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ECONOMIC DURESS BY THREATENED BREACH OF CONTRACT

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ABSTRACT

This paper examines the development and scope of the doctrine of economic duress. It argues that expansion of the doctrine of duress to include the exercise of economic pressure requires a set of consistent principles of application if the doctrine is to be a useful tool in curbing unacceptable commercial pressures. The courts have so far failed to provide a clear test for determining the existence of economic duress. A part of the reason for this is the lingering effect of the "overborne will theory." This theory acts as a conceptual bar to the development of a responsive and predictable test for economic duress. This paper supports the modern test for duress proposed by Lord Scarman in Universe Tankships Inc of Monrovia *v* International Workers' Federation *[1982] AC 366 and identifies illegitimacy of pressure as the key element in a principled development of the doctrine of economic duress. Finally a comprehensive test for establishing the illegitimacy of pressure is proposed based on the concept of bad faith.*

The text of this paper (excluding contents page, footnotes and bibliography) comprises approximately 12,500 words.

ECONOMIC DURESS BY THREATENED BREACH OF CONTRACT

I INTRODUCTION

The existence of the doctrine of duress is illustrative of the law's willingness, in certain circumstances, to interfere in relationships which, on their face, appear entirely consistent with the general law. Claims for duress arise where a party has applied pressure to another in order to coerce that other party to enter an agreement or to take some other action. An agreement resulting from the exercise of duress may be entirely consistent with the law, however, the courts will, in appropriate circumstances, examine the way in which such agreements are brought about. Even in the eighteenth and nineteenth centuries, at the height of the philosophy of *laissez-faire*, the law would interfere where duress could be shown. However, as will be seen below, the concept of duress was, at that time, substantially more restricted than is the case today.

The application of the doctrine of duress has extended far beyond its origins in threats to the person and to property. If duress is to remain an effective and responsive doctrine it is essential that its expansion be based on a coherent and consistent conceptual basis. A principled approach must be taken in the development of duress. This paper identifies the past and current judicial approaches to the doctrine of duress and attempts to establish the most appropriate basis on which to develop the concept of economic duress. The concept of illegitimacy of pressure is identified as the key to establishing a workable doctrine of economic duress and a comprehensive test for illegitimacy is proposed.

II THE CONCEPT OF DURESS

A The Justification for Relief

It is overly simplistic to say that relief is justified in cases of duress because the weaker party has been pressured to act in some way. Pressures of

various sorts and weights are constantly driving the way in which we act. We accept many types of pressure as ordinary incidents of everyday life:[1]

> [I]n life, including the life of commerce and in finance, many acts are done 'under pressure, sometimes overwhelming pressure'; but they are not necessarily done under duress. That depends on whether the circumstances are such that the law regards the pressure as legitimate.

There exist, however, certain pressures which the courts see as justifying relief for those exposed to them. That the relief provided where duress is established is the recovery of money paid or the setting aside of a contract is a clear indication that the principal aims of duress are to protect the victim and to prevent the oppressor from gaining from his or her actions. Retribution or punishment of the coercer is not an aim of the doctrine of duress. A remedy is provided to give effect to the victim's rights, principally the right to freedom of choice. This right to freedom of choice is not, however, an unlimited freedom. It is limited by the moral and legal constraints imposed by society. The particular freedom that the doctrine of duress guarantees is the freedom to choose free of certain pressures that the law does not countenance. Seddon[2] suggests that this concern for the rights of the victim can be justified in a number of ways. Morally, the dignity of the individual dictates that this freedom be protected. So too politically, where the very concept of democracy demands it, and economically, where, it is argued, wealth is maximised in a market where both buyers and sellers are able to exercise choice without undue coercion. These justifications may seem to suggest that relief should be provided in response to any pressure. Freedom, however, "must be limited in order to be possessed".[3]

Seddon provides another possible justification for the provision of relief in response to unacceptable pressure by viewing such pressure as a breach of the social contract. Part of the social contract involves the surrender of total freedom in return for guarantees of a more limited freedom. Thus individuals surrender the right to coerce in exchange for freedom from the coercion of

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1 *Universe Tankships Inc of Monrovia* v *International Transport Workers' Federation* [1982] AC 366, 560-561 per Lord Scarman.

2 N Seddon "Compulsion in Commercial Dealings" in PD Finn (ed) *Essays on Restitution* (The Law Book Company, Sydney, 1990) 138.

others. However, at least in societies based on the free market system, not all rights of coercion are surrendered. For example, as Stewart points out, "the free market system, and the economic individualism which still nominally underlies it, basically assume the existence of, and submission to, commercial pressure."[4] In almost every commercial transaction one party is in a superior bargaining position to the other. A capitalist society allows its members to utilise such strength in certain ways to secure commercial advantages.

The line between acceptable and unacceptable forms of coercion is drawn primarily in response to the social and moral attitudes of society. Thus while originally only coercion based on threats to the person grounded relief under the doctrine of duress, the prohibited forms of coercion have now expanded. Today we are entitled to be free of many more forms of coercion and correspondingly we are denied the right to utilise them ourselves.

Ultimately, however, these justifications for the granting of relief must be balanced against the competing interests for non-intervention. This balancing is particularly in evidence in the case of economic duress. Application of the doctrine of economic duress must be tempered by the need for commercial certainty and by the doctrine of freedom of contract.

B The Nature of Relief

The nature of the relief available where duress has been established depends largely upon the advantage secured for the stronger party by the exercise of duress. Where that advantage is the payment of money, the restitutionary remedy of an action for money had and received is available to the victim.[5] Where the duress has resulted in the entry into a contract, that contract is regarded as being voidable at the instance of the victim.[6] Where a person performs services under duress a claim for *quantum meruit* will be available to the victim allowing him or her to recover reasonable remuneration for those

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4 A Stewart "Economic Duress - Legal Regulation of Commercial Pressure" (1984) Melbourne University Law Review 410, 422.

5 *Astley* v *Reynolds* (1731) 2 Strange 915; 93 ER 939 (KB); *Maskell* v *Horner* [1915] 3 KB 106; See also Lord Diplock's comments in *Universe Tankships Inc of Monrovia* v *International Transport Workers' Federation* above n 1, 385, which, while relating to economic duress are of wider application.

6 *North Ocean Shipping Co Ltd* v *Hyundai Construction Co Ltd (The Atlantic Baron)* [1979] QB 705, 719; *Pao On* v *Lau Yiu Long* [1980] AC 614, 634, 636; *Universe*

services.[7] The transfer of goods under duress can be remedied by a claim for *quantum valebat.*

Non-restitutionary remedies will continue to be available to the victim where the duress itself constitutes a tort or a breach of contract. Thus, in such circumstances, ordinary principles of tort and contract will apply.

In addition, the exercise of duress may constitute a breach of section 23 of the Fair Trading 1986 which provides that:

> No person shall use physical force or harassment or coercion in connection with the supply or possible supply of goods or services or the payment of goods or services.

Where this is the case the Fair Trading Act 1986 provides a wide range of orders that a court may make on the application of the victim. These orders can include:[8]

- an injunction;
- a declaration that the contract is void;
- a variation of the contract;
- requiring the coercer to refund money or return property to the victim;
- requiring the coercer to pay to the victim the amount of any loss.

Thus there are potentially a number of avenues of relief, both restitutionary and non-restitutionary, available to the victim of duress.

C Denial of Relief

There will be occasions when, despite the existence of operative duress, relief will be denied to the victim.

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7 Lord Goff and G Jones *The Law of Restitution* (3ed, Sweet & Maxwell, London,

1 Causation

Relief will only be justified where there exists a causal link between the pressure that has been exerted and the victim's subsequent action. It was made clear by the Privy Council in *Barton* v *Armstrong*[9] that the pressure need not be the sole motivating force so long as it is *a* cause of the victim's action. Thus, in that case, relief was granted to the plaintiff despite there having been sound business reasons for his actions. The Court was satisfied that the threats to the plaintiff's safety had been a factor in his decision to do as the defendant demanded. Lord Goff took a somewhat different view of the causation requirement in respect of economic duress in *Dimskal Shipping Co* v *International Transport Workers' Federation (The "Evia Luck")*.[10] Lord Goff considered that the pressure must have constituted a "significant cause inducing the plaintiff to enter into the relevant contract."[11] However, Lord Goff cites in support of this statement the cases of *Barton* v *Armstrong*[12] and *Crescendo Management Pty Ltd* v *Westpac Banking Corporation*[13] both of which clearly state that the pressure need only be "one of the reasons for the person entering into the agreement".[14] Regardless, where it can be shown that the victim would have acted in the same manner in the absence of duress, this will provide a defence to the coercer and the victim will have no restitutionary remedy. The onus here is on the coercer to prove that the pressure had no effect.[15]

2 Affirmation

Restitutionary relief will also be denied where the victim can be taken to have subsequently affirmed the contract entered into or the payment made under duress. Because a contract entered into under duress is voidable and not void, such a contract may be affirmed by the victim. Affirmation may be by way of a positive act on the part of the victim but equally it would appear that delay in seeking a remedy may constitute affirmation. In *North Ocean Shipping Co Ltd* v *Hyundai Construction Co Ltd (The Atlantic Baron)*[16] while there was found to

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9 [1976] AC 104, 118-119.
10 [1992] AC 152.
11 Above n 10, 165.
12 Above n 9.
13 (1988) 19 NSWLR 40.
14 Above n 13, 46.
15 *Barton* v *Armstrong*, above n 9; *Cresendo Management Pty Ltd* v *Westpac Banking*

be duress on the facts, relief was denied due to the absence of protest on the part of the victim once the pressure was no longer operative and the eight month delay between the release of the pressure and the bringing of a claim by the victim.

That any action taken while under the effect of duress may be affirmed by lapse of time after the duress has ceased to operate is consistent with the position in respect of undue influence. There are a number of cases of undue influence in which relief has been denied as a result of delay in seeking to set aside the relevant transaction.[17] Affirmation requires a "fixed, deliberate and unbiased determination not to impeach the transaction"[18] and the courts have been prepared to accept that delays of several years will provide a basis from which to infer such a determination. While the delay in *The Atlantic Baron* was only eight months, arguably, in a commercial context this is sufficient to establish affirmation. The need for commercial certainty demands that parties can rely on the validity of the contracts they have made. If large commercial contracts could be set aside eight months after the pressure inducing them had ceased and when there had been no indication given to the dominant party that the victim had entered the contract under duress, commerce in general would be adversely affected. Commercial parties could not rely on the validity of their transactions which would increase the perceived risks in transacting making parties less willing to commit to transactions.

Certainly where it could be said that the coercer was aware of the duress and its effect a court will be far less likely to find affirmation in silence. Thus in *Atlas Express Ltd* v *Kafco (Importers and Distributors) Ltd*[19] a one month delay in seeking relief was not even argued by counsel to amount to affirmation. In that case not only was the delay relatively short and over the Christmas holiday period, but when the threat had been made by Atlas Express Ltd ("Atlas"), it had deliberately made itself unavailable to discuss the situation. The actions of Atlas demonstrate that it was well aware that Kafco (Importers and Exporters) Ltd ("Kafco") were entering the contract unwillingly.

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17 *Wright* v *Vanderplank* (1856) 8 De GM & G 133; 44 ER 340 (action commenced 10 years after the gift was made); *Turner* v *Collins* (1871) 7 Ch App 329 (action commenced seven years after the benefit was conferred); *Allcard* v *Skinner* (1887) 36 Ch D 145 (no attempt to recover property until six years after the undue influence had ceased).

18 M Cope *Duress, Undue Influence and Unconsionable Bargains* (The Law Book

3 *Third parties*

Further difficulties in obtaining relief can arise where the duress has resulted in the conferment of a benefit on a third party who is without notice of the duress.[20] Although the third party will have been enriched at the victim's expense, restitution may not be possible where the third party can establish a defence such as change of position.[21] Similarly, relief will be denied against the bona fide purchaser for value without notice.[22] These principles are well established in the context of undue influence and are equally applicable in the case of duress.[23] In such a case the victim must look to other than restitutionary remedies. Where the coercion has occurred "in trade" the seeking of an order under section 43 of the Fair Trading Act 1986 that the coercer pay to the victim the amount of any loss would seem to be a particularly appropriate avenue of relief in such circumstances.

III EARLY FORMS OF DURESS

A *Duress of the Person*

In its original form, duress at common law extended only to threats of violence against a person. Relief was further limited by the requirement that the threat had to be to the life, the loss of a limb, or to the imprisonment of the party or his or her family.[24] Early authorities also required that the threat be one which would have coerced the "constant man".[25] This objective test meant that there was little room for relief for those of less than average robustness.

Today duress of the person is wider in its scope. A greater range of threats are seen to be within its ambit and the "constant man" has been replaced by a subjective test which focuses on the effect of the pressure on the coerced party. This broadening of the scope of duress of the person came about from

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20 The third party who has notice of the duress can be in no better position than the person who exercises the duress (see Goff and Jones, above n 7, 230 at n 9).

21 *Lipkin Gorman (A Firm)* v *Karpnale Ltd* [1991] 2 AC 548; Goff and Jones, above n 7, 231.

22 Cope, above n 18, 223.

23 Cope, above n 18, 222.

24 DW Greig and JLR Davis *The Law of Contract* (The Law Book Company Ltd, Sydney, 1987) 942.

25 See PD Maddaugh and JD McCamus *The Law of Restitution* (Canadian Law Book

the fusion of law and equity in the mid-1870's. Prior to this, while common law duress had restricted itself to dealing with threats to life, health, liberty or physical comfort, equity encompassed a broader concept of coercion or duress. Equity offered protection from the effects of threats by a stronger party where such threats had affected the judgment of the weaker party:[26]

> It was considered to be equitable fraud for the stronger party to retain the advantage of a contract which he had extorted from one unable to protect himself by reason of the pressure brought to bear on him.

Since fusion it is arguable that equitable and common law duress have become indistinguishable. Support for this view can be found in the case of *Barton* v *Armstrong*.[27] In that case the Privy Council were prepared to consider both common law and equity cases in coming to their conclusion:[28]

> Their Lordships do not think that the common law authorities are of any real assistance.... On the other hand they think that the conclusion to which Jacobs JA [in the Court below] came was right and that is supported by the equity decisions.

Greig and Davis argue that this could only be justified on the basis that the two forms of duress had become identical.[29]

This increasing breadth of application meant that moral pressure could ground a claim of duress. In *Kaufman* v *Gerson*[30] the English Court of Appeal held that duress was established where the plaintiff had threatened a wife "with the dishonour of her husband and children". The plaintiff had threatened to bring criminal charges against the defendant's husband unless the defendant agreed to pay the money misappropriated by her husband. The Court was of the opinion that, had she not complied, the proceedings "would probably have resulted in the ruin of the husband, and the disgrace of his wife and children."[31] The Court saw no difference in principle between coercion based upon threats to health and liberty and coercion by moral pressure.

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26 Greig and Davis, above n 24, 942.
27 [1973] 2 NSWLR 598; appealed to the Privy Council, above n 9.
28 Above n 9, 118.
29 Above n 24, 943.

The move away from the "constant man" requirement toward a subjective test added further flexibility to the application of duress of the person. It also reflected a greater concern for the rights and freedoms of individuals by providing recognition that a person is no less coerced simply because a more robust person might have better weathered the pressure that was applied. This rejection of a purely objective test is to be welcomed in respect of duress to the person and duress of goods where threats are directed at fundamental rights. However, the subjective approach is not as appropriate in the case of economic duress where the rights attacked are not of such a fundamental nature. The requirement of no reasonable alternative in the doctrine of economic duress provides an objective element to the inquiry. Where a reasonable alternative exists economic duress will not be established.[32]

B Duress of Goods

Duress of goods involves threats directed against the property of the victim in order to coerce him or her into acting in a particular manner. The archetypical case is of a demand for payment (or for the agreement to pay) money to avoid the seizure of goods or to secure the release of goods unlawfully seized. It was suggested by Kerr J in *Occidental Worldwide Investment Corporation* v *Skibs A/S Avanti (The Siboen and The Sibotre)*[33] that duress of goods could extend to threats to burn down a house or to slash a painting.

Previously, a peculiar distinction was drawn between the payment of money under duress of goods and the entering into a contract in the same circumstances. It has long been established that money paid under duress of goods is recoverable.[34] However, until recently, it was thought that a promise to pay, supported by fresh consideration, extracted under duress of goods was binding.[35] This distinction has been swept away by modern cases and today a contract obtained under duress of goods is, as under other forms of duress, voidable.[36]

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32 See below Part VI.

33 [1976] 1 Lloyd's Rep 293, 335.

34 *Astley* v *Reynolds*, above n 5.

35 *Skeate* v *Beale* (1841) 11 AD & E 983; 113 ER 688 (KB).

36 See *The Siboen and The Sibotre*, above n 33, 335-336; *North Ocean Shipping Co Ltd* v *Hyundai Construction Co Ltd (The Atlantic Baron)*, above n 6; *Universe Tankships*

A recent example of the rejection of this distinction can be found in *Hawker Pacific Pty Ltd* v *Helicopter Charter Pty Ltd.*[37] Hawker Pacific Pty Ltd ("Hawker") had agreed to repaint a helicopter owned by Helicopter Charter Pty Ltd ("HC"). On completion of the repainting HC were not satisfied with the quality of the work done and Hawker eventually agreed to rectify the problems at their own expense. However, once the work had been satisfactorily completed Hawker refused to release the helicopter to HC until HC had signed a document agreeing to pay Hawker a sum of money and releasing Hawker from any liability in respect of the paint job. Hawker were aware at the time that HC required the helicopter immediately for charter work.

The New South Wales Court of Appeal held that the agreement to pay and the release of liability were obtained under duress and as such were liable to be set aside. Clarke JA said of the distinction between money paid under duress and agreements to pay obtained in the same circumstances:[38]

> This distinction, if correct, leads to the absurd result that if A paid money under duress of goods he could recover the money paid but if he entered into a contract to pay money under similar duress he could not avoid the contract and would be obliged to pay the moneys due thereunder.
>
> In my opinion the distinction is not supportable and to the extent that *Skeate* is authority for the so-called traditional view it should not be followed.

Similarly, in terms of a restitutionary analysis this distinction cannot be supported. Whether there is a payment made under duress or an agreement to pay, the coercer will be unjustly (by the use of duress) enriched at the victim's expense.[39] Enrichment is present whether the obligation is executory or executed.

In addition, even in the case of a payment of money there will often have been, between demand and payment, a *scintilla temporis* where there existed an agreement to pay the sum. With the benefit of hindsight it seems strange that it took 150 years for the law to rid itself of this bizarre distinction.

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37 (1991) 22 NSWLR 298.

38 Above n 37, 306.

IV AN APPROPRIATE BASIS FOR ECONOMIC DURESS

A The Two Approaches

Traditionally the rationale for the application of duress was that the coerced party's will was "overborne", that there was no true consent or agreement.[40] This theory was approved by the Privy Council in *Pao On* v *Lau Yiu Long*[41] where Lord Scarman stated it in these terms:[42]

> Duress, whatever form it takes, is a coercion of the will so as to vitiate consent.... It must be shown that the payment made or the contract entered into was not a voluntary act.

However, the overborne will theory has been criticised by academics as being logically indefensible and, in practice, impossible to implement.[43] As Atiyah points out, "[a] victim of duress *does* normally know what he is doing, *does* choose to submit, and does intend to do so."[44] The victim's will is not "overborne", there exists a very real intention to act in that manner. On one view, the more extreme the pressure, the more real the consent.[45]

Further, the overborne will theory was impossible to reconcile with the fact that duress renders a contract voidable and not void.[46] If there really were no true consent then, logically, any resulting "agreement" must be void *ab initio*.

This academic criticism was eventually taken on board by the judiciary and modern cases in the United Kingdom and Australia appear to have left

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40 PS Atiyah "Economic Duress and the 'Overborne Will Theory'" (1982) 98 Law Quarterly Review 197, 198.

41 Above n 6.

42 Above n 6, 635-636.

43 PS Atiyah *The Rise and Fall of Freedom of Contract* (Clarendon Press, Oxford, 1979) 436. The overbourne will theory of duress was rejected by the House of Lords in the context of the criminal law in the case of *Lynch* v *DPP of Northern Ireland* [1975] AC 653.

44 Atiyah, above n 40, 200.

45 JP Dawson "Economic Duress - An Essay in Perspective" (1947) 45 Mich LR 253,

behind the overborne will theory:[47]

> In my opinion the overbearing of the will theory of duress should be rejected. A person who is the subject of duress usually knows only too well what he is doing. But he chooses to submit to the demand or pressure rather than take an alternative course of action. The proper approach in my opinion is to ask whether any applied pressure induced the victim to enter into the contract and then ask whether that pressure went beyond what the law is prepared to countenance as legitimate?

This followed the decision of the House of Lords in *Universe Tankships Inc of Monrovia* v *International Transport Workers' Federation*[48] in which Lord Scarman, without directly acknowledging the fact, effectively discarded the overborne will theory. In that case Lord Scarman built on his earlier formulation of the test in *Pao On* stating that:[49]

> The authorities upon which these two cases [*Barton* v *Armstrong* [1976] AC 104 and *Pao On*] were based reveal two elements of the wrong of duress: (1) pressure amounting to compulsion of the will of the victim; and (2) the illegitimacy of the pressure exerted. There must be pressure, the practical effect of which is compulsion or the absence of choice. Compulsion is variously described in the authorities as coercion or the vitiation of consent. The classic case of duress is, however, not the lack of will to submit but the victim's intentional submission arising from the realisation that there is no practical choice open to him. This is the thread of principle which links the early law of duress (threat to life or limb) with later developments....

Thus the focus of the duress inquiry in Lord Scarman's view was not on establishing an involuntary act, but rather on identifying an intentional submission to illegitimate pressure.

B The Difference Between the Approaches

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47 *Cresendo Management Pty Ltd* v *Westpac Banking Corp*, above n 13, 45-46. See also Lord Goff's comments in *Dimskal Shipping Co* v *International Transport Workers' Federation*, above n 10, 166.

Although expressed in very different terms these approaches may not be so different in application. Two aspects of the approaches must be considered: the effect of the pressure and the form of the pressure.

1 The effect of the pressure

In terms of the practical effect of the pressure it would appear that they describe the same requirement. In *Pao On* the Privy Council detailed the material factors in determining whether a person's will is overborne for the purposes of the duress inquiry:[50]

> In determining whether there was a coercion of will such that there was no true consent, it is material to inquire whether the person alleged to have been coerced did or did not protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have an alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it. All these matters are, as was recognised in *Maskell* v *Horner* [1915] 3 K.B. 106, relevant in determining whether he acted voluntarily or not.

Under the test enunciated by Lord Scarman in *Universe Tankships* the effect that the pressure must have on the victim was described by him as "compulsion of the will" which he went on to define as intentional submission in the absence of practical choice. The factors relevant in determining this absence of practical choice were set out by Lord Scarman:[51]

> [T]he absence of choice can be proved in various ways, e.g. by protest, by the absence of independent advice, or by a declaration to go to law to recover the money paid or the property transferred: see *Maskell* v *Horner* [1915] 3 K.B. 106. But none of these evidential matters goes to the essence of duress. The victim's silence will not assist the bully, if the lack of any practicable choice but to submit is proved.

Thus the two approaches apply the same criteria in examining the effect of the pressure on the victim .[52] So while the overborne will theory suggests

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50 Above n 6, 635.
51 Above n 1, 400.
52 See M Trebilcock "An Economic Approach to Unconscionability" in B J Reiter and J

the need for automatism on the part of the victim before duress is established, in practice the requirement is far less extreme. The language of the overborne will theory is inconsistent with its application. This is illustrated by Chandler's[53] rationalisation of the overborne will theory. Chandler views the term "vitiation of consent" as denoting "involuntary intent".[54] That is, that "the party's actions are intentional but with a countervailing desire that the ensuing consequences are nullified."[55] Chandler goes on to state that:[56]

> Perhaps the true hallmark of coercion is the lack of voluntary action by the weaker party. The word "voluntary" infers, at the very least, the absence of effective choice: the choice to pursue a legal remedy, the choice of not submitting, the choice to do something different. It is the unavoidable and serious consequences of non-submission which lies at the heart of coercion.

Similarly, in the United States, Williston[57] notes the tendency of courts to use terms such as "involuntary" and "lack of free will" but states that these terms do not mean "no choice", rather they illustrate compulsion to choose between "regrettable alternatives". As the Supreme Court of Ohio held in *Tallmadge* v *Robinson,*[58] "[t]he real and ultimate fact to be determined in every case is whether the party affected really had a choice; whether he had his freedom of exercising his will."

The fact that the two tests overlap in terms of the required effect on the victim can be illustrated by the case of *Pao On* itself. In *Pao On* the Privy Council were required to consider a complex commercial transaction in which the plaintiffs claimed to have been forced to make a promise by threats to break an existing contractual agreement. The plaintiffs had entered an agreement of sale and purchase with Fu Chip Investment Co Ltd ("Fu Chip"), whose shares were owned predominantly by the defendants, in respect of the plaintiffs' shares in Tsuen Wan Shing On Co Ltd ("Shing On"). The payment for these shares was to be by way of shares in Fu Chip. The defendants were concerned that the

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so-called duress cases is whether the conduct of the party against whom the doctrine is pleaded was such as to remove from, or take advantage of, effective access by the other party to a workably competitive range of alternative choices."

53 PA Chandler "Economic Duress: Clarity or Confusion?" [1990] Lloyd's Maritime and Commercial Law Quarterly 270.

54 Above n 53, 274.

55 Above n 53, 274-275.

56 Above n 53, 275.

plaintiffs might dispose of the Fu Chip shares too quickly thereby adversely affecting the value of Fu Chip's shares in general. In order to avoid this, the plaintiffs agreed to retain 60% of the shares for a year in return for a guarantee from the defendants that they would then purchase the shares at a set price (the subsidiary agreement). The Fu Chip shares were expected to rise in value and the plaintiffs realised that they had made a bad bargain. As such, the plaintiffs told the defendants that, unless the guarantee was varied to one of indemnity, the plaintiff would not complete the main contract for the transfer of the Shing On shares. The defendants agreed to the change due to the fear that news of a problem with the main contract would affect public confidence in Fu Chip. The value of the shares in fact fell and, when the plaintiffs sought to rely on the contract of indemnity, the defendants argued that it was voidable for economic duress.[59]

The Privy Council held that economic duress was not established in this case. Although the Privy Council based their decision on the overborne will theory, the question of the existence of alternatives was considered an important evidential factor and, in fact, appears to have formed the basis of their decision:[60]

> In the present case there is unanimity amongst the judges below that there was no coercion of the first defendant's will. In the Court of Appeal the trial judge's findings...that the first defendant considered the matter thoroughly, chose to avoid litigation, and formed the opinion that the risk in giving the guarantee was more apparent than real was upheld.

The defendants had a reasonable alternative available to them. They knew that the main agreement between Fu Chip and the plaintiffs was still valid and that Fu Chip could have sued the defendants for specific performance or damages. Further, the trial Judge found that the success or failure of the main contract could not have affected the true value of Fu Chip's shares. As such the defendant had a real option of exercising a legal remedy. The available alternative "was not one which the fact situation rendered largely useless in

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59 The plaintiffs could not rely on the subsidiary agreement as it had been cancelled when

practical terms."[61] Clearly the decision that there was no duress would be the same applying the test from *Universe Tankships*.

2 The form of the pressure

Thus the main difference between the two approaches to duress is the express requirement in the modern formulation that the pressure exerted be of a type that the law considers illegitimate. However, in *Universe Tankships*, Lord Scarman made it clear that this requirement was present in the earlier authority. His Lordship stated that "[t]he authorities...reveal two elements of the wrong of duress",[62] the second of these elements Lord Scarman identified as illegitimacy of pressure.

That the law has long distinguished between different types of pressures is clearly illustrated by early restrictions on the types of threats that would ground a claim of duress. Initially duress was restricted to threats to the person. Subsequently threats to property were recognised as grounding claims in duress. Thus duress operated only in respect of certain pressures and there were some pressures that the law would not recognise as justifying relief. For example, in *Smith* v *William Charlick Ltd*[63] a threat not to contract in future was held not to give rise to duress despite the fact that the effect of the pressure on the victim would clearly have satisfied the overborne will theory had the threat been of a type the law recognised as grounding a claim of duress.[64] As Isaacs J stated:

> [I]t is plain that a mere abstention from selling goods to a man except on condition of his making a stated payment cannot, in the absence of some special relation, answer the description of "compulsion," however serious his situation arising from other circumstances may be... .

3 Summary

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61 E MacDonald "Duress by Threatened Breach of Contract" [1989] Journal of Business Law 460, 466.

62 Above 1, 400.

63 (1924) 34 CLR 38.

64 The Wheat Harvest Board had threatened not to do further business with a the victim unless he paid additional fees to the Board. The situation would clearly have had the

The fact that the two approaches are substantially the same in application may seem to suggest that this is merely a terminological and theoretical debate, however, it has very important practical implications. There is something far more important at stake here than the designation of the test. The concept of overborne will stands as a conceptual bar to establishing coherent and consistent principles in the application and development of the doctrine of duress. The overborne will theory is entirely adequate for dealing with established categories of duress where the types of threats that are prohibited have long been established and are directed at protection of fundamental rights. However, as Atiyah points out, there is a need when expanding the doctrine beyond its base in threats to the person and threats to goods to examine the vital issue of "what sort of threats is it permissible to make...."[65]

Expanding the doctrine of duress to economic pressure on the basis of the overborne will theory makes the assumption that any economic pressure will potentially ground a claim for duress and all that must be shown is that the pressure had the required effect on the victim. However, in reality, there are pressures, sometimes overwhelming pressures, that we are prepared to countenance as acceptable.[66] As Stewart states:[67]

> To allow business decisions to be reopened on the ground alone that 'overbearing' pressure, of whatever nature, had been exerted would be to defeat the very notion of a free market and the 'freedom to coerce' (within limits) which it presupposes... . To invalidate a commercial contract or payment merely because one party was 'forced' to do something would be absurd: if something further is required it must surely come from an examination of the *type* of pressure exerted.

Some forms of economic coercion are legally and commercially acceptable and a responsive doctrine of duress must recognise this fact.

A further practical reason for rejecting the overborne will theory is the possibility that the often stated requirement that there be an involuntary act will be adopted literally "by those whose business it is to apply the law."[68] Such a

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65 Above n 40, 202.

66 *Universe Tankships*, above n 1, 560-561.

67 A Stewart "Economic Duress - Legal Regulation of Commercial Pressure" (1984) 14

literal interpretation of the test would result in the usefulness of duress as a means of regulating coercive pressure being dramatically reduced.

C The New Zealand Position

In New Zealand the modern formulation of the test focused on the illegitimacy of the pressure exerted has not found favour. The Court of Appeal appear to be indifferent to overseas developments and cling to the concepts of overborne will and lack of voluntary act. As recently as May 1995 the Court of Appeal could confidently assert that, to demonstrate that pressure brought to bear amounted to economic duress:[69]

> [i]t would have to be shown that his [the victim's] will had been so coerced that his consent to it was completely vitiated and so was not a voluntary act: ***Pao On v Lau Yiu Long*** [1980] AC 614 and ***Moyes & Groves Ltd v Radiation New Zealand Ltd*** [1982] 1 NZLR 368.

Similarly in *Mann* v *Buxton*[70] the Court of Appeal were of the view that "coercion or the overbearing of the defendant's will must be at the foundation of any claim to avoid a contract for duress." The more recent Commonwealth cases on economic duress were not even cited by the Court in either of these cases.

In the High Court there has been some recognition of overseas developments. In *Walmsley* v *Christchurch City Council*,[71] Hardie Boys J applied an amalgam of the two approaches. He held that in order to establish duress it must be shown that illegitimate pressure was exerted on the victim which "amounted to a coercion of the will, so that the contract was not a voluntary act on the part of the party under pressure."[72] A similar amalgamation of the two tests can be seen in the judgment of Tipping J in *Shivas* v *Bank of*

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69 *Rouse* v *Anzon Project No 5 Ltd* (unreported, 30 May 1995, Court of Appeal, CA 211-90).

70 Unreported, 31 July 1990, Court of Appeal, CP 49/90.

New Zealand:[73]

> Unless the party seeking to avoid the contract establishes that his will has been compelled to such an extent as to vitiate his consent, then the question of the legitimacy or illegitimacy of the pressure will not arise. Assuming however that this first hurdle is jumped, the party seeking to avoid the contract must show that his will has been overborne by illegitimate commercial pressure.

Some High Court decisions appear to be more progressive and have adopted overseas developments. In *Foster* v *Phillips*[74] Master Hansen held that:[75]

> The first thing to consider is whether or not at the time the Defendant entered into the settlement and the mortgage, the pressure imposed by the Plaintiff was such as to leave no alternative.

Having dealt with this issue the Master went on to consider whether:[76]

> ...the pressure imposed by the Plaintiffs [was] illegitimate in the sense that both the nature of the pressure and the demands made of the defendant were such that the law should not regard the pressure as legitimate....

However, it seems clear that the law as it stands in New Zealand continues to frame the duress inquiry in terms of the overborne will theory enunciated by the Privy Council in *Pao On*. This is consistent with the doctrine of *stare decisis*. In *Breuer* v *Wright*[77] the Court of Appeal held that it is bound by Privy Council decisions from other jurisdictions. However, it is clear from the foregoing discussion[78] that to cast aside the overborne will theory would not be so much a rejection of the Privy Council's decision in *Pao On* as a clarification of the true principles underlying the decision.

V THE DEVELOPMENT OF ECONOMIC DURESS

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73 [1990] 2 NZLR 327, 345.
74 Unreported, 5 September 1990, High Court Auckland Registry, CP 2845/89.
75 Above n 74,
76 Above n 74,

Economic duress is the exercise of illegitimate economic pressure to force another person to submit to a demand. It is in the arena of economic duress that the line between legitimate and illegitimate pressure is most difficult to draw. While threats to the person or to property clearly breach community standards and seek to deny individual rights and freedoms, the threats involved in economic duress are more subtle and thus can be difficult to characterise as illegitimate. As Greig and Davis point out:[79]

> With regard to duress to the person, the threat of injury or imprisonment is regarded, of itself, as unconscionable.... Life and liberty are so highly prized that the law seeks to discourage the use of such threats to obtain the benefits of a contract.

The law has a similarly protective attitude toward personal property rights. However in respect of economic interests the law adopts a far less paternal role. Our economy is based largely on competition. Commercial pressure is a part of every day life and must remain so for our economy to flourish. Thus the law accepts that the exercise of economic pressure can be legitimate. As Lord Diplock put it in *Universe Tankships*, "[c]ommercial pressure, in some degree, exists wherever one party to a commercial transaction is in a stronger bargaining position than the other."[80]

Recognition of economic duress as a basis for relief has come only recently to English law. The first English case to recognise the possibility that economic threats may give rise to relief on the ground of duress was the 1976 case of *The Siboen and The Sibotre*.[81] Three years later in *North Ocean Shipping*[82] Mocatta J built on this recognition and drew on a line of Australian cases[83] as the basis of economic duress. Today, while debate rages as to the scope of the doctrine, it is clear that economic duress is very much a part of our law.

The late development of economic duress in English law can be attributed in part to the lingering effect the *laisez faire* principles of an earlier

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79 Above n 24, 949.
80 Above n 1, 384.
81 Above n 33.
82 Above n 6.
83 *Smith* v *William Charlick Ltd* (1924) 34 CLR 38; *Nixon* v *Furphy* (1925) 25 SR

time. The existence of the pre-existing duty rule also did much to stunt the development of the doctrine of economic duress. The pre-existing duty rule provides that the performance, or promise of performance of a pre-existing contractual obligation owed to the promisee will not constitute good consideration.[84] The basis of this rule was considered by Mahon J in *Cook Islands Shipping* v *Colson*[85] to be:

> ...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....

Thus the pre-existing duty rule was seen to perform a function that is viewed today as more appropriately dealt with by the doctrine of economic duress. As such there was no perceived need to establish another rule to achieve the same ends.

In recent years, however, the pre-existing duty rule has fallen from favour. It is now considered unsatisfactory as a tool for protecting against the use of illegitimate economic pressure. It is an absolute rule of general application and as such is a blunt and unwieldy instrument too inflexible to deal with all the situations to which it is applicable. It applies regardless of whether duress is present or not and thus will strike down what might be completely reasonable and fair commercial bargains. The rule is far broader than the justification given by Mahon J would suggest.

In addition, the rule is contrary to commonsense as it can be easily avoided by the provision of nominal consideration. Thus bargains extorted in circumstances where the justification of the rule demands its operation can be taken outside its scope by the provision of a peppercorn or some other spurious consideration.

A further failing of the rule is that, as a consequence of a finding of no consideration, any contract agreed between the parties that fails the pre-existing duty test must be void *ab initio*. This deprives the courts of the more flexible

remedies available under economic duress where such a contract is considered voidable.[86]

VI ECONOMIC DURESS AND THE ROLE OF REASONABLE ALTERNATIVES

There is some confusion amongst commentators and some judges as to whether the requirement that the victim have no reasonable choice is an element of the illegitimacy inquiry as Hall and Seddon[87] suggest or, as MacDonald assumes,[88] a separate requirement in the establishment of duress. On the basis of Lord Goff's comment in *The Evia Luck*[89] that the pressure must be a "significant cause" it is at least arguable that the existence of alternatives is an issue of causation.[90]

However, when Lord Scarman's modern formulation of the test for duress is considered it becomes clear that the correct view of the alternatives test is that it is an independent and essential element in establishing economic duress. Lord Scarman clearly separates it from the issue of illegitimacy regarding the two as independent limbs of the duress inquiry. This approach has been adopted in New Zealand High Court in *Foster* v *Phillips*[91] and in *Echo Investments Ltd* v *Sheffield*.[92]

The same distinction is made in the United States where the Restatement of Contracts provides that duress exists where:[93]

> ...a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative....

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86 Greig and Davis, above n 24, 951.

87 "Duress" in JA Riordan (ed) *The Laws of Australia* (The Law Book Company, Sydney, 1993) Chpt 35.7, 14.

88 Above n 61, 466.

89 Above n 10, 165.

90 Where the victim has one or more reasonable alternatives available to him or her then arguably the decision to submit to the demand was not significantly caused by the pressure. Other factors must have pushed the victim to submit. It would, of course, still be open to the coercer to prove that the victim would have taken the same course of action in the absence of the duress.

91 Above n 74.

Similarly, American case law is clear that what must be shown is wrongful or improper pressure *and* the absence of any reasonable alternatives.[94]

Thus the alternatives test is clearly a substantive limitation on the application of the doctrine of economic duress. As Palmer says:[95]

> Restitution will be denied where there was an available remedy whereby the plaintiff could have prevented the threatened consequences.

That this is so is clearly illustrated by the decision in *Pao On* where the existence of reasonable alternatives meant that economic duress was not established. As Kerr LJ stated in *B & S Contracts and Design Ltd* v *Victor Green Publications Ltd*:[96]

> I also bear in mind that a threat to break a contract unless money is paid by the other party can, but by no means always will, constitute duress. It appears from the authorities that it will only constitute duress if the consequences of a refusal would be serious and immediate so that there is no reasonable alternative open, such as by legal redress, obtaining an injunction, etc.

While Lord Scarman talked of "practical choice" the alternatives test is generally framed in terms of "reasonable choice".[97] Thus the issue of the existence of alternatives is clearly an objective inquiry. It is not so important whether the victim perceives that he or she has no alternative, rather it is for the Court to determine. As part of this determination the courts must look to the potential effect of any threat if it were to be carried out. This will give a basis on which to judge the reasonableness of any alternatives. The less catastrophic the consequences of weathering the pressure, the more reasonable will be the available alternatives.

VII ECONOMIC DURESS AND ILLEGITIMACY OF PRESSURE

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94 See, for example, *Gruever* v *Midas International Corp* 925 F 2d 280 (CA 9 (OR) 1991); *Brock* v *Entre Computer Centres Inc* 933 F 2d 1253 (CA 4 (Va) 1991).

95 GE Palmer *Law of Restitution* (Little, Brown and Company (Canada) Ltd, Toronto, 1978 and 1994 Supplement) 264.

96 [1984] ICR 419, 428.

It is not every coercive threat to the economic interests of another that will constitute economic duress. The pressure must be of a type that the law considers illegitimate. The test for illegitimacy was set out by Lord Scarman in *Universe Tankships*.[98] In determining the legitimacy of the pressure brought to bear, one must consider:

(1) the nature of the pressure; and

(2) the nature of the demand.

This formulation of the illegitimacy inquiry has been generally accepted by later courts. However, the courts have been less consistent in its application. Despite the apparent simplicity of the test formulated by Lord Scarman, in reality it merely provides a narrower framework within which to judge illegitimacy rather than providing an easy answer to the illegitimacy inquiry. Lord Scarman's test defines illegitimacy at a lower level of abstraction than merely using the term illegitimacy but it offers few clues as to the factors relevant in its application. The case law since *Universe Tankships* has thrown up a wide range of factors seen as relevant in the application of Lord Scarman's test and a number of common threads emerge. However, little certainty emerges as to the weight to be given to each of the various factors.

A The Nature of the Pressure

The nature of the pressure is a product of the threat and the manner in which the threat is made. While the nature of the pressure exerted forms the first limb of Lord Scarman's test for legitimacy it is clear that it cannot be considered in complete isolation from the second limb of the test, the nature of the demand. The two limbs are not separate tests, rather they are two parts of the same test and they overlap substantially.

1 Unlawfulness and illegitimacy

When Lord Scarman formulated his test for illegitimacy he went on to state that "the law regards the threat of unlawful action as illegitimate no matter

what the demand."[99] The test would indeed be one of simple application if there were a direct correlation between unlawfulness and illegitimacy, and between lawfulness and legitimacy. However, Lord Scarman's observation of the link between illegitimacy and unlawfulness does not tell the whole story. There is more to the question of legitimacy of pressure than the legality of the threat. This is illustrated by the recognition that lawful threats can give rise to illegitimate pressure in certain circumstances.[100]

A recent example of such an acknowledgment comes from the English Court of Appeal, in *CNT Cash and Carry Ltd* v *Gallaher Ltd.*[101] In that case the parties disagreed as to who should bear the loss in respect of a stolen consignment of cigarettes. The defendant invoiced the plaintiff for the goods. Initially the plaintiff rejected the invoice but subsequently paid it after the defendant, entirely lawfully, threatened to exercise its discretion to withdraw the plaintiff's credit facilities. The plaintiff then brought proceedings to attempt to recover the money on the grounds of economic duress. Steyn LJ, with whom Farquharson LJ concurred, expressly accepted that "the fact that the defendants have used lawful means does not by itself remove the case from the scope of the doctrine of economic duress."[102] He then referred to a number of English cases in which courts have accepted that threats of lawful action may be illegitimate[103] and cited, with approval, Birks' analysis of the issue:[104]

> Can lawful pressures also count? This is a difficult question, because, if the answer is that they can, the only viable basis for discriminating between acceptable and unacceptable pressures is not positive law but social morality. In other words, the judges must say what pressures (though lawful outside the restitutionary context) are improper as contrary to prevailing standards. That makes judges, not the law or the legislature, the arbiters of social evaluation. On the other hand, if the answer is that lawful pressures are always exempt, those who devise outrageous but technically lawful means of compulsion must always escape restitution until the legislature

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99 *Universe Tankships*, above n 1, 401.

100 *Universe Tankships*, above n 1, 401 per Lord Scarman;

101 [1994] 4 All ER 714. For a similar acknowledgment, four years earlier, in New Zealand, see the decision of Tipping J in *Shivas* v *Bank of New Zealand* [1990] 2 NZLR 327, 345.

102 Above n 101, 718.

103 *Thorne* v *Motor Trade Association* [1937] AC 797, 806-807; *Mutual Finance Ltd* v *John Wetton & Sons Ltd* [1937] 2 All ER 657; *Universe Tankships*, above n 1.

> declares the abuse unlawful. It is tolerably clear that, at least where they can be confident of a general consensus in favour of their evaluation, the courts are willing to apply a standard of impropriety rather than technical unlawfulness.

However, Steyn LJ also recognised that to extend "lawful act duress" to the case before him where there was a bona fide claim in a commercial context would take the doctrine of economic duress too far:[105]

> [I]t seems to me that an extension capable of covering the present case, involving 'lawful act duress' in a commercial context in pursuit of a bona fide claim, would be a radical one with far-reaching implications. It would introduce a substantial and undesirable element of uncertainty in the commercial bargaining process. Moreover, it will often enable bona fide settled accounts to be reopened when parties to commercial dealings fall out.

Steyn LJ went on to state that while the law ought to encourage fair dealing between commercial parties, the courts should not set standards too high where the inquiry they are involved in is focused on the moral or social acceptability of pressure rather than its lawfulness.

The acceptance of "lawful act duress" is supported by a number of commentators.[106] Once it is realised that the test for illegitimacy focuses on the nature of both the pressure and the demand, it is clear that the pressure resulting from lawful threats may sometimes constitute illegitimate pressure. The classic example of illegitimate pressure based on a lawful threat is blackmail:[107]

> Blackmail is often a demand supported by a threat to do what is lawful, e.g. to report criminal conduct to the police. In many cases, therefore, "What [one] has to justify is not the threat, but the demand..." see *per* Lord Atkin in *Thorne* v. *Motor Trade Association* [1937] AC 797, 806.

Baxt has suggested that this decision may be the start of yet another erosion of the law of contract.[108] However, the recognition of the English

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105 Above n 101, 719.

106 For example see: J Cartwright *Unequal Bargaining* (Clarendon Press, Oxford, 1991); Stewart, above n 67; Seddon, above n 2.

107 *Universe Tankships*, above n 1, 401 per Lord Scarman.

Court of Appeal in this case of the possibility of "lawful act duress" is not new.[109] Provided that the courts formulate a coherent basis for the illegitimacy inquiry this area of the law of duress will provide valuable and justifiable protection for those subject to technically lawful but morally or commercially unacceptable pressure.

In the United States the case law is divided as to whether threats to do what one is lawfully entitled to do can constitute duress.[110] The confusion that reigns is clearly illustrated by the statement of the Texas Court of Appeals in the case of *Mathews* v *Mathews*[111] that:

> It is never duress to threaten to do that which one has a legal right to do....However, a vice arises when one employs extortive measures or, lacking good faith, makes improper demands.

However, Palmer[112] acknowledges that threats of lawful action may be regarded as wrongful because of the end sought. Similarly, the Restatement of the Law of Contracts provides that a threat will be improper for the purposes of the duress inquiry where the resulting exchange is not on fair terms and "what is threatened is...a use of power for illegitimate ends."[113] This illustrates the interaction of the two limbs of Lord Scarman's test and reinforces the fact that neither limb can be considered in complete isolation when determining illegitimacy of pressure. That lawful threats may give rise to illegitimate or improper pressure would appear to be the preferable view. To lay down a blanket rule that threats of lawful action can never ground a claim of economic duress would result in a blunt doctrine, insufficiently flexible to differentiate between the wide range of circumstances in which its operation is demanded. In order for the illegitimacy inquiry to align with the justifications for the doctrine

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109 See, for example, the cases at n 103 and *Shivas* v *Bank of New Zealand*, above n 101.

110 *Kelsey-Hayes Co* v *Galtaco Redlaw Castings Corp* 749 F Supp 794 (ED Mich 1990) and *Stofer* v *First National Bank of Effingham* 571 NE 2d 157 (Ill App 5 Dist 1991) support the view that a threat to do a legal act can, in certain circumstances amount to economic duress. To the contrary are cases such as *Lebeck* v *Lebeck* 881 P 2d 727 (NM App 1994) in which the Court held that "[a] lawful demand or a threat to do that which the demanding party has a right to demand is not sufficient to support a claim of duress." Similarly the courts in *Cochrane* v *Ernst & Young* 758 Fed Supp 1548 (ED Mich 1991) and *Liebelt* v *Liebelt* 801 P 2d 52 (Idaho App 1990) clearly state that a threat to do that which there is a right to do cannot ground a claim of economic duress.

111 725 SW 2d 275, 279 (Tex App - Hous [1 Dist] 1986).

of duress it must consider all the circumstances of a particular case and not attempt to define narrowly the factors to be taken into account when determining illegitimacy.

So it should not be the threat alone which determines illegitimacy of pressure, the circumstances in which a lawful threat is made can render such a threat illegitimate. Similarly, it can be argued, the circumstances in which an unlawful threat, such as a threat to breach a contract, is made can mean that the resulting pressure will not be considered illegitimate.

It is clear that threats to breach a contract will not always amount to legal duress.[114] Lord Scarman in *Pao On* made it clear that such threats will only amount to duress where there has been a coercion of the will.[115] Kerr LJ expressed a similar view (although in more modern terminology) when he said in *B & S Contracts and Design Ltd* v *Victor Green Publications Ltd*:[116]

> I also bear in mind that a threat to break a contract unless money is paid by the other party can, but by no means always will, constitute duress. It appears from the authorities that it will only constitute duress if the consequences of a refusal would be serious and immediate so that there is no reasonable alternative open, such as by legal redress, obtaining an injunction, etc.

Comments such as these suggest that all threats to breach a contract are viewed by the courts as constituting illegitimate pressure and it is the second stage of the duress inquiry (the existence of alternatives) that is determinative of the existence of economic duress.[117]

However, there are strong arguments to be made that threats to breach a contract ought not to be considered to automatically result in illegitimate pressure. The test for illegitimacy of pressure is two-pronged. One must look to the threat and the demand. The nature of the threat ought not to be determinative where a threat is unlawful any more than it is where the threat is of lawful action. This is made clear by subsequent formulations of the illegitimacy

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114 For example see *Pao On*, above n 6.
115 Above n 6, 635.
116 Above n 95, 428.

test. Tipping J in *Shivas* v *Bank of New Zealand*[118] reiterated Lord Scarman's test and while he commented that "usually" no difficulty arises in the illegitimacy inquiry where the threat is unlawful, he stressed the need to consider "all the circumstances".[119] In *Foster* v *Phillips*,[120] Master Hansen formulated the inquiry as whether the pressure was illegitimate "in the sense that *both* the nature of the pressure *and* the demands made...were such that the law should not regard the pressure as legitimate" (emphasis added).

Birks' views unlawfulness as a powerfully persuasive guide to the illegitimacy inquiry but states that it is not conclusive. According to Birks "[l]egitimate is a term capable of drawing on social morals, not just law."[121] Greig and Davis argue that the basis of relief in cases of economic duress "is not that the contract should be unlawful by external standards, but that a contract has been concluded by means of a threat which is itself unconscionable."[122]

This attitude, it is submitted, accords with both common sense and commercial reality. The concept that unlawful threats will always be illegitimate appears to stem from the origins of duress in threats to the person. While such threats were unlawful, it was not their unlawfulness which gave rise to relief for duress. Relief was granted not because the threat was of illegal action but rather because the threat was directed at the denial of a fundamental right. If unlawfulness had been the basis of relief then logically duress would have extended to all unlawful threats. Common law duress was protecting fundamental and not merely legal rights. Similarly, unlawfulness was not the basis of relief in Equity. There it was unconscionability that was the driving force.

Other commentators have also rejected the unlawful/illegitimate analogy.[123] As Seddon points out:[124]

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118 Above n 73.
119 Above n 73, 345.
120 Above n 74.
121 Birks, above n 104.
122 Greg and Davis, above n 24, 956.
123 Goff and Jones, above n 7; R Clark *Inequality of Bargaining Power: Judicial Intervention in Improvident and Unconscionable Bargains* (Carswell, Toronto, 1987); Birks, above n 104; AS Burrows *The Law of Restitution* (Butterworths, London, 1993); Stewart, above n 67. But to the contrary see N Rafferty "The Element of

> If every threat of breach [of a contract] is automatically to be considered unacceptable for the purpose of the duress inquiry, it would mean that the boundaries of actionable duress would be far too wide.... If a threat to break a contract is regarded as unacceptable, then too many compromise agreements would be vulnerable to being set aside.

Greig and Davis[125] argue that a threat to breach a contract cannot, of itself, be sufficient because then any renegotiation of a contract could be subsequently set aside as every such renegotiation carries with it at least an implied threat not to continue with the existing contract. As Griffiths LJ said in *B & S Contracts and Design Ltd* v *Victor Green Publications Ltd*:[126]

> Many commercial contracts are varied during their currency because the parties are faced with changing circumstances during the performance of the contract, and it is certainly not on every occasion when one of the parties unwillingly agrees to a variation that the law would consider that he had acted by reason of duress. The cases will have to be examined in light of their particular circumstances.

Unlawfulness of the threat is, of course, an element of the illegitimacy inquiry (and a highly persuasive one) but it should not be decisive.

2 *The issue of good faith*

It is not just the need to consider the second limb of the illegitimacy inquiry that makes it clear that a threat to breach a contract is not, of itself, illegitimate. The manner in which the threat is made also plays an important role. In *Atlas Express Ltd* v *Kafco (Importers and Distributors) Ltd*,[127] Tucker J seems to implicitly accept that a threat to breach a contract did not, of itself, constitute illegitimate pressure. In that case the defendant was an importer of basketware and had secured a contract to sell and deliver the basketware to a national firm. The plaintiff was a carrier who contracted with the defendant to deliver the baskets at £1.10 per carton based on their own estimation of a minimum of 400 cartons per load. Actual load sizes were found to be only 200 cartons and so the plaintiff attempted, without success, to persuade the defendant to vary the agreement. Four days later the plaintiff sent an empty

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125 Above n 24, 957.

lorry to the defendant's premises with a message that the lorry would leave empty unless the defendant agreed to vary the original contract. The defendant attempted to contact the plaintiff but the plaintiff's manager had absented himself from the office. The defendant signed the agreement and subsequently refused to pay. The plaintiff brought an action to recover the money it believed was owing.

Tucker J held that this was clearly a case of economic duress. There was no question but that the pressure brought to bear was illegitimate. The plaintiff had asserted no legal justification for the threat to breach the contract, it was aware of the impossibility of the situation it put the defendant in (there was no chance of making alternative arrangements and the defendant's buyer would have sued if the goods were not delivered and this would have ruined the defendant), it left communication of the threat to a third party and the plaintiff's manager made himself unavailable to the defendant at the time when the ultimatum was given. The pressure was illegitimate when considered in the context of the surrounding circumstances.

It was clear from the facts of *Atlas Express* that what was threatened was a breach of contract. However, Tucker J did not stop his inquiry at that point. He felt the need to go further and consider the manner in which the pressure was exerted. As Chandler[128] points out, the conclusion that the pressure was illegitimate came only after Tucker J had considered a number of factors. The further factors considered by Tucker J clearly illustrate bad faith on the part of Atlas.[129]

B The Nature of the Demand

It is not only in terms of the nature of the pressure that the issue of bad faith comes into play. Bad faith appears to have a pivotal role in determining the nature of the demand. The distinction between bad faith as a component of the nature of the pressure and bad faith with respect to the demand does not appear to have been expressly acknowledged. Bad faith is usually regarded as a component of the illegitimacy inquiry in a general way.[130] However, it is clear

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128 PA Chandler "Economic Duress - Clarity or Confusion" [1990] Lloyds Maritime and Commercial Law Quarterly 270.

129 Though Burrows, above n 123, inexplicably contends that there was no obvious bad

that bad faith will relate either to the manner in which the threat is made, or to the nature of the demand and it is conceptually useful to distinguish between the two.

The decision in *B & S Contracts Ltd*[131] illustrates the role of bad faith in determining the nature of the demand. In that case the plaintiffs had agreed to erect stands for the defendants for an exhibition. The contract contained a clause providing that the plaintiffs would make every effort to carry out the contract but its due performance was subject to variation or cancellation in the event of, among other things, a strike. The workers that the plaintiffs arranged to put up the stands worked for a subsidiary of the plaintiffs but had recently been given redundancy notices. Once the workers had arrived at the site they refused to proceed with the work unless their demand for £9000 severance pay (to which they were not entitled) was met. The plaintiffs then approached the defendants and threatened to cancel the contract unless the defendants paid half that sum. The plaintiffs would not accept an offer by the defendants to advance them £4500 of the contract price and so the defendants paid the money. However, the defendants subsequently deducted £4500 from the invoice price before paying. The plaintiff sued to recover the £4500.

The Court of Appeal had no difficulty finding operative economic duress in this case. The members of the Court emphasised the bad faith exhibited by the plaintiffs. The plaintiffs did not refuse to pay as a matter of principle, they simply did not want to reduce the sum that they would have received for the contract.[132] The sum they required "was put on the table and available to the plaintiffs. But they decided not to accept it on the terms offered; they wanted it as extra...."[133] The Court held that it would have been reasonable for the plaintiffs to have met the cost. Clearly, on the facts, the plaintiffs had taken advantage of the defendants' vulnerable position to force them to pay the £4500.

Goff and Jones[134] also see a role for the concept of bad faith in relation to the demand. However, they see it more as a lack of good faith. They pose the question: what should be the position where the threatener believed that it was commercially reasonable to ask for a variation of an existing contract? They

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131 Above, n 96.
132 As per Griffiths LJ, above n 96, 426.

give as an example the builder who finds hidden horrors in the sub-soil, while digging the foundations of a building. In such circumstances the builder might think it justifiable to demand extra remuneration to complete the work. As Palmer and Catchpole point out:[135]

> It can therefore be very hard on a contractor, who genuinely and reasonably believes that he has a valid excuse for non-performance and who seeks to effectuate what amounts, in his view, to a legitimate renegotiation of the contract, to characterise too readily his declaration of intention to cease performance on the original terms as a threat to do something "illegitimate."

Palmer and Catchpole favour a test for the illegitimacy of threats to breach a contract similar to that proposed by Goff and Jones: that legitimacy be judged according to whether the threatener honestly and reasonably believed in the validity of the claim. Palmer and Catchpole appear to be focusing on a belief in the legal validity of the claim, however, a flexible and responsive doctrine ought also to consider the commercial validity of the claim. This is an approach which finds support in the United States.

Bad faith, or lack of good faith, features prominently in the United States in determining whether pressure is improper for the purposes of economic duress. It is clear that the existence of bad faith in respect of the demand is one of the factors in considering the wrongfulness of a threat of lawful action.[136] Similarly it would seem that bad faith plays a role in determining whether a threat of illegal action amounts to an improper threat.

The Restatement of the Law of Contracts provides that a threat will be improper if it "is a breach of the duty of good faith and fair dealing under a contract...."[137] The Restatement goes on to explain that:[138]

> ...the "extortion of a 'modification' without legitimate commercial reason is ineffective as a violation of the duty of good faith.... The test of 'good faith' between

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135 Palmer and Catchpole "Industrial Conflict, Breach of Contract and Duress" (1985) 48 Modern Law Review 102, 106.

136 See *Southmark Properties* v *Charles House Corp* 742 F 2d 862 (CA La 1984); *Carpenter* v *US* 4 Cl Ct 705 (Cl Ct 1984); *Gruever* v *Midas International Corp*, above n 94.

merchants or as against merchants includes 'observance of reasonable commercial standards of fair dealing in the trade'....and may in some cases require an objectively demonstrable reason for seeking a modification... ."

The comments of the California Appeals Court in *Rich & Whillock Inc* v *Ashton Development Inc*[139] are illustrative of the role of bad faith in the wrongful threat/illegitimacy inquiry. The Court in that case held that "a *bad-faith* threat to breach a contract...may constitute a wrongful act for the purposes of economic duress" (emphasis added). To the same effect is the case of *Zebedeo* v *Martin E Segal Co Inc*[140] in which the Court held that "[w]here one party insists upon a contractual provision, which it honestly believes itself entitled to, unless such belief is patently unreasonable, conduct cannot be wrongful, and thus cannot constitute duress."

C Identifying Bad Faith Demands

While bad faith in the manner in which the threat is made is easily identifiable (as in *Atlas Express*), bad faith in the nature of the demand can be harder to identify. The lack of any reasonable legal or commercial grounds for the making of a demand will be the key to identifying a bad faith demand. Along with the factors discussed above, there are others that may be relevant to this inquiry.

1 The necessity of the threatener

This factor appears to be strikingly absent from commonwealth caselaw. An obvious example is *Atlas Express Ltd.* In that case there was certainly bad faith in the manner in which the threat to breach the contract was made. However, the Judge completely failed to consider the position of the threatener (Atlas). What would have been the effect on that company had it performed the contract as originally entered? Would it have simply resulted in a lesser profit or a bearable loss, or would it have forced the company into insolvency? Arguably, where a threatener is placed in an impossible situation, where there is no reasonable alternative, a demand for a variation of the contract makes commercial sense and illegitimacy ought not to be found to exist.[141]

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139 157 CA 3d 1154 (Cal App 4 Dist 1984).

Burrows[142] suggests that a threat to breach a contract should be considered legitimate where it is aimed at merely correcting what was always a bad bargain. However, such a low threshold can not be justified. If the test were formulated on this basis the courts would be required to protect people from their bad bargains. Nothing more would need to be proved by the threatener than that the terms of the original contract were unfair. There would be no requirement to show that undue hardship would result from the performance of the contract on those terms and no requirement to show that the threatened party had unconscionably obtained those terms. Such a test would be completely contrary to the basis of the free market system in which we operate.

2 *Substantive fairness*

Justification for a demand can only exist where the demand is reasonably necessary to protect the legitimate interests of the threatener. Thus the concept of proportionality is relevant to the question of bad faith. In relation to threatened breaches of contract, Sutton identifies the need for "oppressive conduct which goes beyond what is reasonably necessary to protect the [threatener's] legitimate interests"[143]. The fairness of the renegotiated terms may be a good indication of the existence of bad faith. Terms that provide a windfall for the threatener at the victim's expense, rather than simply righting some imbalance, are unlikely to satisfy the good faith requirement.

Burrows rejects the idea of substantive fairness as a test for illegitimacy on the grounds that such a test would result in a narrow doctrine of economic duress as "it will be rare for terms proposed by a party threatening a breach of contract to fall outside the possible bounds of fairness."[144] However, it is not necessary, or desirable to view substantive fairness as determinative of the illegitimacy inquiry. Rather it is merely one factor in determining the existence of bad faith and as such it can play a valuable role. The existence of substantively fair terms will not preclude the operation of the doctrine of economic duress where other factors demand its application.

In addition, a rejection of any role for substantive fairness in determining the existence of duress draws a sharp dividing line between substantive and

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142 Above n 123.

procedural matters. In *Brighouse* v *Bilderbeck*[145] Cooke P, in the context of examining the duties of a reasonable employer, stated that it is wrong to distinguish between the reason for a dismissal and the manner of dismissal. Both substantive and procedural matters are relevant in determining whether a dismissal is unjustified. Similarly, in determining the existence of economic duress, both the substance of an agreement and the manner in which it came about will be relevant.

D Summary

Bad faith is the key to establishing a workable test for the existence of economic duress where there is a threatened breach of contract.[146] It is the touchstone for illegitimacy and its existence, where there is a threat to breach a contract, is determinative of illegitimacy. As the British Columbia Court of

145 [1994] 2 ERNZ 243.

146 It has been suggested in a recent text that in establishing duress "[t]he defendant does not have to be shown to have behaved badly and has indeed often acted in absolutely good faith." See P Birks and Chin Nyuk Yin in "The Nature of Undue Influence" in J Beatson and D Friedmann *Good Faith and Fault in Contract Law* (Clarendon Press, Oxford, 1995) 62. However, the authorities cited by the authors for this statement relate solely to cases of duress to the person and duress of goods. As already discussed in this paper the requirement of illegitimacy is already established in respect of threats of that type and so no issue of good faith arises. It is only the expansion of duress

Appeal in *Harry* v *Kreutziger*[147] stated:

> [The] single question is whether the transaction, seen as a whole, is sufficiently divergent from community standards of commercial morality that it should be rescinded.

A test based on bad faith achieves the appropriate balance between the aims of duress and the need for commercial certainty. Commercial reality dictates that not every threat to breach a contract should automatically be considered to result in illegitimate pressure. There will be times when such a threat will be made and the victim will have no alternative but to submit and yet the doctrine ought not to operate to provide relief. This may appear harsh but the law must be appropriate to the "deliberate and ruthless"[148] nature of the commercial world. A test of bad faith achieves this as even in the deliberate and ruthless commercial world bad faith is to be abhorred.

So what is this bad faith that we look for when there has been a demand accompanied by a threat to breach a contract? The bad faith may be in the manner in which the threat was made, as in *Alas Express*, or it may relate to the demand itself, as in *B & S Contracts*. Notwithstanding the decision in *Atlas Express*, bad faith in the manner in which a threat is made ought not to be determinative of illegitimacy. Consideration must be given to the second limb of the illegitimacy inquiry. A good faith basis for the demand made in *Atlas Express* would have gone some way to negating the effect of the bad faith involved in the manner in which the threat was made and the reasoning of the Court is weakened by its failure to consider this point.[149]

Bad faith in the nature of the demand clearly rests on the concept of justification: was the threatener legally or commercially justified in making the demand? As such, it is important to note that the term "bad faith" is not restricted to positive acts of bad faith but extends to a lack of good faith in making the demand. There is a lack of good faith when a demand is made in the absence of any reasonably held belief of legal or commercial justification. The requirement of good faith goes not only to the actual making of the threat itself

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147 (1978) 95 DLR (3d) 231, 241.

148 *Queensland Wire Industries Pty Ltd* v *Broken Hill Proprietary Co Ltd* (1989) 167

but also to the extent of the demand. Even where there are legal or commercial justifications for the making of a demand, if what is demanded goes beyond what is reasonable in the circumstances then there will be bad faith.

Determination of these issues should not be unduly difficult . The claim of a reasonable held belief in a legal justification will pose no problem to the courts. The courts are often required to adjudicate on the reasonableness of beliefs and the law is their province. Of more difficulty is the determination of the reasonableness of a commercial justification. However, with the increased awareness of commercial issues amongst the judiciary and consideration of evidence of industry practice the inquiry is well within the ability of the courts.

Where there is a threatened breach of contract the bad faith test will apply in the following manner to determine whether the resulting pressure is illegitimate:

(a) If a threat to breach a contract is made in good faith, based on reasonably held commercial or legal ground, the pressure resulting from such a threat will not to be characterised as illegitimate.

(b) Where there is bad faith in both the manner in which the threat is made and in the demand made then a finding of illegitimate pressure is inevitable.

(c) Where there is no bad faith in the manner in which the threat is made but the demand is tainted with bad faith, the resulting pressure will be illegitimate.

(d) Where there is bad faith in the manner in which the threat is made but the demand itself is justified, the Court must balance the nature of the justification with the extent of the bad faith. Where the conduct is highly unconscionable, a compelling justification must be shown to avoid a finding of illegitimacy.

VIII CONCLUSION

Economic duress represents one of the many areas of the law in which the courts have demonstrated an increased willingness to grant relief in respect of unfair or unfairly obtained bargains. However, this doctrine is still in its infancy and as such it is sometimes difficult to distinguish between economic duress that renders a contract voidable and mere legitimate commercial pressure which will not ground a claim for relief. In order to formulate coherent and consistent principles for the application of economic duress it is essential that the overborne will theory be cast aside. The modern test formulated by Lord Scarman in *Universe Tankships* provides a potential framework for a principled approach to economic duress. However, the courts have failed to clearly define the concept of illegitimacy thereby decreasing commercial certainty, one of the very things that the judges seem at pains to protect. A clearer picture of the limits of legitimate commercial pressure can only benefit commerce by providing more certainty to commercial parties caught in what may appear to be impossible situations.

The bad faith test for illegitimacy proposed in this paper goes some way to narrowing the grey area of uncertainty which blights the doctrine of economic duress. It does not, however, completely remove the uncertainty involved in the application of the doctrine and it would not be desirable for it to do so. The uncertainty that remains provides discretion for the courts which is vital for a flexible and workable doctrine. This is yet another balance that must be maintained. Too much uncertainty results in confusion and lack of faith in the rule, but too little will result in a harsh and inflexible doctrine ill suited to the role that we would have economic duress play.

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