See *ante*, p. 246. [88] See *ante*, p. 243. [89] *Ludgater* v. *Love* (1881) 44 L.T. 694.
[90] *Lloyd* v. *Grace, Smith & Co.* [1912] A.C. 716.
[91] *Pearson (S.) & Son Ltd.* v. *Dublin Corporation* [1907] A.C. 351 (principal believes to be true, but agent knows to be false).
[92] *Blackburn, Low & Co.* v. *Vigors* (1887) 12 App. Case. 531., at p. 541.
[93] *Ibid.*, *per* Lord Halsbury at p. 538.
[94] *Biggar* v. *Rock Life Assurance Co. Ltd.* [1902] 1 K.B. 516; *Newsholme Bros.* v. *Road Transport etc. Insurance Co. Ltd.* [1929] 2 K.B. 365. Cf. *Stone* v. *Reliance Mutual Insurance Socy.* [1972] 1 Lloyd's Rep. 463.
[95] (1887) 12 App. Cas. 531. This case was decided before the Marine Insurance Act 1906: *ante*, p. 259.

disclosed to his principal. The principal sued on the policy of insurance effected by X, but the insurers disclaimed liability on the ground that Y's knowledge ought to be imputed to the principal, and that this knowledge would vitiate the policy effected by the innocent X.

The House of Lords refused to accept this defence, holding that no knowledge could be imputed because Y's agency had been determined before the policy sued on had been effected.

No deceit where 'innocent division of ingredients'

But even where the knowledge of the principal and agent can be treated as one, in order for an action in *deceit* to lie, it must be shown that one of the two was dishonest. If, upon examination, the facts resolve themselves into an 'innocent division of ingredients',[96] no deceit will be established. An innocent state of mind on the part of the agent cannot be added to an innocent state of mind on the part of the principal so as to produce fraud. This is clearly shown by *Armstrong* v. *Strain*:[97]

The defendant employed a firm of estate agents to sell his bungalow for him. One Skinner, a member of the firm, represented to the plaintiff that 'any building society would lend £1,200 on it', that is, that it was a property of considerable value. In fact, this was quite untrue as the bungalow had been underpinned several times to prevent it from falling down. The defendant knew that the bungalow was in poor condition, but he did not authorize Skinner to make the representation, nor did he deliberately employ him with that end in view. Skinner himself had no knowledge of the underpinning. The plaintiff bought the bungalow on the faith of the representation and, on discovering the underpinning, sued for damages for fraud.

The action failed. The trial judge, Devlin J.,[98] found that there was no fraud intended either by the defendant or by his agent. Although the defendant knew facts which falsified the agent's representation, this did not make him guilty of deceit. The intentions of both principal and agent were quite innocent, and it was not possible to put them together to produce fraud. This decision was upheld by the Court of Appeal.

or negligence

It is a moot point how far these same principles would apply if a third party sought to make the principal liable in damages for negligent misstatement or under section 2(1) of the Misrepresentation Act 1967.[99] Both at common law and under the Act,[100] the principal may be liable in damages for a misrepresentation made by the agent, acting within the scope of its authority, as if the misrepresentation had been made by the principal. Although the misrepresentation may have been made by the agent without negligence and with reasonable ground to believe and belief in its truth, it may be that knowledge or means of knowledge on the part of the principal, or of a fellow agent or of an employee of the principal, of facts which would show the representation to be untrue would, in certain

[96] Devlin (1937) 53 L.Q.R. 344; *Armstrong* v. *Strain* [1951] 1 T.L.R. 856, *per* Devlin J. at p. 871.

[97] [1952] 1 K.B. 232. See also *Cornfoot* v. *Fowke* (1840) 6 M. & W. 358; *Gordon Hill Trust* v. *Segall* [1941] 2 All E.R. 379. Cf. *London County Freehold and Leasehold Properties Ltd.* v. *Berkeley Property and Investment Co. Ltd.* [1936] 2 All E.R. 1039, which must now be explained as a case of an agent's fraud.

[98] [1951] 1 T.L.R. 856.

[99] See *ante*, pp. 242–3.

[100] *Gosling* v. *Anderson* (1972) 223 E.G. 1743.

circumstances, be sufficient to render the principal liable in negligence or under the Act.[101]

(c) Settlement with the Agent

Does payment to agent discharge debt?

It often happens that either the principal or the third party incurs a debt to the other under a contract made through an agent. The principal or the third party thereupon settles with the agent, intending that the agent should pay across the money and so discharge the debt. Sometimes, however, the agent fails to do so, and makes away with the money or becomes bankrupt. Is the debtor then liable to pay over again? The answer will depend on whether it is the principal or the third party who is making the payment.

Payment by principal

Where the principal pays the agent, the general rule is that the principal is not discharged.[102] But where there are indications that the third party looks to the agent alone for payment and in consequence the principal settles with the agent,[103] or where the third party's conduct leads the principal to suppose that the debt has already been paid,[104] the third party is estopped from claiming to be paid over again. Normally, however, this is not the case. So in *Irvine & Co.* v. *Watson & Sons*:[105]

> The defendants employed C & Co. as agent and brokers to buy palm oil for them. C & Co. purchased the oil from the plaintiffs, revealing at the time of sale that they were buying for principals, but not stating the name of the principals. The terms of the sale were 'Cash on or before delivery'. It was not infrequent in the oil trade to require payment of a portion of the price before delivery, but it was not invariable, and in the present case no such demand was made. The oil was delivered, and, on delivery, the defendants paid the price to the brokers, not knowing that they had not paid the plaintiff. C & Co. stopped payment, and the plaintiffs sued the defendants for the price.

It was held that the defendants were liable. The plaintiffs knew that the brokers were contracting not on their own account but on behalf of principals, so that they did not look exclusively to the brokers for payment. Moreover, there was no conduct on their part which would estop them from suing for the price. It was not an invariable custom of the trade to insist on prepayment, and failure to do so would not therefore induce in the defendants a reasonable belief that payment had already been made.

A difficulty, however, arises in the case of an undisclosed principal. If an undisclosed principal pays the agent for the price of goods sold to it, there is authority for saying that, once the existence of the undisclosed principal is discovered, the seller cannot sue the undisclosed principal.[106] This decision proceeded on the ground that a demand for payment could not be made from 'those who were only discovered to be principals after they had fairly paid the price to those whom the

[101] Cf. Atiyah and Treitel (1967) 30 M.L.R. 369, at p. 374.
[102] *Irvine & Co.* v. *Watson & Sons* (1880) 5 Q.B.D. 414.
[103] *Smith* v. *Ferrand* (1827) 7 B. & C. 191.
[104] *Wyatt* v. *Hertford (Marquis of)* (1802) 3 East 147.
[105] (1880) 5 Q.B.D. 414. [106] *Armstrong* v. *Stokes* (1872) L.R. 7 Q.B. 598.

vendor believed to be the principals, and to whom alone the vendor gave credit'.[107] But this case is contrary to earlier authority,[108] and it was subsequently criticized by the Court of Appeal.[109] No estoppel could legitimately arise since the seller was unaware of the undisclosed principal's existence, and thus could not have induced it to settle with the agent. It may therefore be that it does not represent the law.

Payment by third party

If it is the third party who settles with the agent, again the general rule is that the third party is not discharged. The reason for this is that an agent who is authorized to sell is not necessarily authorized to accept the purchase money. In *Butwick* v. *Grant*:[110]

> The plaintiff through his agent, Chait, sold a quantity of sports-jackets to the defendant. After delivery, he sent in his account with his name printed on it. The defendant, however, paid Chait, who failed to deliver the money to the plaintiff. The plaintiff sued the defendant for the price of the jackets.

It was held that he was entitled to succeed as Chait had no authority to accept the money. Payment, however, to an agent who has such authority, either from an express mandate of the principal or in the ordinary course of business, will constitute a good discharge.[111] It would also seem that where the principal is undisclosed, payment to the agent before disclosure would be effective, for the principal has led the third party to believe that the agent is dealing on its own account.[112]

III. The Relations Between the Agent and Third Parties

Agent employed to establish privity of contract

An agent who is employed to establish privity of contract between the principal and a third party, in most instances will acquire no rights and incur no liabilities in respect of the contract which is entered in the capacity of agent. But 'it is not the law that, if a principal is liable, his agent cannot be',[113] and the agent may be found to have undertaken personal liability.[114] It is therefore our first task to discover the circumstances in which an agent may be under a personal liability.

(a) Personal Liability of the Agent

Agent contracts for named principal

Where an agent contracts, as agent, for a named principal, so that the other party to the contract looks through the agent to a principal whose name is disclosed, it

[107] At p. 610.
[108] *Heald* v. *Kenworthy* (1855) 10 Exch. 739, at p. 745.
[109] *Irvine & Co.* v. *Watson & Sons* (1880) 5 Q.B.D. 414, *per* Bramwell L.J. at p. 417.
[110] [1924] 2 K.B. 483.
[111] *Howard* v. *Chapman* (1831) 4 C. & P. 508; *International Sponge Importers* v. *Watt* [1911] A.C. 279.
[112] *Curlewis* v. *Birkbeck* (1863) 3 F. & F. 894. Cf. *Drakeford* v. *Piercy* (1866) 7 B. & S. 515.
[113] *Yeung Kai Yung* v. *Hong Kong and Shanghai Banking Cpn* [1981] A.C. 787, *per* Lord Scarman at p. 795.
[114] See Reynolds (1969) 85 L.Q.R. 92.

may be laid down, as a general rule, that the agent drops out of the transaction so soon as the contract is made. The agent acquires neither rights nor liabilities.

Whether agent personally liable is question of construction

But this matter is always one of the proper construction to be put upon the conduct of the parties where the contract is oral, or upon the wording of the document and the surrounding circumstances if it is written.[115] There is nothing to prevent both principal and agent being severally liable on, and entitled to enforce, a contract which the agent has made on behalf of the principal, if that was the intention of the parties.[116] The agent may, for example expressly or impliedly undertake liability for payment,[117] or may be considered to have done so by trade usage.[118] Or the document in which the contract is written may give no indication that the agent was acting as such, although both parties knew this to be the case: 'Where a person signs a contract in his own name, without qualification, he is *prima facie* to be deemed to be a person contracting personally: and, in order to prevent this liability from attaching, it must be apparent from the other portions of the document that he did not intend to bind himself as principal.'[119]

But agent is liable in any event

There are, however, other cases in which the law holds an agent personally liable, even though the agent contracts on behalf of the principal.

(i) If party to a deed

First, an agent who is party to a deed is bound thereby even though described as agent,[120] except possibly where the agent is acting under a power of attorney.[121]

(ii) If signs negotiable instrument without qualification

Secondly, an agent who signs as party to a negotiable instrument, such as a bill of exchange or promissory note, either as drawer, indorser, or acceptor, will be personally liable even though words which describe the agent as such, or as filling a representative character, are added to the signature.[122] The agent must go even further and indicate clearly that the signature is only on the principal's behalf. Thus the addition of the words 'receiver',[123] 'executor',[124] or 'director'[125] will not

[115] *Chapman* v. *Smith* [1907] 2 Ch. 97, at p. 103. See also *Elpis Maritime Co. Ltd.* v. *Marti Chartering Co. Inc. (The Maria D)* [1992] 1 A.C. 21; *Punjab National Bank* v. *De Boinville* [1992] 1 W.L.R. 1138, at p. 1155.

[116] *The Swan* [1968] 1 Lloyd's Rep. 5, at pp. 13–14.

[117] *Hall* v. *Ashurst* (1833) 1 C. & M. 714; *Rusholme & Bolton, etc. Ltd.* v. *S. G. Read & Co.* [1955] 1 W.L.R. 146; *Format International Security Printers Ltd.* v. *Mosden* [1975] 1 Lloyd's Rep. 37; *Fraser* v. *Equitorial Shipping Co. Ltd.* [1979] 1 Lloyd's Rep. 103.

[118] *Fleet* v. *Murton* (1871) L.R. 7 Q.B. 126; *Perishables Transport Co.* v. *Spyropoulos* [1964] 2 Lloyd's Rep. 379.

[119] *2 Smith's Leading Cases*, 12th edn., p. 379; *Brandt (H.O.) & Co. Ltd.* v. *Morris (H. N.) & Co. Ltd.* [1917] 2 K.B. 784; *Hichens Harrison Woolston & Co.* v. *Jackson* [1943] A.C. 266, at p. 273; *Tudor Marine Ltd.* v. *Tradax Export S.A.* [1976] 2 Lloyd's Rep. 134. Cf. *The Santa Carina* [1977] 1 Lloyd's Rep. 478 (oral contract); *Seatrade Gronigen B.V.* v. *Geest Industries Ltd.* [1996] 2 Lloyd's Rep. 375 (signature had to be read in conjunction with other parts of document).

[120] *Appleton* v. *Binks* (1804) 5 East 148.

[121] Powers of Attorney Act 1971, s. 7(1), as amended by the Law of Property (Miscellaneous Provisions) Act 1989, ss. 1(8) and 4. This exception probably only applies where the principal is named in the deed: *Harmer* v. *Armstrong* [1934] Ch. 65.

[122] Bills of Exchange Act 1882, s. 26. Cf. *ibid.*, s. 17. See also Companies Act 1985, s. 349(4). Cf. *Bondina* v. *Rollaway Shower Blinds Ltd.* [1986] 1 W.L.R. 517.

[123] *Kettle* v. *Dunster and Wakefield* (1927) 43 T.L.R. 770.

[124] *Liverpool Bank* v. *Walker* (1859) 4 De G. & J. 24.

[125] *Elliott* v. *Bax-Ironside* [1925] 2 K.B. 301.

necessarily relieve the agent of liability; but such expressions as 'for and on behalf of X as agent', or '*per pro.*' will do so.[126]

(iii) If the principal is foreign

Thirdly, although there is no rule of law to the effect that an agent who contracts on behalf of a foreign principal will be personally liable, the fact that a principal is a foreigner may be of some weight in determining whether the mutual intention of the third party and the agent was that the agent should be personally liable to be sued as well as the principal, particularly if credit has been extended by the third party.[127]

(iv) If principal not in existence

Fourthly, an agent who contracts on behalf of a non-existent principal risks incurring personal liability on the contract so made. The case of *Kelner* v. *Baxter*[128] has previously been cited to show that a company cannot ratify contracts made on its behalf before it was incorporated. The same case also shows that the agent so contracting may incur liabilities which the company cannot assume by ratification. 'Both upon principle and upon authority', said Willes J.,[129] 'it seems to me that the company never could be liable upon this contract: and construing this document *ut res magis valeat quam pereat*, we must assume that the parties contemplated that the persons signing it would be personally liable'. But the question whether or not an agent who contracts on behalf of a non-existent principal is personally liable depends, at common law, upon the construction of the particular contract, and the signature of the contract may be such as to show that it was made with the principal alone, so that the agent acquires neither rights[130] nor liabilities[131] under the contract. There is certainly no rule of law that an agent is automatically a party whenever there is no principal capable of being bound by the agreement.[132] However, section 36C(1) of the Companies Act 1985[133] provides that a contract which purports to be made by or on behalf of a company at a time when the company has not been formed has effect, subject to any agreement to the contrary, as one made with the person purporting to act for the company or as agent for it, and he or she is personally liable on the contract accordingly. This provision applies whatever the form of the signature, i.e. whether the agent signs on behalf of the company or as the company itself.[134] It also seems that the person concerned can sue as well as be sued.

(v) Misrepresentation

Finally, an agent who, while acting on behalf of the principal, is guilty of deceit, will be liable in damages in tort. Although, in certain circumstances, such an agent may also be liable for negligent misstatement,[135] where the principal owes a duty

[126] *Elliott* v. *Bax-Ironside* [1925] 2 K.B. 301, *per* Scrutton L.J. at p. 307; Bills of Exchange Act 1882, ss. 25, 31(5).
[127] *Teheran-Europe Co. Ltd.* v. *S. T. Belton (Tractors) Ltd.* [1968] 2 Q.B. 545, at p. 558; see *ante*, p. 642.
[128] (1866) L.R. 2 C.P. 174.
[129] At p. 185.
[130] *Newborne* v. *Sensolid (Great Britain) Ltd.* [1954] 1 Q.B. 45.
[131] *Hollman* v. *Pullin* (1884) 1 Cab. & El. 254.
[132] *Black* v. *Smallwood* (1966) 117 C.L.R. 52 (Australia).
[133] Inserted by the Companies Act 1989, s. 130(4).
[134] *Phonogram Ltd.* v. *Lane* [1982] Q.B. 938.
[135] *Smith* v. *Eric S. Bush* [1990] 1 A.C. 831 (mortgagee's valuer); *Henderson* v. *Merrett Syndicates Ltd.* [1995] A.C. 145; *Resolute Maritime Inc.* v. *Nippon Kaiji Kyokai* [1983] 1 W.L.R. 857, at p. 861 (shipbrokers); *Dodds and Dodds* v. *Millman* (1964) 45 D.L.R. (2d) 472 (Canada).

of care to the third party, it has been stated that the existence of a further duty of care is not necessary for the reasonable protection of the third party and that 'caution should be exercised before the law takes the step of concluding . . . that an agent acting within the scope of his authority on behalf of a known principal, himself owes to third parties a duty of care independent of the duty of care he owes to his principal'.[136] But it has been held that an agent cannot, *as agent*, be made liable in damages under section 2(1) of the Misrepresentation Act 1967.[137]

Agency but not name of principal disclosed

An agent who contracts as agent, but does *not* disclose the name of the principal, is also, as a rule, not personally liable on the contract which is made. Yet here too, as where the name of the principal is disclosed, the matter is one of construction.[138] But, although there is a *prima facie* rule that the agent drops out of the transaction, the terms of the contract or trade usage may again indicate a contrary intention.[139]

(b) 'Agent' Acting as Principal

Agent revealing that it is principal

Is it possible for a person who has purported to contract as agent for an unnamed principal, to state that he or she is in fact the real principal? The answer is that this is possible, for if the other party to the contract was willing to take the liability of an unknown person, it is hard to suppose that the agent was the one person in the world with whom the other party was unwilling to contract. At any rate, the character or the solvency of the unnamed principal could not have induced the contract. Thus in *Schmaltz* v. *Avery*:[140]

The plaintiffs entered into a contract of charterparty with the defendant. The plaintiffs described themselves as 'agents of the freighter', and it was provided in the contract that, since they were contracting 'on behalf of another party' all personal liability on their part should cease when the cargo was shipped. They then revealed themselves as principals and sought to enforce the charterparty.

It was held that they were entitled to do so. In this case, the 'agent' was allowed to sue on the contract, and by the same token ought similarly to incur liability under it.

[136] *Gran Gelato Ltd.* v. *Richcliff (Group) Ltd.* [1992] Ch 560, *per* Nicholls V.-C. at p. 571 (solicitor). See also *McCullagh* v. *Lane Fox & Partners Ltd.* (1996) 49 Con. L.R. 124 (estate agent); Cane (1992) 108 L.Q.R. 539.

[137] *Resolute Maritime Inc.* v. *Nippon Kaiji Kyokai* [1983] 1 W.L.R. 857 (despite the fact that s. 2(1) provides that 'the person making the misrepresentation' is to be liable).

[138] *Fleet* v. *Murton* (1871) L.R. 7 Q.B. 126, at p. 131.

[139] *Southwell* v. *Bowditch* (1876) 1 C.P.D. 374, at p. 376; *Hichens, Harrison Woolston & Co* v. *Jackson & Sons* [1943] A.C. 266; *Perishables Transport Co.* v. *N. Spyropoulos (London) Ltd.* [1964] 2 Lloyd's Rep. 379.

[140] (1851) 16 Q.B. 655. See also *Harper & Co.* v. *Vigers* [1909] 2 K.B. 549. Cf. *Sharman* v. *Brandt* (1871) L.R. 6 Q.B. 720.

(c) Undisclosed Principal

Undisclosed principal

If the agent acts on behalf of a principal whose existence is not at the time disclosed (the 'undisclosed principal'),[141] the other contracting party, when on discovering the true facts, is entitled to elect whether to treat the principal or the agent as the party with whom the contract was made.

The reason for this rule is plain. If T enters into a contract with A, T is entitled at all events to treat A, the party with whom T supposed the contract was made, as liable. If T subsequently discovers that A is in fact the representative of P, T is entitled to choose whether to accept the actual state of things, and treat P as the party to the contract, or whether to adhere to the supposed state of things upon which the contract was entered, and continue to treat A as the party to it.

The liability of the agent continues until the other contracting party has done some act which unequivocally indicates that it regards the principal as the party solely liable.[142]

(d) Unauthorized Acts of the Agent

Agent acting without authority

Where a person purports to act as agent for a named principal but without any authority to do so, the party who was thus induced to enter into a contract has one of three remedies if damage has been suffered as a result.

Breach of warranty of authority

First, the other party may sue on a warranty of authority. This is an implied promise on the part of the professed agent that, in consideration of the other party entering into the contract, the professed agent warrants the existence of a principal and that the contract is within the authority conferred by that principal.[143]

This rule applies not only to transactions or representations which would result in contract, but also to any representation of authority whereby one induces another to act detrimentally.[144] It is immaterial that the agent had no knowledge or means of knowledge that it was acting without authority, for 'moral innocence, so far as the person who he has induced to contract is concerned, in no way aids that person or alleviates the inconvenience and damage which he sustains'.[145] Liability is based on a promise implied by law. The warranty is, moreover, a continuing warranty, and therefore the agent is liable even though the authority, though valid at the time of the contract, has, unknown to the agent, been determined, as by the death or mental incapacity of the principal.[146]

Deceit

Secondly, if the professed agent knew that it had not the authority which it was assumed to possess, it may be sued by the third party in an action for deceit.[147]

[141] See *ante*, p. 642.
[142] See *ante*, p. 644.
[143] *Collen* v. *Wright* (1857) 8 E. & B. 647; *Penn* v. *Bristol and West Building Society* [1997] 1 W.L.R. 1356.
[144] *Starkey* v. *Bank of England* [1903] A.C. 114.
[145] *Collen* v. *Wright* (*supra*, n. 143), *per* Willes J. at p. 657. See also *Suart* v. *Haigh* (1893) 9 T.L.R. 488 (H.L.); *Yonge* v. *Toynbee* [1910] 1 K.B. 215; *post*, p. 656.
[146] See *post*, pp. 655, 656.
[147] *Polhill* v. *Walter* (1832) 3 B. & Ad. 114; *ante*, p. 240.

Negligence

Finally, if the agent failed to take reasonable care in representing the existence or extent of its authority, it may be liable in damages for negligent misstatement.[148]

[148] *Hedley Byrne & Co. Ltd.* v. *Heller & Partners Ltd.* [1964] A.C. 465, disapproving (at p. 532) the decision to the contrary in *Heskell* v. *Continental Express* [1950] 1 All E.R. 1033. See also *Smith* v. *Eric S. Bush* [1990] 1 A.C. 831; *Caparo Industries Plc.* v. *Dickman* [1990] 2 A.C. 605; *Spring* v. *Guardian Assurance plc.* [1995] 2 A.C. 296; *White* v. *Jones* [1995] 2 A.C. 207; *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145. For a review of the litigation involving the Lloyd's names, see Cane in Rose, ed., *Consensus Ad Idem* (1996), p. 96.

23

Termination of Agent's Authority

An agent's authority may be terminated in one of two ways: (1) by act of the parties, and (2) by operation of law. In certain circumstances, however, it will be irrevocable, and, where the Commercial Agents Regulations 1993 apply, although the agent's *authority* can be terminated, there are restrictions on the principal's ability to terminate the agency contract.[1]

I. Modes of Termination

(a) Act of the Parties

Agreement

The relation of principal and agent is generally founded on mutual consent, and may be brought to a close by the same process which originated it, by agreement.

Revocation

It may also be determined, so far as the principal and the agent are concerned, by an express revocation on the part of the principal, or an express renunciation on the part of the agent, although this will not affect the rights of third parties under the doctrine of ostensible authority.[2] Agency is thus *prima facie* determinable unilaterally and at will, subject, of course, to any claim which either party may have for breach of contract.

The principal may expressly or impliedly contract not to revoke the agent's authority during a fixed period, or until the agent has carried out the act which has been authorized. In such a case the authority is sometimes loosely said to be 'irrevocable', but this is incorrect. The authority will be effectively revoked, at least from the time that the agent 'accepts' the revocation as a repudiatory breach.[3] But the principal will be compelled to pay the agent damages for breach of contract, or to provide an indemnity against any liability already incurred. The revocation is therefore effective, but unlawful.

The notice of the revocation may be given in any form, even if the original authority was conferred by deed,[4] and it can take effect immediately unless the

[1] The Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053) (as amended by S.I. 1993 No. 3173), regs. 14–15, 17.

[2] *Ante*, p. 627.

[3] Cf. *Atlantic Underwriting Agencies Ltd.* v. *Cia. di Assicurazione di Milano S.p.A.* [1979] 2 Lloyd's Rep. 240 (non-acceptance of repudiatory breach; see *ante*, p. 536).

[4] *The Margaret Mitchell* (1858) Jur. N.S. 1193.

parties otherwise provide in the agreement. But where the agency is a continuing one, and analogous to a contract of service, the agent undertaking to serve the principal and the principal to pay for the services rendered, there is an implied term in the contract that the agency will not be revoked summarily, but only on reasonable notice.[5]

(b) Operation of Law

Determination by operation of law

There are certain circumstances which will put an end to the relationship of principal and agent by operation of law.

Insolvency

(i) Insolvency

The insolvency of either the principal[6] or the agent[7] will determine an agency for most purposes.

Frustration

(ii) Frustration

An agency which is created to deal with certain subject-matter will normally be frustrated by the destruction of that subject-matter.[8] So, for example, if an agent is employed to effect an insurance on a particular piece of property, and the property is destroyed by fire, the agency determines. Also on the outbreak of war, whether either the principal or the agent becomes an enemy, the authority of the agent normally ceases on the ground that it is not permissible to have relations with an enemy alien, and the existence of the relationship of principal and agent necessitates such a relation.[9] But this is not invariably the case, for the agency may be of such a kind (for example, a general power of attorney)[10] that it has no tendency to assist or increase the resources of the enemy.

Death

(iii) Death

The death[11] (or if the principal is a corporation, the dissolution)[12] of the principal determines at once the authority of the agent. The third party's remedy will be against the agent for breach of warranty of authority. It is not necessary for the agent to have notice of the death, so that there may be liability for such breach of warranty, even though the agent was ignorant of the fact that the authority had

[5] *Martin-Baker Aircraft Co. Ltd.* v. *Canada Flight Equipment Ltd.* [1955] 2 Q.B. 556.

[6] The principal's property will be vested in the trustee in bankruptcy and an agent generally cannot dispose of it. See Insolvency Act 1986, ss. 283–4, 307, 315, 436.

[7] *Beckham* v. *Drake* (1849) 2 H.L. Cas. 579. But only if the bankruptcy renders the agent unfit to perform his duties: *McCall* v. *Australian Meat Co.* (1870) 19 W.R. 188; *Bailey* v. *Thurstan & Co. Ltd.* [1903] 1 K.B. 137.

[8] *Rhodes* v. *Forwood* (1876) 1 App. Cas. 256. Cf. *Turner* v. *Goldsmith* [1891] 1 Q.B. 544; *ante*, p. 640.

[9] *Sovfracht (v/o)* v. *Van Udens Scheepvaart en Agentuur Maatschappij (N.V. Gebr.)* [1943] A.C. 204, at pp. 253–5, where doubt was cast on the correctness of the decision in *Tingley* v. *Müller* [1917] 2 Ch. 144. See also *Stevenson (Hugh) & Sons Ltd.* v. *Aktiengesellschaft für Cartonnagen-Industrie* [1918] A.C. 239. Cf. *Schostall* v. *Johnson* (1919) 36 T.L.R. 75 (enemy resident in England).

[10] *Hangkam Kwingtong Woo* v. *Liu Lan Fong* [1951] A.C. 707.

[11] *Campanari* v. *Woodburn* (1854) 15 C.B. 400.

[12] *Salton* v. *New Beeston Cycle Co.* [1900] 1 Ch. 43.

been determined by the death and had no means of finding out that this was so.[13] The representatives of a deceased principal may, however, ratify any contract entered into on behalf of the estate,[14] but they are in no way bound to do so.

A statutory qualification exists in the case of powers of attorney. A donee of a power of attorney who acts in pursuance of the power in ignorance of the death of the donor incurs no liability (either to the donor or to any other person) by reason of the fact that the power has been revoked by the death.[15]

The death of the agent also determines the agency[16] but where the Commercial Agents Regulations apply, compensation may be due where the agency is terminated in this way.[17]

(iv) Mental incapacity

Mental incapacity

The effect of the mental incapacity of the principal is a matter of some difficulty at common law.[18] In *Yonge* v. *Toynbee*:[19]

> The defendant, after instructing solicitors to defend on his behalf a threatened action, became insane before the action was heard. The solicitors, in ignorance of this fact, duly entered an appearance to the writ, and took all necessary steps on their client's behalf. When the defendant's insanity became known to the plaintiff, he sought to have the appearance and all subsequent proceedings struck out, and to make the solicitors personally liable for the costs incurred, on the ground that their authority to act had been determined by the defendant's insanity.

The Court of Appeal decided in the plaintiff's favour, holding that the solicitors had warranted an authority which they had ceased to possess. On the other hand, in *Drew* v. *Nunn*:[20]

> The defendant, being sane, held out his wife to have authority to deal with the plaintiff on his behalf. He subsequently became insane, but the wife continued to deal with the plaintiff who had no notice of the defendant's insanity. The defendant recovered, and sought to resist an action against him for the price of the goods supplied to his wife during the period of his insanity.

This defence did not succeed. The Court of Appeal did not expressly decide how far the disability affected the continuance of authority, but held that 'the defendant, by holding out his wife as agent, entered into a contract with the plaintiff that she had authority to act on his behalf, and that until the plaintiff had knowledge that this authority was revoked he was entitled to act on the defendant's representations'.[21]

[13] *Blades* v. *Free* (1829) 9 B. & C. 167; *Yonge* v. *Toynbee* [1910] 1 K.B. 215. Cf. *Smout* v. *Ilbery* (1842) 10 M. & W. 1.
[14] *Re Watson* (1886) 18 Q.B.D. 116.
[15] Powers of Attorney Act 1971, s. 5(1) (5). But see *post*, p. 658.
[16] *Friend* v. *Young* [1897] 2 Ch. 421.
[17] Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053), reg. 17(8).
[18] See *post*, p. 658 for the effect of the Enduring Powers of Attorney Act 1985.
[19] [1910] 1 K.B. 215.
[20] (1879) 4 Q.B.D. 661.
[21] (1879) 4 Q.B.D. 661, *per* Brett L.J. at p. 669. See also *Re Parks* (1957) 8 D.L.R. (2d) 155 (Canada).

These two cases can be reconciled on the ground that, although mental incapacity puts an end to the agency as between principal and agent, it can have no effect on third parties who continue to contract in the belief that the agency is still in existence. The principal is estopped from denying the authority of the agent unless and until the third party becomes aware of the revocation. Nevertheless the decision in *Yonge* v. *Toynbee* does produce a somewhat curious result, for, as we have seen,[22] if a person contracts with a mentally incapacitated person, the contract is good unless, at the time of contracting that person was aware of the disability. But if a contract is made by a third party with an incapacitated person through an agent, and no question of estoppel arises, the contract is void, even though the third party had no knowledge of the disability. Further, if two persons make a binding contract, and one of them, subsequently unknown to the other, becomes mentally disabled, the contract is not in general avoided by that event. *Yonge* v. *Toynbee*, however, obliges us to say that if the contract is one of agency, it will be an exception to this general principle. There is also the additional difficulty that, if the principal is estopped from denying the contract which the agent purported to make for the principal it is hard to see how there can have been a breach of the agent's warranty of authority at all, or if it has been technically broken, what damage the third party has suffered, since the third party's rights against the principal are exactly what the agent professed to be able to create. The decision in *Yonge* v. *Toynbee* requires reconsideration.[23]

The mental incapacity of the agent would also seem to determine the agency.

II. Irrevocable Authority[24]

Revocation precluded

THE authority given to an agent may become irrevocable in three main instances: (a) when it is coupled with an interest, (b) when it is contained in a power of attorney, (c) when revocation would cause the agent personal loss. Additionally, as indicated *supra*, where the Commercial Agents Regulations 1993 apply, although the agent's *authority* can be terminated, there are restrictions on the principal's ability to terminate the agency contract, at least without compensation.

(a) Authority Coupled With an Interest

Cases where agent acquires interest

An authority coupled with an interest is irrevocable during the subsistence of the interest. This rule has been explained by Wilde C.J. to mean that 'where an agreement is entered into on a sufficient consideration, whereby an authority is given for the purpose of securing some benefit to the donee of the authority, such an authority is irrevocable'.[25] So where a principal and agent agree for valuable consideration or under seal that the agent is to have authority, for example, to

[22] *Ante*, p. 230.
[23] See Law Commission Working Paper No. 69 (1976).
[24] Reynolds in Cranston, ed., *Making Commercial Law* (1997), p. 259.
[25] *Smart* v. *Sandars* (1848) 5 C.B. 895, at p. 917.

collect rents in order to secure a loan,[26] or to sell certain land and discharge a debt owed to the agent by the principal out of the purchase money,[27] the principal thereby confers an interest on the agent, and the agency cannot be revoked unilaterally by the principal, or by the death, incapacity, or insolvency of the principal.[28]

But the authority must be given with the object of protecting or securing an interest of the agent, and it is not sufficient that it does so incidentally. Thus in *Smart* v. *Sanders*:[29]

> The defendants, who were corn factors, were entrusted by the plaintiffs with certain wheat to sell on their behalf. They subsequently advanced the sum of £3,000 to the plaintiffs, which the plaintiffs failed to repay. The plaintiffs gave orders that the wheat was not to be sold, but the defendants nevertheless sold it to secure their advance.

In an action against them, the defendants pleaded that the agency, being coupled with an interest, was irrevocable; but the Court held that this was an improper application of the rule. The authority had not been given to secure the advance of £3,000, since it had been given prior to, and independently of, the loan.

(b) Powers of Attorney

Powers of attorney

An instrument creating a power of attorney must be made under seal.[30] Where a power of attorney is expressed to be irrevocable and is given to secure a proprietary interest of the donee of the power, or the performance of an obligation owed to the donee, then, so long as the donee has that interest or the obligation remains undischarged, the power cannot be revoked by the donor without the consent of the donee, or by the death, incapacity, insolvency, winding-up, or dissolution of the donor.[31]

If a power of attorney is effectively revoked, the donee of the power does not incur any liability, either to the donor or to any third party, if at the time the donee of the power does not know of the revocation.[32] Similarly, where a third party, without knowledge of the revocation, deals with the donee of the power, the transaction between them is treated as valid as if the power was still then in existence.[33]

Enduring powers of attorney

Subject to the statutory provisions outlined above, at common law a power of attorney is automatically revoked upon the donor becoming mentally incapable. Many powers of attorney are given just because of this possibility, but at a time when the assistance of the attorney became essential if the donor's affairs were to be managed properly, the attorney lost its authority to act.[34] The inconvenience of this led to the enactment of the Enduring Powers of Attorney Act 1985, which

[26] *Spooner* v. *Sandilands* (1842) 1 Y. & C. Ch. 390. Cf. *Doward, Dickson & Co.* v. *Williams & Co.* (1890) 6 T.L.R. 316 (no security).
[27] *Gaussen* v. *Morton* (1830) 10 B. & C. 731.
[28] *Quaere* whether the agency persists despite the dissolution of a principal which is a company.
[29] (1848) 5 C.B. 895.
[30] Powers of Attorney Act 1971, s. 1(1) as amended by the Law of Property (Miscellaneous Provisions) Act 1989, s 1.
[31] 1971 Act, s. 4.
[32] *Ibid.*, s. 5(1).
[33] *Ibid.*, s. 5(2)-(7). See also *ibid.*, s. 6 (share transactions).
[34] Law Com. No. 122, *The Incapacitated Principal* (1983), § 3.2.

allows such powers of attorney to be given if the requirements of the Act are followed. For example, the person giving the power must understand the nature of the juristic act at the time the power is given, a prescribed form (in which the powers of the donee are explained) must be followed, and following the incapacity of the donor, the donor is required to apply to the Court of Protection to register the power.[35]

(c) Agent's Personal Liability or Loss

Agent would incur personal liability or loss

Where the agent has, in pursuance of its authority, contracted a personal liability or become liable to personal loss, the agency cannot be revoked by the principal without the agent's consent, for this would be to defeat rights already established.

The liability incurred by the agent may either be a legal liability, as where the agent is bound by contract to pay to a creditor of the principal a debt which the agent has been authorized to receive;[36] or it may simply be a loss which is likely to occur in fact. Thus in *Seymour* v. *Bridge*:[37]

The defendant employed the plaintiffs, who were stockbrokers, to buy shares for him according to the rules of the Stock Exchange. They purchased the shares from a jobber in the usual way, but the defendant, before settling day, repudiated the transaction on the ground that the numbers of the shares had not been specified in accordance with Leeman's Act 1867.[38] This Act would indeed have invalidated the purchase, but the Stock Exchange forces its members to complete such bargains under pain of expulsion. The defendant must have been taken to have known of this rule as he contracted on that basis.

It was held that the plaintiffs' authority could not be revoked by the defendant so as to cause the plaintiffs actual loss, and that the defendant was bound to indemnify them for the money which they had paid for the shares.

The liability or loss must have been in the contemplation of the parties at the time that the authority was conferred.[39] Thus, where an investor did not know of the custom in *Seymour* v. *Bridge*, he was held, under circumstances in other respects precisely similar to those in that case, not to be bound to pay for the shares.[40] Also the principle does not apply where the contract entered into by the agent is not merely void, but illegal.[41]

(d) Commercial Agents

Commercial agents

Where the Commercial Agents Regulations[42] apply, the principal's freedom to terminate a commercial agency is restricted. If the contract is for an indefinite

[35] Enduring Powers of Attorney Act 1985, s. 2; Enduring Powers of Attorney (Prescribed Form) Regulations 1990 (S.I. 1990 No. 1376); *Re K* [1988] Ch. 310. See generally Cretney, *Enduring Powers of Attorney*, 3rd edn. (1991).

[36] *Hodgson* v. *Anderson* (1825) 3 B. & C. 842.

[37] (1885) 14 Q.B.D. 460.

[38] Banking Companies' (Shares) Act 1867, repealed by the Statute Law Revision Act 1966.

[39] *Read* v. *Anderson* (1884) 13 Q.B.D. 779, at p. 783.

[40] *Perry* v. *Barnett* (1885) 15 Q.B.D. 388.

[41] See *ante*, p. 393.

[42] The Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053) as amended by S.I. 1993 No. 3173.

period, minimum periods of notice are specified,[43] and, save where the termination is on the ground of the agent's breach, the agent is entitled to be compensated for damage.[44] It is arguable that under the Regulations compensation is calculated by reference to the commission the agent would have earned had the contract continued to be performed in the normal manner in which the parties had intended,[45] and not, as at common law, on the basis of the principal's acting to minimize its liability to the agent.[46] This right to compensation exists even where the principal's termination of the agency contract is not a breach of contract.[47]

[43] The Commercial Agents (Council Directive) Regulations 1993 (S.I. 1993 No. 3053) as amended by S.I. 1993 No. 3173, reg. 15 (one month for the first year of the contract, 2 months for the second year, and 3 months for the third and subsequent years). An agreement for a fixed period which continues to be performed after that period has expired is (reg. 14) converted into one for an indefinite period.

[44] *Ibid.*, regs. 17, 18(a), as amended.

[45] *Page* v. *Combined Shipping & Trading Co. Ltd.* [1997] 3 All E.R. 656.

[46] *Ante*, p. 565.

[47] 1993 Regulations, reg. 17(1)(6).