Freedom from Contract: Economic Duress and Unconscionability

by

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INTRODUCTION

Throughout the nineteenth century laissez-faire ideology permeated politics, economics, morality, and of course, the law. The twentieth century has seen the rise of socialism and the welfare state; the laissez-faire ideology has waned, and left its legal legacy — the classical common law theory of the freedom of contract — in a precarious and ambivalent position.[1]

On the one hand, there are recent dicta indicating a determination to adhere firmly to the doctrine of freedom of contract. Authoritative examples include *Photo Productions Ltd* v *Securicor*,[2] *The Chikuma*,[3] *Multiservice Bookbinding Ltd* v *Marden*,[4] and *Sports International Ltd* v *International Footwear Ltd*[5].

On the other hand, there are increasing numbers of authoritative decisions and dicta tending to undermine the freedom to contract. In *National Carriers Ltd* v *Panalpina (Northern) Ltd* (1981)[6] for example, Lord Wilberforce observed:

> The movement of the law of contract is away from a rigid theory of autonomy towards the discovery, or, I do not hesitate to say, imposition, by the Courts of just solutions, which can be ascribed to reasonable men in the position of the parties.

[1] G Gilmore, *The Death of Contract*, [1974]; P S Atiyah, *The Rise and Fall of Freedom of Contract* [1979].
[2] [1980] AC 827.
[3] [1981] 1 WLR 314.
[4] [1979] Ch 84.
[5] [1984] 2 All ER 321.
[6] [1981] AC 675, 696.

In *Lloyds Bank* v *Bundy*[7], Lord Denning noted that in "the vast majority of cases" the courts will not interfere with the freedom of contract. But, he continued, there are a number of categories of cases

> . . . in which the courts will set aside a contract, or a transfer of property, when the parties have not met on equal terms — when the one is so strong in bargaining power and the other so weak — that, as a matter of common fairness, it is not right that the strong should be allowed to push the weak to the wall.[8]

Lord Denning went on to consider those categories. He discussed duress, undue influence, unconscionability, "undue pressure",[9] and unjust salvage agreements.[10] He concluded that all these categories though traditionally regarded as distinct are in fact based on a "single thread", namely the principle of inequality of bargaining power:

> By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other.[11]

Thus Lord Denning claimed for the courts the power to rewrite any unfair bargain where there is inequality of bargaining power.[12]

In the ten years since *Lloyds Bank* v *Bundy* was decided Lord Denning's judgment has received no elaboration, little support,[13] and much criticism[14] particularly in two recent cases of high authority. His dicta have certainly not grown into a comprehensive body of law, and it seems unlikely that they will do so.[15] But Lord Denning's judgment should not be discounted. Lord Denning has shown that the freedom to enforce unfair contracts is so circumscribed that it is no longer (and perhaps never was) any more than half the story. And he has drawn attention to, and clarified, the other half — namely, that the circumstances in which a party may be freed from an unfair contract are

[7] [1975] QB 326.
[8] *Ibid*, 336–337.
[9] *Ormens* v *Beadel* [1860] 2 Giff 166; *D & C Builders Ltd* v *Rees* [1966] 2 QB 617.
[10] *Akerblom* v *Price* [1881] 7 QBD 129; *The Port Caledonia and The Anna* [1903] P 184.
[11] [1975] 1 QB 326, 339.
[12] For a dissection of the passage quoted see Slayton "The Unequal Bargain Doctrine", (1976) 22 McGill LJ, 94.
[13] *Clifford Davis Management Ltd* v *WEA Records Ltd* [1975] 1 All ER 237; *McKenzie* v *Bank of Montreal* (1975) 55 DLR (3d) 641; *Coleman* v *Myers* [1977] 2 NZLR 225, 332 CA *per* Cooke J.
[14] Goff and Jones (*Law of Restitution* (2nd ed 1978) 201) describe Lord Denning's views as "radical propositions which find little support in earlier precedent". The most recent, and the strongest, judicial criticisms of the principle of inequality of bargaining power are in *Alec Lobb (Garages) Ltd* v *Total Oil GB Ltd* [1985] All ER 303 CA, and *National Westminister Bank* v *Morgan* [1985] All ER 821.
[15] *Meates* v *AG* [1983] NZLR 308.
Gartside v *Sheffield Young & Ellis* [1983] NZLR 37.
Hedley Byrne v *Heller* [1964] AC 465.
Junior Books Ltd v *Veitchi Co Ltd* [1983] 1 AC 520.

not isolated exceptions but share the single thread of inequality of bargaining powers.

It is now generally accepted that the heyday of contract is over. It is giving way to tort[15] on one front, and restitution on the other. Professor Atiyah says that freedom of contract is disintegrating,[16] and Professor Gilmore says it is dead.[17] Freedom from contract is growing. Two especially fertile areas are economic duress and unconscionability.[18] This article looks at the recent cases. An attempt is made to place them in the context of the general decline of contract and the rise of statutory controls over contract.

ECONOMIC DURESS

Contracts entered into under duress are voidable by the coerced party. There are four well established categories of duress: (1) duress of the person; (2) improper application of legal process; (3) duress of goods; and (4) money paid to obtain the fulfilment of a duty. In addition, the law relating to duress of goods has opened the door to the concept of economic duress.

A threat to breach a contract can amount to duress. In *IA Sundell & Sons Pty Ltd* v *Emm Yannoulatos (Overseas) Pty Ltd*[20] the appellant had agreed to sell iron to the respondent at an agreed price. The appellant refused to deliver unless the respondent paid an extra £30 per ton above the contract price. The court accepted that "a compulsive threat . . . to refrain from performing merely a contractual duty"[21] could amount to duress.

A person who obtains a benefit from another by threatening not to contract with him in the future however is generally not liable to restore the benefit because the threat is not wrongful. High authority suggests that this is so even where the threat is made and the benefit procured by someone enjoying a monopoly. In *Smith* v *William Charlick Ltd*[22] the respondents faced the Australian Wheat Harvest Board. The Board, which enjoyed a monopoly, demanded from the respondents further monies for wheat already sold to and paid for by them. It threatened not to sell any more wheat to the respondents unless the demand was met. The respondents paid the monies demanded and sued for restitution. The High Court of Australia dismissed their claim on the ground that the payment was made:

[16] P S Atiyah, *The Rise and Fall of Freedom of Contract* (1979).
[17] G Gilmore, *The Death of Contract* (1974).
[18] The scope of the doctrine of undue influence may be expanding also: *Lloyds Bank Ltd* v *Bundy* [1975] QB 326; *National Westminster Bank* v *Morgan* [1985] All ER 821; *Tufton* v *Sperni* [1952] 2 TLR 516; *In Re Craig* [1971] Ch 95; *Hodson* v *Marks* [1971] Ch 892.
[19] Goff & Jones, *Law of Restitution* (2nd ed 1978) 163.
[20] (1956) 56 SR (NSW) 323, 328.
[21] *Ibid*, 328.
[22] (1924) 34 CLR 38

not in order to have that done which the Board was legally bound to do, but in order to induce the Board to do that which it was under no legal obligation to do.[23]

Eric Gnapp Ltd v *Petroleum Board*[24] was a similar case. The plaintiff had entered an unfair contract with the defendant because "there was no-one else with whom he could contract for the supply of the particular commodity he required".[25] But the English Court of Appeal held that none of the essential elements of duress was present[26] and gave no relief.

These decisions mark the high water mark. A series of more recent cases shows that the concept of economic duress has gained ground since the heyday of laissez-faire.

The defendants in *The Siboen and the Sibotre*[27] had chartered two ships from the plaintiff-owners. The defendants persuaded the owners to reduce the rate of hire. They achieved this by threatening to go bankrupt if the rates were not lowered. This threat was strongly coercive because the market had slumped and if the charterers returned the ships the owners would have had to lay them up. The charterers knew this. Kerr J expressed the view that it was possible in law for economic pressure to amount to duress.[28] On the facts, however, he declined to allow restitution on the ground of economic duress because the pressures to which the owners had been subject had been insufficient to "vitiate their will". (He allowed the plaintiffs to recover however on the alternative ground that the defendants' representation that they could not but default on the contract at the original rate was fraudulent.)

The Atlantic Baron[29] concerned a contract to build a ship. The shipbuilders demanded payments above the contract price without legal justification. They threatened to terminate the contract if their demands were not met. Mocatta J analysed the cases and concluded that duress "may take the form of economic duress" and that "a threat to break a contract may amount to such economic duress".[30] He held that the defendants' threat to break their contract had amounted to economic duress, and that the plaintiffs could have recovered the excess payment had their subsequent conduct not affirmed the variations to the contract.

The third case is *Pao On* v *Lau Yiu Long*.[31] The defendants complained that the plaintiffs had procured variations of complex existing contracts by threatening to breach them. The Privy Council acknowledged, obiter, that economic duress was possible in law, but held that it was not made out on the facts. Lord Scarman said:

[23] *Ibid*, 51 *per* Knox CJ
[24] [1949] 1 All ER 980
[25] *Ibid*, 986.
[26] *Idem*.
[27] [1976] 1 Lloyds Rep 293.
[28] *Ibid*, 334–336.
[29] [1978] 3 All ER 1170.
[30] *Ibid*, 1182.
[31] [1979] 3 All ER 65.

> It is, therefore, unnecessary for the Board to embark on an enquiry into the question whether English law recognizes a category of duress known as 'economic duress'. But, since the question has been fully argued in this appeal, their Lordships will indicate very briefly the view which they have formed. At common law money paid under economic compulsion could be recovered in an action for money had and received: see *Astley* v *Reynolds*. The compulsion had to be such that the party was deprived of 'his freedom of exercising his will'. It is doubtful, however, whether at common law any duress other than duress to the person sufficed to render a contract voidable; see Blackstone's Commentaries and *Skeate* v *Beale*. American law (Williston on Contracts) now recognizes that a contract may be avoided on the ground of economic duress.The commercial pressure alleged to constitute such duress must, however, be such that the victim must have entered the contract against his will, must have had no alternative course open to him, and must have been confronted with coercive acts by the party exerting the pressure: see Williston on Contracts. American judges pay great attention to such evidential matters as the effectiveness of the alternative remedy available, the fact or absence of protest, the availability of independent advice, the benefit received, and the speed with which the victim has sought to avoid the contract. Recently two English judges have recognized that commercial pressure may constitute duress the pressure of which can render a contract voidable: see Kerr J in *The Siboen and the Sibotre* and Mocatta J in *The Atlantic Baron*. Both stressed that the pressure must be such that the victim's consent to the contract was not a voluntary act on his part. In their Lordships' view, there is nothing contrary to principle in recognizing economic duress as a factor which may render a contract voidable, provided always that the basis of such recognition is that it must amount to a coercion of will, which vitiates consent. It must be shown that the payment made or the contract entered into was not a voluntary act.[32]

The fourth and most recent case in this series is *Universe Tankships of Monrovia Ltd* v *International Transport Workers Federation*.[33] The defendant trade union "blacked" the plaintiff's ship and refused to let her sail unless the plaintiff paid £80,000, which it did.

The House of Lords by a majority allowed the plaintiff to recover on the ground of economic duress. Little was said as to the nature and ambit of economic duress generally, because (1) much of the plaintiff's argument was conceded, and (2) "the economic duress complained of was exercised in the field of industrial relations to which very special considerations apply".[34]

But Lord Diplock did confirm that a contract procured by economic duress is voidable and he offered an explanation for why this is so:

> It is not that the party seeking to avoid the contract which he has entered into with another party, or to recover money that he has paid to another party in response to a demand, did not know the nature or the precise terms of the contract at the time when he entered into it or did not understand the purpose for which the payment was demanded. The rationale is that his apparent consent was induced by pressure exercised upon him by that other party which the law does not regard as legitimate, with the consequence that the consent is treated in law as revocable unless approbated either expressly or by implication after the illegitimate pressure has ceased to operate on his mind. It is a rationale similar to that which underlies the avoidability of contracts entered into and the recovery of money exacted under colour of office, or under undue influence or in consequence of threats of physical duress.[35]

[32] *Ibid*, 79.

[33] [1982] 2 WLR 803. This case is usefully analysed by A J Steward "Economic Duress" (1984) 14 Melb. U. L. Rev.

[34] *Ibid*, 813 *per* Lord Diplock.

[35] *Idem*.

Lord Scarman and Lord Brandon of Oakbrook dissented, but Lord Scarman agreed with the majority that it was "already established law that economic pressure can in law amount to duress".[36]

The leading New Zealand case on economic duress is *Moyes & Groves Ltd* v *Radiation New Zealand*[37] which was decided by the Court of Appeal before the *Universe Tankships*[38] case came before the House of Lords. Cooke J, with whom Somers and Ongley JJ agreed, referred briefly to *Pao On* v *Lau Yiu Long*[39] and the cases discussed therein, and said:

> In the light of these and other authorities I would be prepared to accept that in New Zealand law economic duress can be a ground for avoiding liability under a contract. But it is certainly something which should not be found lightly.[40]

Economic duress was also discussed in *Aotearoa International* v *Scancarriers*.[41] The judgment of the Court of Appeal[42] was delivered by Cooke J. He repeated what was said in *Moyes & Groves*[43] and observed that the conduct alleged by the plaintiff to constitute economic duress was the defendant's standard practice, that both parties had had legal advice before entering into the settlement and that "the situation was a confused one." "Like the *Moyes & Groves* case" he concluded, "the present is an instance of a prudent and sensible compromise in good faith, with which there is insufficient ground for the Courts to interfere."

The decision of the Court of Appeal was reversed by the Judicial Committee of the Privy Council (which on this occasion included Sir Owen Woodhouse among its members) on the ground that there had never been a contract. Economic duress went entirely unmentioned. (Privy Council appeal no 9 of 1985, 18 July 1985.)

The ingredients and ambit of economic duress remain controversial.[44] But it is clear that the variation of a contract resulting from a threatened breach will not necessarily be voidable for duress. Duress leaves room for compromise and for submission to honest claims. Where the aggrieved party has adequate legal remedies, his submission to the threat may simply have been based upon a belief that his commercial interests would best be served by agreeing to vary the contract.

[36] *Ibid*, 828.
[37] [1982] 1 NZLR 368.
[38] [1982] 2 WLR 803.
[39] [1979] 3 All ER 65.
[40] [1982] NZLR 368, 372.
[41] A132/83, 28 September 1984, CA.
[42] At the time of writing an appeal to the Privy Council was pending.
[43] [1982] 1 NZLR 368
[44] A good discussion of the diversity of academic thought can be found in M H Oglivie, "Economic Duress, Inequality of Bargaining Power and Threatened Breach of Contract", (1981) 26 McGill L J 289. See also A J Stewart "Economic Duress" (1984) 14 Melb UL Rev 410.

UNCONSCIONABLE BARGAINS[45]

There are a number of well-established areas of the law where equitable relief is available against harsh or unconscionable bargains. The clearest examples are the rules relating to penalties and forfeiture. But it is unclear to what extent the courts have a general residuary jurisdiction to interfere with the freedom of contract on the ground that a contract (or part of it) is harsh or unconscionable. During the first three quarters of the twentieth century, the legacy of nineteenth century laissez-faire ideology inclined the courts to favour freedom of contract.

In England the doctrine of unconscionability remained dormant but it was applied by the New Zealand Court of Appeal in *Richardson* v *Harris*[46] in 1930, by the High Court of Australia in *Blomley* v *Ryan*[47] in 1956, and by the British Columbian Court of Appeal in *Morrision* v *Coast Finance*[48] in 1966.

The doctrine has received remarkably little elaboration. A landmark case was *Archer* v *Cutler*[49] where McMullin J asserted the Court's "jurisdication to set aside unconscionable bargains in the exercise of its general equitable jurisdiction". He reviewed the cases and set aside the contract before him on the ground that it was unconscionable.

The most recent authority is *Hart* v *O'Connor*.[50] O'Connor was a farmer. He sold his farm to Hart, and died soon after. His trustees sought to have the sale set aside. They argued that O'Connor had lacked the necessary mental capacity, and also that the contract was unconscionable.

Cook J in the High Court reluctantly decided that the defence of laches was established, and gave judgment for Hart.

The New Zealand Court of Appeal reversed the trial judge's finding of laches, set aside the contract for lack of capacity, and approved the views on unconscionability expressed by McMullin J in *Archer* v *Cutler*.

Hart appealed to the Privy Council and won. The contract was reinstated. The Judicial Committee delivered a lengthy opinion dealing almost exclusively with capacity. On this question *Hart* v *O'Connor* must now be regarded as the leading authority. The Privy Council decisively rejected *Archer* v *Cutler*, which New Zealand Courts (including the Court of Appeal in *Hart* v *O'Connor*) had taken as authority for the proposition that a contract by a person of unsound mind, whose incapacity is unknown to the other contracting party, can be avoided on the ground that it is "unfair" even where there is nothing reprehensible in the conduct of the other party. Their Lord-

[45] This section of this article draws heavily on P J Driscoll, *Unconscionability of Contract* (1982), a dissertation held by the Davis Law Library at the University of Auckland. See also S M Waddams, *The Law of Contracts* (1977).

[46] [1930] NZLR 890.

[47] (1956) 99 CLR 362.

[48] (1966) 54 WWR 257.
(1965) 55 DLR (2d) 710.

[49] [1980] NZLR 386, 402.

[50] [1983] NZLR 280. PC 56/84; reasons given 22 May 1985.

ships closely examined *Archer* v *Cutler* and the cases discussed therein, and concluded:

> In the opinion of their Lordships, to accept the proposition ennunciated in *Archer* v *Cutler* that a contract with a person ostensibly sane but actually of unsound mind can be set aside because it is "unfair" to the person of unsound mind in the sense of contractual imbalance, [ie inequality of exchange] is unsupported by authority, is illogical and would distinguish the law of New Zealand from the law of Australia, as exemplified in *McLaughlin*'s case and *Tremills*' case, for no good reason, as well as from the law of England from which the law of Australia and New Zealand and other "common law" countries has stemmed. In so saying their Lordships differ with profound respect from the contrary view so strongly expressed by the New Zealand Courts.
>
> To sum the matter up, in the opinion of their Lordships, the validity of a contract entered into by a lunatic who is ostensibly sane is to be judged by the same standards as a contract by a person of sound mind, and is not voidable by the lunatic or his representatives by reason of "unfairness" unless such unfairness amounts to equitable fraud which would have enabled the complaining party to avoid the contract even if he had been sane.

Their Lordships also concluded that the contract ought not to be set aside as an unconscionable bargain:

> This issue must also be answered in the negative, because Mr Hart was guilty of no unconscionable conduct. Indeed, as is conceded, he acted with complete innocence throughout. He was unaware of Jack's [ie O'Connor's] unsoundness of mind. . . . There was no equitable fraud, no victimisation, no taking advantage, no over-reaching or other description of unconscionable doings which might have justified the intervention of equity. . . . (pp 22–23 of the Advance Copy)

This may leave open the possibility that a contract properly procured may yet be impeached where the circumstances make it unconscionable to enforce it. This was not the case in *Hart* v *O'Connor* because the plaintiffs there were guilty of considerable delay.

The jurisdiction to set aside unconscionable contracts was recently confirmed by the unanimous decision of the High Court of Australia in *Commercial Bank of Australia* v *Amadio*.[51] It has also, belatedly and cautiously, regained the support of the English courts.[52]

The rule is that in some circumstances the courts will set aside a contract where one party was incapable of adequately protecting his interests and the other has made some immoderate gain at his expense. It applies even though both parties have capacity to contract at common law. The basis of equity's intervention is similar to that underlying the relief granted in cases of undue influence, but a bargain may be set aside even though there is no actual or presumed abuse of an existing relationship of confidence.[53] The doctrine is not limited to any particular type of transaction. Relief has been given from contracts involving

[51] (1983) 46 ALR 402.

[52] *Cresswell* v *Potter* [1978] WLR 255(n); *Multiservice Bookbinding* v *Marden* [1979] Ch 84; *Alec Lobb (Garages) Ltd* v *Total Oil GB Ltd* [1983] WLR 87, [1985] All ER 303.

[53] *Morrison* v *Coast Finance* (1966) 54 WWR 257, 259 *per* Davey JA.

land,[54] matrimonial property,[55] moneylending,[56] and chattels.[57] This list is not exhaustive.

The doctrine is based on a principle of inequality of bargaining power. Davey JA, in *Morrison* v *Coast Finance*, said:

> A plea that a bargain is unconscionable invokes relief against an unfair advantage gained by an unconscientious use of power by a stronger party against a weaker.[58]

In *Blomley* v *Ryan*, Fullagher J said:

> The circumstances adversely affecting a party, which may induce a court of equity either to refuse its aid or to set a transaction aside, are of great variety and can hardly be satisfactorily classified. . . . The common characteristic seems to be that they have the effect of placing one party at a serious disadvantage vis-a-vis the other.[59]

This statement was adopted with approval by McMullin J in *Archer* v *Cutler*,[60] and by the Court of Appeal in *O'Connor* v *Hart*.[61]

The requisite inequality may be due to various factors. There are a number of established categories. If the terms of a contract are unfair and the disadvantaged party can establish "weakness of mind", relief may be given, even though the mental weakness does not amount to lack of capacity.[62] A contract may also be unconscionable and unenforceable if one party obtained it by taking advantage of the other's drunkenness.[63] The same is true where the inequality is due to drugs other than alcohol.[64] The principle may also be applied where the complaining party is not drunk or drugged at the time of contracting but is nevertheless disadvantaged because of his generally dissolute lifestyle.[65] The courts have always set aside dispositions at an undervalue by elderly people who are unable to protect themselves adequately because of the eccentricities of old age or because they are easily led.[66] In *Richardson* v *Harris*[67] the Court of Appeal set aside the sale of a life interest at an undervalue on the ground that the vendor, a farm labourer, was hard-pressed by creditors. Emotional distress is another ground on which unfair contracts have been set aside.[68] This ground for relief

[54] *Blomley* v *Ryan* (1956) 99 CLR 362; *Archer* v *Cutler* [1980] 1 NZLR 386.
[55] *Moffat* v *Moffat* [1982] 1 NZFLR 129; *K* v *K* [1976] 2 NZLR 31; *Cresswell* v *Potter* [1978] 1 WLR 255(n).
[56] *Harris* v *Richardson* [1930] NZLR 890.
[57] *Buckley* v *Irvin* (1960) NI 98.
[58] (1966) 54 WWR 257, 259.
[59] (1956) 99 CLR 362 (HC Aust), at 405.
[60] [1980] NZLR 386, 402.
[61] [1983] NZLR 280, 290.
[62] *Archer* v *Cutler* [1980] 1 NZLR 386; *Buckley* v *Irwin* (1960) NI 98; *Wilton* v *Farnworth* (1948) 76 CLR 646.
[63] *Blomley* v *Ryan* (1956) 99 CLR 362 ("sodden with rum"); *Black* v *Wilcox* (1977) 70 DLR (3d) 192.
[64] *Fleury* v *Homocrest Dairy Co-op* (1958) 15 DLR (2d) 161.
[65] *Sag* v *Barwick* (1812) 1 V & B 195 (perpetual hangovers); *Dannage* v *White* (1818) 1 Swan 137.
[66] *Archer* v *Cutler* [1980] 1 NZLR 386; *Longmater* v *Leger* (1860) 2 Giff 157.
[67] [1930] NZLR 890.
[68] *Towers* v *Affteck* [1974] 1 WWR 714.

tends to arise particularly with regard to matrimonial property agreements.[69] Poverty and ignorance have long been relevant considerations.[70] In *Creswell* v *Potter*[71] Megarry J said that the requirements as to poverty were met where the plaintiff was "a member of the lower income group." He also stated that "ignorant" nowadays meant "less highly educated" (than whom, he did not say). Ignorance does not mean stupidity; perhaps "inexperienced" would be a less misleading word.[72] There are many cases in which relief has been granted to individuals who were not members of the dominant culture.[73] Finally, the principle also extends to those "who manage to pass through life blissfully unaware of economic realities, and are accordingly liable to be taken advantage of."[74]

Coming within one of the above categories is not sufficient. The plaintiff must show that as a result of being in the category he was put at a serious disadvantage vis-a-vis the other party. In *Ernestway Holdings Ltd* v *Joseph and James*[75] the plaintiff was in her nineties and clearly within the "little old lady" category, but the court refused restitution because it considered her unusually sharp and fully capable of looking after herself.

Nor is it necessary to come within one of the established categories, for it seems the categories of unconscionability are not closed. Professor Sheridan reviewed the cases and concluded:

> Probably the only safe generalization is that the court considers each case on its individual merits to see whether one party has taken advantage of the weakness or necessity of the other to an extent which strikes the judges as being a greater advantage than the current morality of the ordinary run of business men allows.[76]

Sullivan MR in one early case was content simply to say:

> If two persons, no matter whether a confidential relationship exists between them or not, stand in such a relation to each other that one can take an undue advantage of the other, whether by reason of distress or recklessness, or wildness or want of care and . . . one *has* taken undue advantage of the other, a transaction resting upon such unconscionable dealing will not be allowed to stand.[77]

The ambit and essential elements of the jurisdiction are not easy to define. As the Court of Appeal said in *O'Connor* v *Hart*, "unconscionability as a separate ground for avoiding a contract is a somewhat amorphous concept. Its metes and bounds are not clearly defined."[78]

[69] *Mundinger* v *Mundinger* (1968) 3 DLR (3d) 338; *K* v *K* [1976] 2 NZLR 31; *Moffat* v *Moffat* [1982] NZFLR 129; *Backhouse* v *Backhouse* [1978] WLR 243.
[70] *Fry* v *Lane* (1888) 40 ChD 312.
[71] [1978] WLR 255(n).
[72] *Backhouse* v *Backhouse* [1978] WLR 243.
[73] *Riki* v *Codd* (unreported), High Court, Napier, (A 59/78) Hardie Boys J (Maori); *De Koning* v *Boychuk* (1951) 3 DLR 624 (Dutch immigrants); *CBA* v *Amadio* (1983) 46 ALR 402 (Italian immigrants).
[74] P J Driscoll, *supra* at note 45; see also *Paris* v *Machnick* (1973) 32 DLR (3d) 723.
[75] (1978) Recent Law 161.
[76] *Fraud in Equity* (1956) 73.
[77] *Slater* v *Nolan* (1876) IR 11 Eq 367
[78] [1983] NZLR 280, 290.

In *Alec Lobb Ltd* v *Total Oil*[79] the contract was upheld because the weaker party failed to show "moral culpability" on the part of the stronger; but in *Archer* v *Cutler*[80] the contract was set aside, even though the Court exonerated the stronger party from anything in the nature of moral culpability. The cases differ as to whether the weaker party is required to prove that the stronger was aware of the inequality of bargaining power. In *Archer* v *Cutler* such knowledge was not required. In *Alec Lobb* "subjective" knowledge was required. In *Amadio*[81] knowledge was required but judged objectively. The significance of independent advice is unsettled. It is not even clear whether or not inequality of exchange is an essential element of unconscionability.[82]

PROFESSOR S M WADDAMS

An attractive context in which to assess *Lloyds Bank* v *Bundy*[83] and the recent cases on economic duress and unconscionability is the theory of contract presented by Professor Waddams. It is Waddams' thesis:

> . . . that the law of contracts, when examined, for what the judges do, as well as for what they say, shows that relief from contractual obligations is in fact widely and frequently given on the ground of unfairness, and that general recognition of this ground of relief is an essential step in the development of the law.[84]

Waddams says that the courts were reluctant to admit a general power of control over contracts because it was ideologically easier to accept freedom of contract as the general rule, and to see the areas of intervention as isolated "exceptions". He says that general principles of unreasonableness and unconscionability were originally widely used to justify interference with contracts, but that the principles became ossified as isolated categories of cases where relief would be given. This led to the enforcement of unconscionable agreements, and also, ironically, the striking down of reasonable agreements merely because they came within the categories where relief was available. For example in *Samuel* v *Jarrah Timber & Wood Paving Corp* relief was reluctantly given against "a perfectly fair bargain."[85]

Waddams discusses a number of areas where the courts grant relief against unconscionable bargains. The most obvious instances are the unconscionability doctrine,[86] forfeitures,[87] penalties,[88] deposits,[89] contracts in restraint of trade,[90] and cases of duress[91] and undue

[79] [1983] 1 WLR 87; [1985] 1 All ER 303.
[80] [1980] 1 NZLR 386.
[81] (1983) 46 ALR 402.
[82] *Blomley* v *Ryan* (1956) 99 CLR 362, 405 *per* Fullager J.73 (1966) 54 WWR 257.
[83] [1975] QB 326.
[84] S M Waddams, *The Law of Contracts* (1977) 266.
[85] [1904] AC 323, 325 *per* Lord Halsbury.
[86] *Idem.*
[87] *Shiloh Spinners Ltd* v *Harding* [1973] AC 691; *Stockloser* v *Johnson* [1954] 1 QB 476.
[88] *Dunlop Pneumatic Tyre Co Ltd* v *New Garage and Motor Co* [1915] AC 79.
[89] *Dunlop Pneumatic Tyre Co Ltd* v *New Garage and Motor Co* [1915] AC 79
[90] *Stockloser* v *Johnson* [1954] 1 QB 476.
[90] *A Schroder Music Publishing Ltd* v *Macaulay* [1974] 1 WLR 1308
[91] Goff and Jones, *Law of Restitution* 161-191.

influence.[92] The fundamental breach argument was another judicial attempt to control unfair contracts. As Lord Denning said in *Gillespie Bros* v *Roy Bowles Transport*:

> The judges . . . have never confessed openly to the test of reasonableness. But it has been the driving force behind many of the decisions.[93]

The same can be said of the cases relating to the incorporation of terms in documents (notices, tickets, etc). The law is supposed to be that terms are incorporated if the *notice* is reasonable, but it is apparent from the cases that a term is likely to be incorporated if the *term* is reasonable.[94] Judges have also provided relief from unconscionable contracts by "interpreting" the unconscionable elements out of them.[95] This is very clear in the cases of "strict" constructions of exemption clauses.[96] The cases also show that the court's power to imply terms into contracts is a flexible judicial tool often used to control contracts that would otherwise be unfair.[97]

Waddams concludes that lip service is still paid to the notion of freedom of contract, but that the exceptions to it are now so extensive that it is no longer realistic to regard the freedom of contract as the general rule. Rather, the freedom of contract is no more than a superfluous fiction, an "empty shell", which "at last can be discarded without effecting any great change in the actual practice of the courts". The recognition of unconscionability as a general ground of relief, he says, is an essential step in the development of the law. It would make the law more, not less, certain because:

> . . . if as appears to be the case, agreements are in practice set aside quite frequently and generally, it must conduce to certainty rather than uncertainty to recognize the general principle.

Moreover a general principle of unconscionability would "fill the gaps between the existing islands of intervention",[98] and remove anomalies.[99] Clearly inequality of exchange is not in itself sufficient to justify judicial intervention. But, suggests Waddams,

> . . . a large inequality of exchange combined with inequality of bargaining power . . . goes a long way to suggest a case for relief.[100]

Perhaps Waddams overstates his case, but it cannot be denied that the enforcement of contracts often works injustice. The courts are constantly asked for relief and the cases on unconscionability and economic duress show that they are responding.

[92] *Ibid*, 192–206.
[93] [1973] QB 400, 415.
[94] *Thornton* v *Shoe Lane Parking* [1971] 2 QB 163.
[95] *L Schuler A G* v *Wickman Machine Tool Sales Ltd* [1974] AC 235 (HL).
[96] *Alderslade* v *Hendon Laundry Ltd* [1945] KB 189; *Gillespie Bros* v *Roy Bowles Transport* [1973] QB 400.
[97] *Denmark Productions Ltd* v *Boscohel Productions Ltd* [1969] QB 699.
[98] S M Waddams, *The Law of Contracts* (1977) 332–333.
[99] See for example *Bridge* v *Campbell Discount Co Ltd* [1962] AC 600, 629.
[100] S M Waddams, *The Law of Contracts* (1977) 334.

LEGISLATION

The whole of the common law world has seen increasing statutory control over the freedom to contract. Such legislation generally takes one of two forms. The first is the prohibition of particular undesirable contractual terms or the prescription of desirable terms. This technique works well, but only where it is possible to isolate desirable or undesirable terms in more or less standard transactions. The clearest New Zealand examples of this kind of legislation are the Hire Purchase Act 1977 and the Property Law Act 1952 (as amended by the Property Law Amendment Act 1975).[101] Sections 11, 12 and 13 of the Hire Purchase Act provide that "there shall be implied in every hire purchase agreement" terms that the vendor has the right to sell the goods, that the goods are free from encumbrances, and that the goods are of merchantable quality and fit for their required purpose. Section 51(1) states, "The provisions of this Act shall have effect notwithstanding any provisions to the contrary in any agreement." Similarly the Property Law Act provides some control over unfair leases of dwellinghouses. Most importantly s116H(1) provides, "In every lease of a dwellinghouse there shall be implied on the part of the lessor a warranty that the dwellinghouse is . . . in a fit and habitable condition". Section 104C places a general restriction on contracting out of this and related provisions. There is every reason to think that these statutes have substantially redressed some of the more serious "inequalities of bargaining power" in our society.

The second form of statutory control over unconscionable bargains is to give the court the power to grant relief from them. The most noteworthy New Zealand example of this kind of legislation is the Credit Contracts Act 1981. Section 10(1) provides:

> Where . . . the court considers that —
>
> (a) A credit contract, or any term thereof, is oppressive; or
>
> (b) A party under a credit contract has exercised, or intends to exercise a right or power conferred by the contract in an oppressive manner; or
>
> (c) A party under a credit contract has induced another party to enter into the contract by oppressive means —
>
> the court may re-open the contract.

Section 9 defines "oppressive" as meaning "oppressive, harsh, unjustly burdensome, unconscionable, or in contravention of reasonable standards of commercial practice". Although relief has been given under the Act in several cases, the judges have consistently and expressly declined to offer any general principles as to its scope.[102] But it would seem that if a contract is a "credit contract" under the Act then any term may be attacked as "oppressive", even though it does not relate to the credit element of the contract.[103]

[101] Consider also the Matrimonial Property Act 1976 and the Sale of Goods Act 1908.

[102] *Udy* v *Kuzinas* (unreported), High Court, Rotorua, (A 1/83) Pritchard J.

[103] P J Majurey, "The Re-Opening of Oppressive Credit Contracts under the Credit Contracts Act 1981: A Case of Caveat Creditor"; vol 5 (1984) AULR 17, 21; *Gibson* v *Dealer Discounting* (1984) 7 TCL No 20.

Perhaps the most important legislation of this kind in the whole of the common law world is s 2-302 of the Uniform Commercial Code (US) which controls sale agreements generally. Section 2-302(1) provides:

> If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

The fears of commercial chaos that were aroused by the enactment of this provision have proved unfounded. The reported cases show that most successful litigants have been consumers, and in particular, consumers who were poor or otherwise disadvantaged. "The courts have not generally been receptive to pleas of unconscionability by one merchant against another".[104]

Other miscellaneous attempts to control unconscionable transactions are less direct. Examples are the disclosure requirements of the Credit Contracts Act and the "cooling off" period during which the consumer may withdraw provided by the Door to Door Sales Act 1967.

STATUTES AND THE COMMON LAW

Some argue that statutes giving relief from unconscionable transactions are exceptions, leaving intact the general sanctity of contract.[105] Such statutes can even be seen as strengthening freedom of contract in that, as exceptions, they prove the rule. It is also commonly said that the judges should support the common law freedom of contract and refrain from rewriting contracts because:

> If they did attempt to do so, they would be confronted with the resolution of economic questions and disputes which the common law is not equipped to solve.[106]

But this is less convincing than the opposing argument. Legislation reflects the needs of society. The classical common law theory of freedom of contract encapsulates an ideology which has largely passed into history. The fact that the need for control of contracts has become so pressing in particular cases as to prompt legislative intervention argues in favour rather than against the need for general judicial control of contract: common law and statute law ought to develop in harmony.

In this regard much can be learnt from the American experience. In America it is now orthodox law that the courts will give relief against unconscionable contracts. The core of this jurisdiction is s 2-302 of the Uniform Commercial Code but American courts generally give relief against unconscionable contracts as a matter of common law where the Code is inapplicable; the common law has developed so as to complement the statute. A distinction is generally drawn in American law between "procedural unconscionability" and "substantive uncons-

[104] White and Summens, *Uniform Commercial Code* (2nd ed 1980) 149.
[105] eg Lord Scarman, *National Westminster Bank* v *Morgan* [1985] All ER 821, 830.
[106] Goff and Jones, *Law of Restitution* (2nd ed 1978) 186.

cionability".[107] The former is where some element of oppression or wrongdoing has occurred in the process of making the contract; and the courts can use doctrines like duress and undue influence as merely illustrative of a broader principle requiring that undue advantage not be taken. (Compare Lord Denning's judgment in *Lloyds Bank* v *Bundy*).[108] Substantative unconscionability, in contrast, goes to the terms of the contract. In practice it most commonly covers unfair exemption clauses and excessive prices.

A similar distinction seems recently to have been introduced to Commonwealth law. The opinion of the Privy Council in *Hart* v *O'Connor* includes this statement (p 10):

> If a contract is stigmitized as "unfair", it may be unfair in one of two ways. It may be unfair by reason of the unfair manner in which it was brought into existence; the contract induced by undue influence is unfair in this sense. It will be convenient to call this "procedural unfairness". It may also, in some contexts, be described (accurately or inaccurately) as "unfair" by reason of the fact that the terms of the contract are more favourable to one party than to the other. In order to distinguish this "unfairness" from procedural unfairness, it will be convenient to call it "contractual imbalance". The two concepts may overlap. Contractual imbalance may be so extreme as to raise a presumption of procedural unfairness, such as undue influence or some other form of victimisation. Equity will relieve the party from a contract which he has then induced to make as a result of victimisation. Equity will not relieve a party from a contract on the ground only that there is a contractual imbalance not amounting to unconscionable dealing.

It is curious that the tightest constraints[109] on contract have developed in the land of Ayn Rand and Milton Friedman — perhaps the mischief there is greater. But all the legislation and case law discussed in this article supports the view that the rest of the common law world is following the American way, and there is judicial support for the view that Parliament and the judges ought to develop the law in harmony rather than counterpoint. Again it comes from Lord Denning. His view of how the judges should perceive their role in this era of increasing legislative attempts to grant relief against unconscionable transactions seems a fitting and optimistic note on which to end:

> The Law Commission, in their codification of the law of landlord and tenant, recommend that some such term should be implied by statute. But I do not think we need wait for a statute. We are well able to imply it now in the same way as judges have implied terms for centuries. Some people seem to think that, now there is a Law Commission, the judges should leave it to them to put right any defect and to make any new development. The judges must no longer play a constructive role. They must be automatons applying the existing rules. Just think what this means. The law must stand still until the Law Commission has reported and Parliament passed an Act on it; and, meanwhile, every litigant must have his case decided by the dead hand of the past. I decline to reduce the judges to such a sterile role. They should develop the law, case by case, as they have done in the past; so that the litigants before them can have their

[107] Loff, "Unconscionability and the Code" (1976) 115 Un Pa LR 485.
[108] [1975] 1 QB 632.
[109] Not only unconscionability but also economic duress were first developed in the United States: Dalzell, *Duress by Economic Pressure* (1942) 20 N Carolina LR 23, at 7 and 341; J P Dawson, *Economic Duress* (1947) 45 Mich LR 253.

differences decided by the law as it should be and is, and not by the law of the past. So I hold here that there is clearly to be implied, for the common parts, some such term as the Law Commission recommend.[110]

[110] *Liverpool City Council* v *Irwin* [1975] 3 All ER 658, 666.