20 Contract Law—Vitiating Factors

Key Points

After reading this chapter, you will be able to:

- describe the difference between void and voidable contracts;
- describe the various vitiating factors that may make a contract void or voidable.

Void and voidable contracts

While the presence of the five characteristics outlined above give rise to a prima facie valid contract, there may be other factors at work which either undermine that validity (making it voidable) or destroy it entirely (making it void).

Void contracts

Where a contract is void the general rule is that the parties must be returned to their pre-contractual positions. This is known as restitution. Therefore, any money or goods that have changed hands must be returned. Where this is not possible (*e.g.* where goods have been consumed or service performed), the court may order payment in quasi-contract on a *quantum meruit* (as much as it is worth) basis.

Voidable contracts

Where the contract is voidable, the party wishing to avoid it can apply for the equitable remedy of rescission. Again, the aim is to return the parties to their pre-contractual position. As with all equitable remedies, rescission is discretionary and the courts will not grant it where:

- the party seeking to rescind the contract has previously affirmed it, *i.e.* has continued to perform the contract in the knowledge that it was voidable. Delay in seeking rescission

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does not, in itself, amount to affirmation but may be regarded as such where rescission would be unreasonable after such a lapse of time (this would be an example of the application of the maxim "delay defeats Equity");

- restitution (or *restitutio in integrum*) is not possible. The courts to do not insist on precise restitution—it is sufficient that goods can be returned in **substantially** the same state as that in which they were received;
- a third party has acquired rights in the subject matter of the contract in good faith and for value.

Vitiating factors

Lack of required formality

Most contracts are simple contracts, meaning that there are no formal requirements to be met in creating one. However, some contracts (*e.g.* those concerning interests in land or shares) must be made in writing or evidenced in writing in order to be valid.

Duress and undue influence

Where a person has been pressurised to enter into a contract, it will be voidable (***Pao On v. Lau Yiu Long*** [1980]). There are two forms of pressure recognised by law:

- **Duress.** Originally, the common law notion of duress only applied where the pressure took the form of physical violence to the person or the threat of such violence. More recently, it has been expanded to include commercial pressure (or "economic duress"—*Universe Tankships Inc of Monrovia v. International Transport Workers Federation, The Universe Sentinel* [1983]).
- **Undue influence.** The equitable doctrine of undue influence recognises more subtle forms of pressure and the abuse of privileged positions of influence. A presumption of undue influence arises where the parties were in a special fiduciary relationship (or relationship of trust), *e.g.* doctor and patient, solicitor and client.

Illegality

A contract is void if it is illegal either in its objective or manner of performance, *e.g.* contracts to commit a crime, tort or fraud, promote sexual immorality or corruption in public life, contracts of trade with an enemy in wartime. Where a contract is void for illegality, the general position is that any goods or money transferred is not recoverable (***Parkinson v. College of Ambulance Ltd and Harrison*** [1925]).

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Contrary to public policy

Contracts contrary to public policy are void, *e.g.* contracts prejudicial to the institution of marriage, contracts in unreasonable restraint of trade, gaming and wagering contracts.

Mistake

There are rare occasions where a mistake by one of the parties will make the contract void:

Mistake as to the subject matter. Where one party believes the contract to be about one thing and the other believes it to be about something different, there is no real agreement and the contract is void (*Raffles v. Wichelhaus* [1864]). However, where the parties believe they are contracting about the same thing and are merely mistaken as to its quality, the contract is valid.

Mistake as to the existence of the subject matter. Where, unknown to the parties, the subject matter of the contract has ceased to exist prior to the contract being made, that contract is void (*Strickland v. Turner* [1852]). Where the subject matter ceases to exist after agreement but before performance, the contract may be frustrated (see below).

Mistake as to the person. Where one party is mistaken as to the identity of the other party, this will only make the contract void where the precise identity of the person is relevant to the decision to enter the contract (*Cundy v. Lindsay* [1878]).

Misrepresentation

Where a statement made during contractual negotiations does not become a term of the contract, it remains a pre-contractual representation. If that statement was untrue, it is a misrepresentation, and the misrepresentee may have a remedy against the misrepresentor. Whether this is the case depends upon the following factors.

Nature of the representation. It must be a statement of fact, not of law, opinion or intention. Generally, it must be a positive statement. Silence will not amount to misrepresentation (*Fletcher v. Krell* [1873]) except in three circumstances:

- where the representor fails to inform the representee of a change in circumstance which makes a previously true statement false (*With v. O'Flanagan* [1936]);
- where the representation, although literally true, leaves out important information which thereby creates a false impression (*Nottingham Patent Brick & Tile Co v. Butler* [1886]);

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- where the contract is one of the utmost good faith (*e.g.* an insurance contract).

Nature of the inducement. A misrepresentation is only operative where it induces the misrepresentee to enter into the contract. Therefore the representee must show he relied on the truth of the statement in making that decision. Where he carried out independent investigations into its truth, there is no such reliance (*Attwood v. Small* [1838]). Where, however, the representee had the opportunity to carry out such investigations but declined to do so, there is reliance on the statement (*Redgrave v. Hurd* [1881]). While the representation must be a factor in the representee's decision, it need not be the sole factor (*Edgington v. Fitzmaurice* [1885]).

Nature of the misrepresentation. There are three types of misrepresentation:

- **fraudulent**—where the representor makes the statement knowing it to be false, believing it to be false or being reckless as to its truth (*Derry v. Peek* [1889]).
- **negligent**—where the representor believes the statement to be true but that belief is unreasonable.
- **innocent**—where the representor believes the statement to be true and that belief is reasonable.

The consequences of misrepresentation

An operative misrepresentation makes the contract voidable. The remedies available to the misrepresentee depend upon the type of misrepresentation:

- **fraudulent**—damages (in the tort of deceit) and rescission;
- **negligent**—damages (under section 2(1) of the Misrepresentation Act 1967) and rescission (or damages in lieu under section 2(2) of the 1967 Act);
- **innocent**—rescission (or damages in lieu under section 2(2) of the 1967 Act).

Revision Notes

You should now write your revision notes for Vitiating Factors. Here is an example for you and some suggested headings:

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VF②—Voidable contracts

- innocent pty may avoid contract and seek rescission (return to pre-contractual position)
- rescission = equitable = discretionary—not granted:
  - affirmation
  - restitution not possible (substantial restitution OK)
  - legitimate 3rd pty rights

VF①—Void contracts

VF②—Voidable contracts

VF③—Lack of Form

VF④—Duress & Undue Influence

VF⑤—Illegality

VF⑥—Public Policy

VF⑦—Mistake

VF⑧—Misrepresentation

Using your cards, you should now be able to write a short paragraph in response to each of the following questions:

Explain the rules of law relating to each of the following:

1. Void contracts.
2. Voidable contracts.
3. Lack of required formality.
4. Duress and undue influence.
5. Illegality.
6. Public policy.

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7. Mistake.
8. Misrepresentation.

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21 Contract Law - Terms of the Contract

Key Points

After reading this chapter, you will be able to;

- **describe** contractual terms by status.
- **describe** contractual terms by origin;

It is the terms of the contract that define the rights and duties of the parties to it. These may be classified in two ways:

- **By status**—this creates three categories:
  - **conditions**—the most significant or important terms: they define the principal rights and duties of the parties, and are central to or lie at the heart of the contract;
  - **warranties**—the less significant or minor terms: they identify the secondary rights and duties of the parties, and lie at the periphery of the contract;
  - **innominate terms**—terms whose status or importance is unclear and that can only be decided in light of the consequences of the term being breached.
- **By origin**—this creates two categories:
  - **express terms**—terms expressly stated by the parties themselves;
  - **implied terms**—terms implied into the contract by law, either common law or statute. At common law, the courts are reluctant to interfere in the nature of the contract as decided by the parties. Therefore, they will only imply a term where it is both reasonable and obvious and necessary to give business efficacy or make commercial sense of the contract (*The Moorcock* [1889]; *Liverpool C.C. v. Irwin* [1977]). The most obvious source of such implied terms is commercial custom and practice (*Hutton v. Warren* [1836]). Regarding statute, a number of Acts of Parliament imply terms into contracts, *e.g.* the **Sale of Goods Act 1979** and the **Supply of Goods and Services Act 1982**.

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Revision Notes

You should now write your revision notes for Terms of the Contract. Here is an example for you and some suggested headings:

Terms①—Status

- conditions—central or primary obligations
- warranties—peripheral or secondary obligations
- innominate terms—status unclear—determined by consequences of breach

Terms①—Status

Terms②—Origin (express and implied)

Using your cards, you should now be able to write a short paragraph in response to each of the following questions:

1. Explain the distinction between conditions, warranties and innominate terms.
2. Explain the difference between express and implied terms.

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22 Contract Law—Discharge of Contract

Key Points

After reading this chapter, you will be able to:

- describe discharge by performance and agreement;
- describe discharge by frustration;
- describe discharge by breach.

Performance

Most contracts are discharged by each party performing his obligations. The general rule is that each party must perform his obligations exactly and entirely, otherwise they will be in breach and will forfeit any rights under the contract. However, this rule may operate very harshly, and there are a number of significant exceptions:

Severable contracts. Where the contract consists of obligations which can be sub-divided (*e.g.* to carry freight at so much per ton), a party may claim for those elements performed while remaining liable for breach of those not performed (*Ritchie v. Atkinson* [1808]; *Atkinson v. Ritchie* [1809]).

Prevention of performance. Where one party is prevented from performing his obligations by the other, that failure of performance will not bar that party from bringing an action for breach of contract by the other (*Planche v. Colburn* [1831]).

Acceptance of partial performance. Where one party has partially performed his obligations and the other has accepted this, this may be regarded as the abandonment of the original contract and the creation of a new, less extensive one. However, this will only apply where the other party has a genuine choice whether to accept the partial performance (*Sumpter v. Hedges* [1898]).

Substantial performance. Where one party has substantially performed their obligations, then they may enforce the contract subject to a reduction to compensate for the defect in

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performance (*Hoenig v. Isaacs* [1952]). This only applies where the defect in performance is minor, *i.e.* where the other party has still received a substantial benefit (*Bolton v. Mahadeva* [1972]).

Tender of performance. Where one party tenders performance and this is rejected by the other, the tender is regarded as equivalent to performance. This exception does not apply where the obligation is one to make payment—an unsuccessful tender of payment does not release the person of the obligation to pay.

Agreement

The parties to the contract can agree to vary or discharge it. As such an agreement amounts to a contract to end a contract, it must be supported by fresh consideration.

Frustration

Generally, contractual liability is strict—it is not necessary to show that the party in breach was at fault in their failure to perform. However, the doctrine of frustration is one area of non-performance where fault (or rather the absence of fault) does play a part. In **Taylor v. Caldwell** [1863], it was held that where performance of the contract had become impossible and neither party was at fault, then both parties were discharged from any further obligations. This position has subsequently developed into the modern doctrine of frustration: **the parties to a contract are released from any further obligations where an unforeseen event occurs which makes further performance either:**

- **impossible,**
- **illegal, or**
- **radically different from that anticipated by both parties at the time the contract was made**

and the frustrating event was not the fault of either party.

These three variations require further explanation:

Impossibility. Subsequent impossibility in performance may occur in three ways:

- subject matter is destroyed (*Taylor v. Caldwell* [1863]);

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- subject matter becomes unavailable (*Jackson v. Union Marine Insurance Co Ltd* [1874]; *Morgan v. Manser* [1948]);
- in a contract for personal services, one of the parties dies.

Illegality. Where a subsequent event (*e.g.* new legislation or the outbreak of war) makes further performance illegal, the contract will be frustrated (*Fibrosa Spolka Akcyjna v. Fairburn Lawson Combe Barber Ltd* [1943]).

Radical difference. Where further performance would produce a result radically different from that anticipated by both parties at the time the contract was made, the contract will be frustrated (*Krell v. Henry* [1903]; *Herne Bay Steamboat Co v. Hutton* [1903]). To amount to a radical difference, the actual and anticipated results of performance must be almost totally different, *e.g.* events which would lead to a reduction in anticipated profits will not frustrate the contract (*Davis Contractors Ltd v. Fareham U.D.C.* [1956]).

A party cannot plead frustration where the frustrating event is due to their own fault, *i.e.* the frustration must not be self-induced (*Maritime National Fish Ltd v. Ocean Trawlers Ltd* [1935]).

The consequences of frustration

While the question whether a contract has been frustrated remains an issue of common law, the consequences of frustration are regulated by statute—**Law Reform (Frustrated Contracts) Act 1943**:

- frustration immediately discharges the contract and releases the parties from any further obligations (**section 1(1)**);
- money paid prior to the frustrating event can be recovered (**section 1(2)**);
- money due to be paid prior to the frustrating event, but not in fact paid, ceases to be payable (**section 1(2)**);
- expenses incurred under the contract may be recovered up to the amount of sums paid or due to be paid prior to the frustrating event (**section 1(2)**). If no sums had been or were due to be paid, no expenses may be recovered;
- a party that has acquired a valuable benefit under the contract prior to the frustrating event may be ordered to pay a reasonable sum for it, whether or not any sums had been or were due to be paid (**section 1(3)**).

This allows the court to apportion any loss resulting from frustration in a fair way.

Breach

Breach of contract takes two forms:

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- **Actual breach.** A party fails to perform any or all of their obligations (non-performance) or performs them improperly (defective performance).
- **Anticipatory breach.** A party gives a clear indication of an intention not to perform their obligations. This gives rise to an immediate cause of action (*Hochster v. De la Tour* [1853]).

The consequences of breach depend upon the status of the term breached:

- **Breach of condition**—gives the injured party a right to damages and the option to repudiate (treat as discharged) the contract (*Heyman v. Darwins Ltd* [1942])—**repudiatory breach.**
- **Breach of warranty**—gives the injured party a right to damages only. They remain bound to fulfil their own obligations under the contract—**mere breach.**
- **Breach of an innominate term**—here the rights of the injured party depend upon the consequences of the breach (*Cehave NV v. Bremer Handelsgesellschaft mbH, The Hansa Nord* [1976]). If the breach substantially deprives the injured party of his anticipated contractual benefits, it is a breach of condition. Where the consequences are less severe, it is a breach of warranty.

Revision Notes

You should now write your revision notes for Discharge of Contract. Here is an example for you and some suggested headings:

Discharge③—Breach

- actual/anticipatory
- condition = repudiatory breach
- warranty = mere breach
- innominate—depends on consequences (Hansa Nord)

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Discharge①—Performance & Agreement

Discharge②—Frustration

Discharge③—Breach

Using your cards, you should now be able to write a short paragraph in response to each of the following questions:

Explain the rules of law relating to:

1. Discharge by performance.
2. Discharge by agreement.
3. Discharge by frustration.
4. Discharge by breach.

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