The enforceability of contractual variations: Moyes & Groves Ltd v. Radiation New Zealand Ltd

John Land*

Changed circumstances will often render the original terms of a contract unsuitable. The parties may agree to a change but the rule that an existing obligation under a contract cannot amount to good consideration for the change may defeat the parties' aims. The difficulty can be circumvented if some new consideration is offered or if a deed is signed. But this will not necessarily occur in every deserving case. In Moyes & Groves *v.* Radiation New Zealand Ltd, *the Court of Appeal upheld an agreement to pay a higher price on the basis that it was a compromise of disputed claims. The author discusses inadequacies in this decision and suggests that, but for the pre-existing duty rule, the search for extra consideration would have been unnecessary. He advocates abolition of that rule and points out that the problem caused by contractual variations which have been unfairly obtained can be resolved by using the developing doctrine of economic duress.*

I. INTRODUCTION

It is a well established rule of the law of contract that the performance of a duty which the promisee already owes under an existing contract with the promisor cannot constitute consideration. A promise by one party to a contract to vary its terms will not then be enforceable unless some new obligation is undertaken in exchange for it.

This rule, which has been subjected to a good deal of criticism,[1] is known as the pre-existing duty rule. The rule operates to strike down all contractual variations which favour one side only. When obtained fairly, however, such variations may well be deserving of enforcement. Consider the case of a manufacturer and supplier of goods who is suddenly faced with an unexpected increase in the price of certain important raw materials. Due to this change in circumstances, he makes a request for extra remuneration for the performance of his contractual duty. The party to whom the duty is owed, the purchaser, considers the request

* This article was submitted as part of the LL.B. (Honours) programme.

1 See, for example, Reiter "Courts, Consideration and Common Sense" (1977) 27 Toronto L.J. 439.

and comes to the conclusion that agreement is in his best overall interests. Such a variation should be enforced. To deny enforcement is to defeat the reasonable expectations of the parties. The agreement is a fair commercial arrangement that the lay person would expect to be binding.

The pre-existing duty rule has also, however, served to strike down extorted agreements. A variation on the example above illustrates the point. The supplier threatens to break the contract unless a demand for increased remuneration is agreed to. No good reason for the demand is given. The purchaser has a special need for performance and in the circumstances no real choice but to agree. In this case the innocent party should not be held to such an agreement. The pre-existing duty rule would strike this agreement down. However, it would do so not because of the duress, but because there was no consideration for the promise to pay more.

Recent developments in the law suggest that duress in the form of commercial pressure can now in itself be a ground for the setting aside of contracts entered into under such pressure. Extorted agreements of the kind described above are under this emerging doctrine of economic duress voidable at the option of the innocent party. It will be argued that such a result removes any justification for the continued existence of the pre-existing duty rule.

The recent case of *Moyes & Groves Ltd* v. *Radiation New Zealand Ltd*[2] involved the enforceability of a sensible contractual variation, but one under which one party undertook no extra obligations above those owed under the original contract. A strict application of the pre-existing duty rule may have denied enforcement to this variation. Such an unjust result was avoided, but the way the case was resolved illustrates the distortions of the law which may often be necessary to achieve the right result. In this note, it is proposed to examine the decision itself and then to consider more generally the status of the pre-existing duty rule in current law.

II. *MOYES & GROVES*: THE FACTS AND DECISION

In June 1973 Radiation New Zealand Ltd (the buyer) ordered from Moyes & Groves Ltd (the seller) some machine parts which had to be manufactured in India. The contract price was $400. The seller's order with the manufacturers was placed in October 1973. The parts arrived in June 1976 about two years later than they would normally have been expected. The buyer had not been in any urgent need of the parts and both parties had forgotten about the contract. The manufacturers had invoiced the parts to the seller at $2,737. The seller offered to supply the parts at this price, failing which the goods would have to be returned to India. The buyer, however, asserted its claim under the original contract. By agreement between the parties the seller then wrote to the manufacturers asking them to absorb some of the cost increase, but they were not prepared to do so. On the seller repeating its offer to supply at $2,737, the buyer offered to pay $611.12, a sum reflecting the loss of value of money since the order was made.

2 [1982] 1 N.Z.L.R. 368.

Finally, on 1 December 1976, the seller wrote to the buyer rejecting that offer and indicating that the parts would be returned to India unless the buyer agreed to pay $2,737 before 10 December. Customs had given the seller ten days to pay the duty and uplift the parts. In its letter, the seller also referred to a recent devaluation, the cost of which it said it would bear. The buyer then replied by telex and letter: "Appears no alternative but to accept your price under protest". Having obtained the parts, however, the buyer paid only $400.

In the lower courts the issue primarily focussed on was whether or not the original contract had been abandoned. If the original contract was still in existence, then the seller, in return for the buyer's promise to pay $2,737, would only have been performing obligations that it was already bound to perform. If on the other hand the contract had been abandoned, then the delivery of the parts would no longer be an obligation owed the buyer and could therefore be consideration for the buyer's promise. In the Magistrate's Court, Gilliand S.M. held that the original contract had been abandoned and that the buyer's promise was therefore supported by consideration. In the Supreme Court, however, Casey J. did not think that the inactivity and delay were sufficient to establish an abandonment of the contract.

The Court of Appeal did not decide the difficult question of whether the contract had been abandoned. Their Honours were satisfied that the agreement at the higher price amounted to a compromise of disputed claims. This compromise itself provided consideration for the buyer's promise, making it unnecessary to decide the issue as to abandonment.

III. THE FINDING OF A COMPROMISE

A compromise of disputed claims is quite distinct from the lay person's concept of compromise. To the lay person, a compromise is the settling of a disagreement by mutual concession. Both parties withdraw to some extent from their initial demands or proposals. For a legal compromise, however, such an element of give and take is neither necessary nor sufficient. A compromise of disputed claims is an agreement to settle a dispute under which both parties give up their right to contest the matter further. This settlement need not involve concessions on both sides and indeed did not in *Moyes & Groves* (where the seller's demand prevailed).

It is well settled that a compromise of disputed claims amounts to a valid contract with consideration being provided by each party giving up their respective claims. For the surrender of a claim to be consideration, it must, however, be made bona fide. The party making the claim must have a genuine belief that it has at least a fair chance of success.[3] He also must not deliberately conceal from the other party facts which might affect the validity of the claim.[4] It is sometimes said that in addition to being bona fide, the claim must also be "a real claim, a question which is not vexatious or frivolous to litigate."[5] However,

3 *Callisher* v. *Bischoffsheim* (1870) L.R. 5 Q.B. 449, 452.
4 *Miles* v. *New Zealand Alford Estate Co.* (1885) 32 Ch.D 266, 284.
5 *Owners of Tank Steamer Portofino* v. *Berlin Derunaptha* (1934) 39 Com. Cas. 330, 341 per Scrutton L.J.

the conflict of opinion on this issue[6] does not "reflect an important conceptual difference. There will be few cases involving an honest or bona fide belief in a claim which is vexatious or frivolous."[7]

There are strong reasons for the enforcement of true compromises. These include "the reduction of litigation . . . , the encouragement of finality in commercial affairs, and protection of the strong probability of reliance on the compromise."[8] For these reasons, the courts have often expressed their willingness to support compromises.[9]

In *Moyes & Groves* the Court of Appeal held that the buyer's acceptance of the higher price concluded such a compromise of disputed claims. However, the judgments contain little analysis and for this reason, the finding of compromise is open to criticism. Firstly, the judgments do not demonstrate that the seller really made a claim of entitlement to treat the contract as abandoned. Secondly, the judgments do not establish that the buyer agreed to compromise.

The first problem is whether the seller actually made a claim of entitlement. It does not clearly appear from the facts or reasoning contained in the judgments that the seller made such a claim.

Cooke J. did not address this issue. His Honour stated that "the seller had considerable grounds for contending that it had a right to treat its contract with the buyer as abandoned. . . ."[10] There is no statement, however, as to whether the seller did in fact contend that it had a right to treat the contract as abandoned. No doubt given the delay a claim to treat the contract as abandoned would have been a reasonable one. This, however, is not the important point. The judges' role is not to determine what the parties could have done in the circumstances and decide on that basis. It is instead their role to see what the parties actually did do and apply the law to those facts. If there was no claim, there is no compromise.

Somers J. asserted that the "correspondence shows that there was a genuine disagreement between the parties as to their respective rights and obligations."[11] The correspondence does indeed show a disagreement. The disagreement, however, seems merely to have been as to what price the parties were prepared to accept. We are told that the buyer asserted "its claim under the original contract"[12] but nothing about the seller having made a similar claim of entitlement. From the correspondence we can deduce that the seller was not willing to perform the original contract, but not that it claimed to have a right not to perform. The finding of compromise cannot be supported unless the seller, expressly or impliedly, made a bona fide claim of entitlement. The judgments, however, do not demonstrate that this was the case.

6 Canvassed by the New Zealand Court of Appeal in *Couch* v. *Branch Investment (1969) Ltd* [1980] 2 N.Z.L.R. 314.
7 *Wigan* v. *Edwards* (1973) 1 A.L.R. 497, 513 per Mason J.
8 Reiter, supra n.1, 489.
9 See, for example, *Binder* v. *Alachouzos* [1972] 2 Q.B. 151.
10 Supra n.2, 371.
11 Ibid. 373.
12 Ibid. 372.

The second problem with the finding of a compromise in *Moyes & Groves* is that the judgments do not clearly demonstrate that the buyer agreed to compromise. There can be no compromise where one party reserves the right to dispute the claim in the future. An example of this is provided by the facts of *Sundell & Sons* v. *Emm Yannoulatos*.[13] In that case a contract for the sale of iron was entered into. Pursuant to the contract, the buyers established a letter of credit in favour of the sellers. There was then a cost increase, which the sellers claimed they were entitled to pass on to the buyers. The buyers, under threat of non-performance, agreed to increase the letter of credit. The buyers, however, made it quite clear that their agreement was made without prejudice to their rights under the original contract. Although the sellers made a bona fide claim of entitlement the case was obviously not one of compromise. The buyers did not agree to give up their right to contend that the original contract was binding.[14]

The position in *Moyes & Groves* is not as clear as in the *Sundell* case. The buyer did not expressly assert its rights to dispute the claim. Its promise to pay the increased price was, however, made "under protest". In the Supreme Court Casey J. felt that "an acceptance in this form . . . was clear notice that the validity of the promise to pay would later be contested."[15] If this is so, it is a contradiction to say there was a compromise. A party does not give up a claim if he intimates that he intends to pursue it.

It could be argued that the interpretation put on the protest by Casey J. was not necessarily the correct one. It has been said that "the word 'protest' is itself equivocal. It may mean the serious assertion of a right or it may mean no more than a statement that payment [or a promise] is grudgingly made."[16] Possibly the buyer did not do enough to indicate that it did not regard the transaction as closed. In English contract law, the test for whether there is agreement is an objective one.[17] If it would appear to a reasonable person in the position of the seller that the buyer intended to put an end to the dispute, then there would be a binding compromise.

The acceptance "under protest", then, can possibly be seen as an agreement to compromise the claim although a grudging one. However, the position is unclear and the issue merited some analysis from the court. In the writer's opinion the court was too ready to find that a compromise of disputed claims had been concluded.

IV. THE INADEQUACIES OF THE PRE-EXISTING DUTY RULE

It is not hard to see why the Court of Appeal was so ready to find a compromise in *Moyes & Groves*. The agreement was one which was deserving of enforcement.

13 (1956) 56 S.R. (N.S.W.) 323.

14 See also *Re Hooper & Grass Contract* [1949] V.R. 269 and *O. L. Knutson* v. *The Bourkes Syndicate* [1941] S.C.R. 419 where although bona fide claims were made there was clearly no question of compromise.

15 *Radiation New Zealand Ltd* v. *Moyes & Groves Ltd* (1979) Unreported, Auckland Registry M.1155/78 at p. 5.

16 *Mason* v. *The State of New South Wales* (1959) 102 C.L.R. 108, 143 per Windeyer J.

17 See, for example, *Boulder Consolidated Ltd* v. *Tangaere* [1980] 1 N.Z.L.R. 560.

There was no objectionable pressure. There had been a large and unexpected increase in cost. The seller restricted its demand to the cost increase and was willing to bear the loss of a recent devaluation. Its demand then was quite reasonable in the circumstances. Further, the buyer, while still wanting the parts, had no pressing need for them. It was therefore not under a compulsion to agree.

If the buyer still wanted to stand on the original contract, it could have sued for damages. If successful the damages awarded would have put the buyer in the same position as if the original contract had been performed. The buyer, however, did agree to the increased price and did so without making it clear that it wished to reserve its rights under the original contract. As a result the seller quite reasonably thought it could rely on the promise to pay more and delivered the parts it otherwise would not have.

In all the circumstances, it seems fair that the buyer should be held to its promise to pay more. However, the pre-existing duty rule could conceivably (as it did in the Supreme Court) have rendered the promise unenforceable. The promise would only have been certain of enforcement had the seller made use of certain devices which can be used to avoid the pre-existing duty rule.

Firstly, the seller could have insisted on a mutual rescission of the original contract. Having secured an agreement to discharge the original contract, a replacement contract at the higher price would be binding. The agreement to rescind is supported by consideration as both parties give up their rights under the original contract. The replacement contract itself is binding as it generates its own consideration. As the rescission discharges the obligations under the original contract, the delivery of the goods by the seller is no longer the performance of a duty already owed to the buyer. There is, therefore, no difficulty in it constituting consideration for the buyer's promise.

Secondly, the seller could have insisted that the parties enter into a formal deed, complying with section 4 of the Property Law Act 1952. The variation could then be binding without fresh consideration.

Finally, the seller could have stipulated that it was to provide some nominal consideration in return for the promise to pay more. In such a case also, the variation would be binding.

The pre-existing duty rule then can be circumvented if the party who owes the duty is aware of the devices available and the need to use them. However, there seems no reason why the seller's position should be strengthened if it did make use of such devices. The importance of such formalities under the existing law means that the enforceability of sensible contractual variations will often depend on whether the party benefiting was legally advised. Such a determinant of enforceability is arbitrary and unjust.

In the case of isolated gratuitous promises the use of formalities or presence of consideration can perform a cautionary function. Such promises are particularly likely to have been made without sufficient deliberation. The presence of some nominal consideration or the use of formalities like the deed serves to draw the promisor's attention to the significance of what he is doing. The use of legal

formalities also has the effect of directing that a particular promise is to receive enforcement. The fact that a gratuitous promise is contained in a deed indicates that it is intended to be binding. So also if the promise is supported by nominal consideration since the parties "have taken the trouble to cast their transaction in the form of an exchange."[18]

In the case of contract variations, however, there is not the same risk of a promise being made carelessly and without the intention that it should be binding. Legal consequences are already attached to the relationship between the parties and care is likely to be taken in any modification of this relationship.[19] The fact that the promise is connected to an existing business deal also suggests that the promise will be a serious one.[20]

Formalities and "fresh" consideration serve no useful purpose in the case of contract variations. That their presence should determine enforceability in that context is therefore, given the arbitrary distinctions that result, highly unsatisfactory. There is no reason why a sensible contractual modification like the one in *Moyes & Groves* should not be enforced, even though unsupported by fresh consideration or the use of some other technical device.

V. THE REASONS BEHIND THE PRE-EXISTING DUTY RULE

No test can be formulated for what constitutes consideration that will work in every case. As a general rule, however, if an act involves benefit to the promisor and/or detriment to the promisee, then that act if given in exchange for the promise will constitute consideration for it. The justification often given for the pre-existing duty rule is that because the promisee was already bound to render the performance and because the promisor already had the right to such performance there is no "legal" detriment or benefit.

However, it is wrong to say that the promisor gets no benefit from the performance of the duty already owed him. He gets the benefit of ensuring performance and avoiding litigation. It is equally wrong to say that the promisee incurs no detriment in performing the duty he already owes. Performance either in itself or because it precludes the undertaking of some other activity may be more onerous than paying damages. There is then benefit and detriment in fact. An assertion that there is no "legal" benefit or detriment can therefore only mean that there is some other reason for refusing to enforce the promise.[21]

The true justification for the pre-existing duty rule seems to be the protection of the party to whom the duty is owed from extortion. The New Zealand case of *Cook Islands Shipping Co. Ltd* v. *Colson*[22] illustrates the use of the rule for this purpose. The plaintiff was a shipping company engaged by the defendant

18 Fuller "Consideration and Form" (1941) 41 Columbia L.R. 799, 820.
19 Swan "Consideration and the Reasons for Enforcing Contracts" (1976) Western Ontario L.R. 83, 88.
20 Fuller, supra n.18, 818.
21 Corbin *Corbin on Contracts* (West Publishing Co, St Paul Minn., 1952) para. 172, p. 248.
22 [1975] 1 N.Z.L.R. 422.

to carry building materials to Rarotonga. The contract required the plaintiff to load at Portland a quantity of cement and an unspecified quantity of other materials. The defendant's obligation under the contract was to pay freight for the cargo loaded according to a certain set rate. The plaintiff's expectation was that loading would be completed in one day, but it soon became apparent that it would not. According to the plaintiffs, the delay was because the amount of cargo was much greater than that expected. There was no specific finding on the point, but it is more likely that the failure to load within one day was actually caused by other factors unrelated to the size of the cargo, notably an industrial dispute which occurred at the same time.

The plaintiff told the defendant that the ship would sail that night unless the extra loading time was paid for at $75 per hour. Again, though not found as a fact, it is probable that the plaintiff never actually intended that the ship leave that night. The defendant then agreed to the demand, but only did so because the departure of the ship that night would have meant the leaving behind in New Zealand of materials essential for the performance on time of a contract in Rarotonga. The plaintiff knew of the defendant's special need to have the materials transported on this ship.

Mahon J. held that the promise to pay more was unenforceable for want of consideration. It was given in return for the performance of duties already owed to the promisor under the original contract. The pre-existing duty rule was thus utilised to strike down what was obviously an extorted agreement. The willingness of Mahon J. to approve the rule was clearly influenced by this factor. In support of the rule his Honour cited and approved of authority[23] which indicated the true reason behind the rule. This was:[24]

> the requirement of legal policy that one contracting party should not be subject to an extorted demand for further payment under threat of non-performance, especially where due performance is of special importance to that party.

This policy was given effect to in the *Cook Islands* case. The pre-existing duty rule served there to render unenforceable a promise obtained by unfair pressure. However, the pre-existing duty rule is incapable of coping satisfactorily with the problem of extortion. It is an undiscerning rule striking down both fairly and unfairly obtained bargains. The fact that a contract variation is reasonable and obtained without unfair pressure will not save it if it is made without fresh consideration. Further, because of the limitations on the pre-existing duty rule, it is unable to render unenforceable many variations that are objectionable. The application of the rule in the *Cook Islands* case would have been avoided had, for example, the plaintiff been sufficiently shrewd to offer some nominal consideration in return for the promise to pay more.

Given these inadequacies, it is clear that the policy of not enforcing extorted agreements would be better achieved through deciding, on the facts of each particular case, whether unfair pressure had been applied. The development of

23 *Lingenfelder* v. *Wainwright Brewery Co.* 15 S.W. 844 (1891); Goodhart "Performance of an Existing Duty as Consideration" (1956) 72 L.Q.R. 490.
24 Supra n.22, 435.

the doctrine of economic duress has made this possible. The doctrine renders voidable those contracts which are entered into under unfair pressure of exactly the kind described by Mahon J.

VI. ECONOMIC DURESS: *THE ATLANTIC BARON* AND *PAO ON*

The doctrine of economic duress though clearly established is still in a relatively early stage of development. It is not yet settled what exactly constitutes economic duress. For this reason, it is proposed to set out the facts and decisions in *The Atlantic Baron*[25] and in *Pao On* v. *Lau Yiu Long*.[26] The cases provide a basis for a discussion of the doctrine's scope and its usefulness in regulating unfair pressure. The cases also highlight some further inadequacies of the pre-existing duty rule.

A. *The Atlantic Baron*

The defendants (the "builders") agreed to build an oil tanker for the plaintiffs (the "owners") for a fixed price payable in instalments. The contract also provided for the builders to open a letter of credit. This was to act as security for repayment of the instalments if the builders defaulted in performance. After the first instalment was paid, the American dollar was devalued by 10%. As a result, the amounts payable under certain sub-contracts relating to the vessel increased. The builders then demanded a 10% increase in the purchase price in respect of the remaining instalments. The owners were advised that there was no legal basis for this claim. The builders never put forward any legal basis for their claim and made it clear that they did not intend to perform the contract unless the increased price was agreed to.

In the meantime, the owners were negotiating a highly lucrative charter of the ship to the Shell company. Not agreeing to the builders' demands would result in the loss of a substantial profit from this charter. Eventually the owners agreed to the increased price "without prejudice to our rights". The owners also asked that the letter of credit be increased accordingly and this was done. The owners made no subsequent protests and did not claim to recover the extra payments until eight months after delivery of the ship.

Mocatta J. held that the builders' increasing of the letter of credit was consideration for the owners' promise to pay more. This finding can, however, be criticised. The increasing of the letter of credit was not the price of the promise to pay more but a natural consequence of it. The owners bargained, not for the increase in the letter of credit, but for the continued performance of the contract.[27] A less artificial finding of consideration would have been possible had the pre-existing duty rule not been considered good law.

His Lordship, after holding that the new agreement was supported by con-

25 *North Ocean Shipping Co. Ltd* v. *Hyundai Construction Co. Ltd* [1979] 1 Q.B. 705.
26 [1980] A.C. 614.
27 An almost identical argument to that accepted in the *Atlantic Baron* was rejected in *Gilbert Steel Ltd* v. *University Construction Ltd* (1976) 67 D.L.R. (3d) 606, 610. Professor Reiter has described the argument as "ludicrous", supra n.1, 452, note 47.

sideration, then held it was voidable for economic duress. The finding that the owners' agreement was made under compulsion was based on the unreasonableness of expecting the owners to resist the pressure and claim damages for breach. This would have deprived them of the prospect of a substantial profit under the Shell charter that was being arranged.

Finally Mocatta J. held that though the contract was voidable the owners had affirmed it through their failure to protest and their delay in bringing any action. This conduct occurred after the owners were free of duress, and objectively it indicated an intention to keep the contract on foot.

B. *Pao On* v. *Lau Yiu Long*

The plaintiffs, the shareholders of one company ("Shing On"), concluded a contract for the sale of their shares to another company ("Fu Chip"). They were to be paid by way of shares in Fu Chip. The defendants were majority shareholders in Fu Chip. They wanted to ensure that the plaintiffs did not suddenly dispose of a large number of Fu Chip shares, as this might depress the market and so reduce the value of their own shareholding. A provision was therefore included in the contract by which the plaintiffs promised they would retain 60% of the Fu Chip shares allocated them for a period of about a year. In return the plaintiffs wanted protection against a drop in value of the Fu Chip shares during the period in which they promised to retain them. Both parties understood that the plaintiffs were to be guaranteed against this eventuality.

As a result a subsidiary agreement was entered into between the plaintiffs and the defendants. This agreement provided for the frozen Fu Chip shares to be sold back to the defendants at the end of their period of retention. The plaintiffs then realised that this agreement was not the kind of guarantee that they had expected. Although the plaintiffs were protected against any fall in value of the Fu Chip shares, they could not benefit from any increase in value. This would deprive them of the very advantage they had sought to gain by taking their price in shares under the main agreement.

The plaintiffs therefore notified the defendants that they would not go ahead with the main agreement with Fu Chip unless the subsidiary agreement was replaced by a true guarantee by way of indemnity. The defendants feared that if the main agreement fell through, the public would lose confidence in Fu Chip shares. The effect on the share price, however, was only likely to be small and probably not permanent.[28] In any event, the defendants finally decided to agree to the plaintiffs' demand. The shares then unexpectedly fell in value. The defendants, however, refused to compensate the plaintiffs under the guarantee contending that it was not binding.

The Privy Council found consideration for the guarantee in three different ways.[29] However, according to their Lordships, the "real consideration" for the guarantees was the "promise to perform or the performance of the plaintiffs'

28 See findings of trial judge set out in the Privy Council judgment, supra n.26, 626.
29 Supra n.26, 628-632.

pre-existing contractual obligations to Fu Chip".[30] The performance of these obligations could be consideration for the defendants' promise of indemnity because they were obligations owed not to the defendants but to a third party (Fu Chip). Had the obligations been owed to the defendants they could not have constituted consideration.

That such a distinction can be drawn further shows the inadequacies of the current law. Fu Chip can only technically be called a different entity. The main agreement was negotiated for by the defendants. It was for the benefit of the defendants that the provision requiring the plaintiffs to retain the shares was inserted. The defendants as the shareholders of Fu Chip clearly had the power to get Fu Chip to enforce the main agreement.[31] It seems absurd that the enforceability of the promise of indemnity could depend on whether as a matter of form the main agreement was entered into by Fu Chip or by Fu Chip's shareholders.

The Privy Council, after holding that the guarantee was supported by consideration, further held that it was not voidable for economic duress. There was commercial pressure but not coercion. The defendants had considered the matter thoroughly and chosen to avoid litigation.[32] The Privy Council referred to some factors which can be relevant in determining whether there is coercion. These were:[33]

> whether the person alleged to have been coerced did or did not protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have an alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it.

VII. THE SCOPE OF ECONOMIC DURESS

The two cases just outlined provide assistance for a discussion of the "test" for economic duress. For economic duress to exist there must be (i) a coercion (or compulsion) of the victim's will which (ii) has been induced by pressure which the law regards as illegitimate.[34]

A. *Coercion or Compulsion of the Will*

In *Universe Tankships Inc. of Monrovia* v. *International Transport Workers Federation*[35] Lord Scarman classified compulsion as "the lack of any practicable choice but to submit".[36] Factors referred to in *Pao On,* such as whether the "victim" protested or had independent advice, were said not to go "to the essence of duress".[37] By defining compulsion as the lack of practicable choice but to submit, more emphasis was placed on the other factor mentioned in *Pao On,* the alternatives open to the "victim". Such an approach is consistent with that taken in America. There for economic duress to exist the threat made must leave

30 Ibid. 631-632.
31 Ibid. 626.
32 Ibid. 635.
33 Idem.
34 *Universe Tankships Inc. of Monrovia* v. *International Transport Workers Federation* [1983] A.C. 366, 383-4 (per Lord Diplock), 400 (per Lord Scarman).
35 [1983] A.C. 366.
36 Ibid. 400.
37 Idem.

"the victim no reasonable alternative".[38] The importance of the alternatives open to the submitting party can in fact be seen in the *Pao On* and *Atlantic Baron* decisions.

In *Pao On* the defendants did have a commercially viable alternative open to them. Litigation might have decreased the value of their shareholding in Fu Chip, but no great loss could have been expected. In the *Atlantic Baron* the owners would, had they resisted the pressure, have been deprived of the prospect of earning a substantial profit under the Shell charter. Resisting the pressure then might not be considered a reasonable alternative.[39] The owners, however, would not have suffered irreparable commercial harm from resisting the pressure and it is primarily for this reason that some academics have criticised the finding of compulsion in the case.[40] The position would have been much clearer had the lucrative Shell charter already been entered into. Resisting the pressure would then have meant breaking a contract with a third party. Such a course of action could almost never be called a viable alternative.

B. *Illegitimate Pressure*

The second element to the test for economic duress is that the pressure exerted be "illegitimate". It seems to have been assumed in the *Universe Tankship* case that "illegitimate" in this context simply means unlawful.[41] Such a determining factor is unnecessarily rigid if the doctrine is to adequately perform the task of regulating unfair pressure. If an extortionate demand is made knowing that the victim is in no position to resist, then clearly the pressure is unfair. If, however, the demand is not made in bad faith and is reasonable in all the circumstances, then it is much more difficult to term the pressure illegitimate.

There is considerable academic support[42] for the view that threats not to perform a contract even if coercive should not always constitute economic duress. This is in fact the position in America. There, for economic duress to exist, the threat must be "improper".[43] Further, under American law, a "threat by a party to a contract not to perform his contractual duty is not, of itself, improper".[44] The *Pao On* case is a good illustration of a threat to break a contract which should not be considered illegitimate pressure. Both parties had understood that

38 American Law Institute *Restatement of the Law, Second : Contracts 2d* (American Law Institute Publishers, St Paul Minn., 1981) s. 175(1).

39 This was the view of Mocatta J. himself, supra n.25, 719.

40 Ogilvie "Economic Duress, inequality of Bargaining Power and Threatened Breach of Contract" (1981) 26 McGill L.J. 289, 300, 302, 317; Stewart "Economic Duress — Legal Regulation of Commercial Pressure" (1984) 14 Melbourne U.L.R. 410, 347, note 63.

41 Supra n.36. See for example Lord Scarman at p. 401.

40 Ogilvie "Economic Duress, Inequality of Bargaining Power and Threatened Breach of Dadson "The Atlantic Baron: Consideration, Economic Duress and Coerced Bargains" (1980) 38 U.T. Fac. L. Rev. 223; England & Rafferty "Contractual Variations: Consideration and Duress" (1980) 18 Osgoode Hall L.J. 627, 638; *Chitty on Contracts* (25 ed., Sweet & Maxwell, London, 1983), para. 488; Stewart, supra n.40, 428-431.

43 *Restatement,* supra n.38 s. 175(1).

44 *Restatement,* supra n.38 s. 176 Comment e; Farnsworth *Contracts* (Little, Brown & Company, Boston, 1982), section 4.17, p. 261.

the defendants would be guaranteed against a fall in value of the shares they had promised to retain. However, the expectation was merely that the defendants would be protected in this way and not that they would also be deprived of the benefit of any rise in the price of shares. This, however, was the effect of the subsidiary agreement. The plaintiffs then obviously had a just claim for the cancellation of the subsidiary agreement and its replacement with a guarantee by way of indemnity. It is inappropriate that the pressure exerted to effect this change should be termed illegitimate.

Another situation where a demand for extra remuneration may be reasonable is where unexpected difficulties arise in the performance of a contract. If the demand is not excessive and there is no element of bad faith, the pressure should not be called illegitimate. The finding of duress in the *Atlantic Baron,* however, is difficult to reconcile with such an analysis. There could be no question of the builders improperly taking advantage of the owners' special need for performance. The builders had no knowledge of the lucrative Shell charter. The owners further disclaimed any allegation that the builders' proposals were made in bad faith. Instead, there was a legitimate reason for the demand as a devaluation of the American dollar had increased the costs in building the oil-tanker. The *Atlantic Baron* then, whether or not a case of compulsion, should not have been considered a case of economic duress.

VIII. THE ADVANTAGES OF ECONOMIC DURESS IN DEALING WITH THE PROBLEM OF EXTORTION

Whatever the exact test for economic duress, it is clear that duress is a far more flexible instrument for dealing with the problem of extortion than the pre-existing duty rule.

The policy implemented in the *Cook Islands* case could now be achieved under the doctrine of economic duress. The case was clearly one of coercion. The defendant only submitted to the demand because of his belief that the ship would otherwise have sailed the same night. This would have left in New Zealand materials essential for the performance on time of a contract in Rarotonga. Nor could the pressure be termed legitimate. The plaintiff did not have a just claim for the extra payment, as it seems that the delay in loading was not actually caused by the defendant. Further, it appears that the plaintiff never really intended that the ship should leave that night and was merely taking advantage of the defendant's special need for performance. The doctrine of economic duress would strike down such an extorted agreement, but unlike the pre-existing duty rule, it would do so whether or not there was "fresh" consideration.

Another advantage of the doctrine in dealing with the problem of extortion is that it also enables the recovery of payments that are made under duress. The fact that an agreement is not supported by consideration is not in itself a ground for the recovery of payments that are made in performance of it.[45]

45 Otherwise any executed gift would be recoverable; Coote "Duress by Threatened Breach of Contract" [1980] C.L.J. 40, 43.

Most importantly, the doctrine of economic duress, unlike the pre-existing duty rule, does not threaten the enforceability of fair bargains. *Moyes & Groves,* unlike the *Cook Islands* case, was not a case of coercion. Suing for damages was a viable alternative to submitting to the demand. There was no urgent need for the parts and damages would have been an adequate remedy. The absence of coercion by itself precludes a finding of duress. It would, however, also be possible to argue that the pressure exerted was not illegitimate, as in the circumstances the seller's demand was a reasonable one.

For such an agreement to be upheld under the current law, however, a court may be forced to strain legal principle, employing an exception to the rule which is not really made out on the facts. That *Moyes & Groves* may itself have been such a case has already been suggested in this note. Distortion of legal principle is, of course, not desirable. More alarming, however, is the possibility that a court may fail to look beyond the technical rules in existence and as a result strike down an agreement deserving of enforcement.[46] This is the most serious danger of attempting to regulate unfair pressure under the guise of consideration.

IX. CONCLUSION

It is not surprising that the pre-existing duty rule has been "subjected to sustained and blistering attack from the academics".[47] A rule that strikes down fair commercial arrangements is indeed deserving of such scorn. It is conceded that gratuitous contractual variations have high possibilities of having been obtained unfairly. However, the doctrine of economic duress is sufficiently flexible to deal with this problem. The concern that a contracting party not be subject to extortionate demands can then no longer be a justification for the pre-existing duty rule. The rule, however, remains the law and while it does so it continues to threaten contractual variations which should be upheld.

The pre-existing duty rule is probably too settled for the courts to feel able to re-examine it.[48] If so, then it is the task and duty of the legislature to remove "that adjunct of the doctrine of consideration which has done most to give it a bad reputation."[49]

46 An example of this is *Gilbert Steel Ltd* v. *University Construction Ltd,* supra n.27.
47 Reiter, supra n.1, 453.
48 Cf. Reiter, supra n.1, 508-509.
49 Patterson "An Apology for Consideration" (1958) 58 Columbia L.R. 929, 936.