CHAPTER 1

Function and Sources of Contract Law in Hong Kong

1.1 Definitions of Contract

[1-1] In civil law jurisdictions, codes generally provide authoritative definitions of fundamental legal concepts.

[1-2] The French Civil Code, for instance, defines 'contract' in the following terms:[1]

> A contract is an agreement by which one or several persons bind themselves, towards one or several others, to transfer, to do or not to do something.

[1-3] Similarly, the Philippines Civil Code contains the following definition:[2]

> A contract is a meeting of minds between two persons whereby one binds himself, with respect to the other, to give something or to render some service.

[1-4] The common law functions differently and operates without official codification. There is no single authoritative definition of 'contract' to which common law lawyers can point. Nevertheless, there exist numerous persuasive definitions of contract which are similar to each other, and to the definitions authoritatively adopted in most civil law systems. Three examples are as follows:

> The law of contract may be provisionally described as that branch of the law which determines the circumstances in which a promise shall be legally binding on the person making it.[3]

> A contract is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognises as a duty.[4]

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1 Art 1101.
2 Art 1305.
3 J Beatson, A Burrows and J Cartwright, *Anson's Law of Contract*, (Oxford University Press, Oxford, 29th edn, 2010) p 1.
4 American Law Institute, *Restatement Second of the Law of Contracts*, section 1.

> A contract is an agreement giving rise to obligations which are enforced or recognised by law. The factor which distinguishes contractual from other legal obligations is that they are based on the agreement of the contracting parties.[5]

[1-5] The common thread connecting all these definitions is the existence of an 'agreement', or a 'promise', or a 'set of promises,' or a 'meeting of minds' which creates obligations binding in law.

[1-6] That the civil law and common law definitions of contract are so similar should not be surprising. Enforceable agreements are part of the *ius gentium*. The term '*ius gentium*' is commonly translated as 'the law of nations', but is perhaps less ambiguously rendered as 'the law common to all peoples', or 'the common law of mankind'. It originated in Roman law as a supplement to the *ius civile*, which was the law regulating relations among Roman citizens. As Roman power expanded and as Roman citizens came into increasing contact with foreigners, a law was developed to regulate relations among non-citizens and between citizens and non-citizens; this was the *ius gentium*. The Roman jurist Gaius (c. 130–180 AD) provides the following characterisation:[6]

> Every people that is governed by statutes and customs observes partly its own peculiar law and partly the common law of all mankind. That law which a people establishes for itself is peculiar to it, and is called *ius civile*, while the law that natural reason establishes among all mankind is followed by all peoples alike, and is called *ius gentium* as being observed by all mankind. Thus the Roman people observes partly its own peculiar law and partly the law of mankind.

[1-7] The *ius gentium* principle of *pacta sunt servanda* ('agreements are to be complied with') is the fundamental principle underpinning the contract law of Hong Kong, and of every other jurisdiction's law of contract. According to the Roman jurists, every civilised people observe this principle, although its detailed manifestation and application varies according to the *ius civile* of particular jurisdictions. A law of contract was, in Roman legal thought, a sign that the people possessing it were not barbarians.

1.2 Contract Law and the Free Society

[1-8] The bindingness of contracts is that which makes them a branch of the law of obligations, the other great branch of which is torts (or 'delict' in most civil law systems). The principal feature of contractual obligations is that they are freely undertaken by the contracting parties themselves. In this sense, contracts are voluntary obligations. Torts, by contrast, involve obligations

5 Edwin Peel, *Treitel: The Law of Contract*, 14th edn (Sweet & Maxwell, 2015) p 1.
6 *Gaius, Institutiones*, as translated by Hans Julius Wolff, *Roman Law: An Historical Introduction*, (University of Oklahoma Press, Norman OK, 1951) pp 82–83.

imposed on parties without their consent—torts are thus involuntary obligations.

[1-9] Contract is also a necessary, albeit insufficient, precondition of a free society. Whenever human beings live together in social contact, means must be found to co-ordinate their activities in pursuit of the various human goods. There must be arrangements within which joint or co-operative activities can be efficiently pursued, with confidence, to their conclusion. There must also be arrangements which allow individuals or groups to pursue their own projects in a way which protects the just interests of those engaged in other, competing or unrelated, activities. These arrangements, taken together, constitute the common good of any society. The more effectively human activities are co-ordinated so as to produce a stable, just and harmonious social order, the better served is the common good of the society.

[1-10] There are basically only three means by which the necessary co-ordination can be achieved. First, those seeking to pursue a common objective or achieve a particular result may arrive at a consensus as to the things that need to be done. However, the realities of human affairs are such that the more numerous the people involved, the longer the time needed and the more complex the desired objective or result, the more difficult it is to achieve or sustain the necessary consensus. The consensus method of co-ordination is rarely suitable outside situations involving relatively small numbers of persons who are bound to each other by ties of family or friendship and in pursuit of goals of relatively limited complexity.

[1-11] Second, those exercising political authority may issue commands in order to mobilise and co-ordinate people for the achievement of objectives determined by that authority. Where command-and-control methods of achieving social and economic co-ordination are the dominant mode of such co-ordination, the freedom of the people to exercise their initiative is severely restricted. Political and economic systems within which command-and-control methods of co-ordination predominate are radically inconsistent with a free society and depend heavily on the exercise of coercive measures against those who refuse or fail to comply with commands. The twentieth century witnessed a number of failed social, political and economic experiments in the extensive use of command-and-control methods of co-ordination, most notably among the Marxist dictatorships.

[1-12] The third means of achieving the necessary social co-ordination is contract. The freedom of the people is preserved by allowing them to determine for themselves the objectives to be pursued, the identity of those whose activities will be co-ordinated, and the distribution of obligations in pursuit of the agreed objectives. An element of coercion is present but in a severely limited form; it is confined to providing mechanisms for enforcing performance or compensation on those who have failed in their agreed

obligations. Circumscribed in this way, the element of coercion magnifies rather than diminishes the people's freedom; it provides an assurance that their freely-established agreements are ultimately backed by the State.

[1-13] A well-functioning law of contract therefore serves inter-locking purposes which are fundamentally moral, respectful of human freedom, and supportive of economic rationality.

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47 American Journal of Jurisprudence (2002) 71–83, at pp 72–75

Natural law theory is teleological. It evaluates a human artifact, human institution, or human activity by how well it achieves its proper purpose, its end, its telos. Aristotle tells us that every art or applied science or systematic investigation, and every action and choice, seems to aim at some good, some end. The end of medicine is health. The end of shipbuilding is a vessel. The end of strategy is victory.[7] And if there is some ultimate end throughout the entire realm of human activity, this end will be the highest good. Will not knowledge of this good, asks Aristotle, be very important to our lives? Would it not better equip us to hit the proper mark, like archers who have a target to aim at?[8] Aristotle says there is such an end. The end of social and political living is the good for man.[9]

Now if some social institution or activity has such an end, it would seem that we should evaluate that institution or activity according to how well it promotes that end. Thus, Saint Thomas Aquinas suggested that if something is constructed to serve some end, its form should be appropriate for promoting that end, just as the form of a saw should be appropriate for cutting.[10]

This teleological approach seems to make good sense, at least in the realm of purposeful activity. We wouldn't construct bridges or buildings if we didn't think they could serve a purpose. And once we have constructed a bridge or a building, we evaluate it by asking how well it serves its purpose (or set of purposes). We take this same teleological approach when we evaluate the performance of a person who has been assigned a specialized function in a cooperative activity. We evaluate a football quarterback, for example, by asking how well he performs his function. …

Let us now consider legal systems. A legal system is a human institution. It involves purposeful and cooperative activity with specialized functions. We don't construct a legal system just for the heck of it. We establish a legal system in order to promote some purpose, some goal, some end. We thus evaluate our legal system at any point in time by asking how well it is serving this end. If we are sincerely interested in evaluating and improving our legal system, we cannot help but take a teleological approach and ask what the proper purpose of the legal system is. I say "proper purpose" because the persons who operate our legal system may have differing

7 See Aristotle, *Nicomachean Ethics*, Martin Ostwald, trans. (Indianapolis: Bobbs-Merrill, 1962), 1094a 1–9, p 3.
8 See ibid 1094a 18–24, p 4.
9 See ibid 1094b 7, p 4 and n 8.
10 See Saint Thomas Aquinas, *The Treatise on Law* [Being *Summa Theologiae*, I-II, QQ.90 Through 97], R J Henle, S J, trans. (Notre Dame, Ind: University of Notre Dame Press, 1993), q. 95, a. 3, c., p 292.

notions as to the purpose of the system, and we must thus answer the question of what should be regarded as the purpose.

Aquinas's answer was that the proper end or purpose of law is to enable all citizens to live good lives, felicitous and fruitful lives, and Aquinas used the term "the common good" to refer to this goal of helping all members of society enjoy good lives.[11] For natural law theorists, a good life is made up of a number of basic human goods. Each theorist seems to have a different list of the basic human goods necessary for a good life. My favorite is the list presented by John Finnis in his book, *Natural Law and Natural Rights*: life and health; knowledge; play; aesthetic experience; friendship; practical reasonableness; and religion.[12]

Note that most of these basic goods cannot be enjoyed by a person unless she has adequate wealth or adequate leisure time or both. The preservation of life and health often costs a lot of money. The acquisition of knowledge requires leisure time, or at least time away from earning a living, and (as many know from experience) a college or university education costs a lot of money. Play obviously requires leisure time and can cost money. Aesthetic experience requires leisure time, and some of the nicer forms of aesthetic experience must be purchased with money. Friendship requires leisure time. So does religion.

Now how can a society organize its economic life so that people have enough wealth and enough leisure time to obtain the basic human goods that make up a good life? Part of the answer to this question is that there must be a division of labor. If you built your own house, grew all of your food, made your own clothes, and provided your children with all of their education, you would have very little leisure time and probably very little wealth. Our economy is more efficient and our standard of living higher because we specialize as carpenters, farmers, shoemakers, or teachers.

But this division of labor creates a distribution problem. How will the carpenter obtain food? How will the farmer obtain a house? I can think of three ways in which goods and services might be distributed in a society that has a highly specialized division of labor. First, we might rely on gifts. The carpenter might donate houses to the farmer, the shoemaker, and the teacher. The farmer might give some of the food he produces to the carpenter, some to the shoemaker, and some to the teacher. And so on. But such a system would not work very well. Aside from the limitations of human generosity, what is the likelihood that you would get a house you want and clothes you would like to wear? Just ask yourself how many of the ties or scarves you received as Christmas gifts were what you really wanted.

A second alternative method of distributing goods and services would involve the government determining who will receive each house, each quart of milk, each pair of shoes. But if your own relatives and friends don't know what you really need or want, what are the chances that better selections would be made by remote government bureaucrats who don't even know you?

The third and preferable method for distributing goods and services is voluntary exchange. You buy the house you want, the food you want, the clothes you want, the formal education you want, by paying money in exchange. You might not have enough money to buy your first choice in food or clothing, but you can do a lot better than you would if you had to rely on the generosity of other citizens or the wisdom of the government bureaucrats. (If all of this sounds like something right out of Adam Smith, it is.)[13]

11 See ibid q. 90, a. 2, c. and translator's comments, pp 131–134.
12 See John Finnis, *Natural Law and Natural Rights* (Clarendon Press, Oxford, 1980) pp 85–90.
13 See Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (University of Chicago Press, Chicago,1976) pp 7–20.

> We can now begin to see why contracts are necessary. Many of our important voluntary exchanges cannot be performed by both parties simultaneously. One party must perform to some extent before she can expect the other party to perform. But she will probably not be willing to begin her performance without a promise from the other party that he will perform his side of the exchange. And that other party is unlikely to commit himself without a promise from the first party. A set of promises, a contract, is therefore necessary.[14]
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> Furthermore, neither party will enter into a contract for a future exchange unless she has good reason to believe that the contract will be beneficial to her. Not only must she have good reason to believe that the other party will probably perform any promise he has made, she must also believe that if the contract is performed and not breached, she will derive a net gain from it and not a net loss, and she must also believe that she will be compensated if the other party does not perform his promise.
>
> We can thus conclude that a major purpose of contract law is to encourage exchange contracts that are likely to be mutually beneficial and discourage exchange contracts that are likely to leave one party with a net loss.[15] This is one reason why our legal system will not allow a person to enforce a contract if he has induced the other party into the contract by means of fraud or duress. If the other party was the victim of fraud, she has been deceived about the value of the exchange to her, and there is too great a risk that performance of the contract would leave her with a net loss.[16] If the other party was the victim of duress, there is a great risk that she was forced into a losing contract in order to avoid an even greater loss that was threatened by the party exercising duress.

[1-14] The existence of a mature and sophisticated law of contract has provided Hong Kong with an enormous advantage in the East Asian region. The territory's rise to prominence first as an industrial powerhouse, then as a commercial and financial one, and always as a regional bastion of liberty, has been intimately connected with the rule of law and a common law system for the enforcement of contractual agreements. The security of bargains which this climate fostered made Hong Kong, for many years, one of the few places in

14 As Finnis puts it, the practice of promising promotes the common good because 'it provides an effective means of maintaining cooperation … over the span of time necessary for the fulfillment of any human project.' See Finnis, *Natural Law and Natural Rights* (Clarendon Press, Oxford, 1980) p 303.

15 Recognising mutual benefit as a major purpose of contract law does not entail a legal rule excusing from liability every party who fails to perform because he saw that performance of the contract would leave him with a net loss. A legal system does not encourage mutually beneficial contracts unless contracting parties can be reasonably confident that they will be given a compensatory remedy if the other party does not perform. Excusing doctrines such as impracticability and frustration of purpose must therefore be confined within rather narrow limits.

16 Economists now recognise that free markets do not work very well when persons engaging in market exchange are not well informed. Joseph Stiglitz, George Akerlof, and A Michael Spence won the Nobel prize in economics for 2001 largely because of their work indicating the importance of information and the need for legal rules that not only proscribe misrepresentation of facts but also require disclosure of important facts. See Louis Uchitelle, '*Three Americans Awarded Nobel for Economics*', New York Times, 11 October, 2001, p C1.

Asia enjoying a climate of freedom in which entrepreneurship and investment could be confidently undertaken.

1.3 Origins of Hong Kong Contract Law

[1-15] As we shall see, the sources of contract law in Hong Kong lie in the English common law.[17] In order to understand the origins of Hong Kong's law of contract, it is therefore necessary to review the development of contract law in England.

(a) Medieval contracts

[1-16] For most of the twelfth and thirteenth centuries, the principal means by which agreements could be legally enforced in England lay in the actions of Debt and, to a lesser extent, Covenant.

[1-17] The conceptual emphasis on the enforcement of an existing debt rather than promissory obligation reflected the pre-modern conditions of the times. Medieval England did not possess a market-based national economy. Its economic and social relations were predominantly feudal, with one's legal rights and obligations principally determined by one's inherited social status. In such an environment, there was little need for a flexible and dynamic law of contract adapted to securing the enforceability of forward-looking agreements. Feudalism placed a premium on economic and social stability, in felicitous contrast to the turmoil of the dark ages which had preceded it. A contract in medieval England was not perceived as a device for securely planning and executing a scheme involving commercial or property relations among citizens equally free to acquire and dispose of assets or to provide and consume services. Rather, the main emphasis was on the enforcement of more basic obligations arising in debt:[18]

> In the main, these early contractual relations did not involve obligations to be performed in the future but rather concerned present exchanges of feudal obligations without any money changing hands. The contract law of the Middle Ages was concerned with security and retention of the status quo rather than with novel trade agreements.

17 See Section 1.4 below.

18 Kevin M Teeven, *A History of the Anglo-American Common Law of Contract* (Greenwood Press, Westport CT, 1990) p 1. Similarly, according to S F C Milsom in *Historical Foundations of the Common Law* (Butterworths, London, 2nd edn, 1981) pp 12, 325: 'Early [English] law does not have to cater much for choice. In the private sphere we … find this reflected in the small part played by contract, and the large part played by enduring relationships of a proprietary nature. … The narrow concept of covenant was the product of a society in which most obligations were seen as flowing from tenure or status. This was obviously the case with agricultural services. The ploughman who did not plough would be summoned to the lord's court as a wrongdoer long before anyone would think of suing him as an equal in contract.'

[1-18] Prior to the reign of King Henry II (1154–1189), and putting aside the important ecclesiastical courts, the judicial function in England was performed almost exclusively by an array of local courts. These were constituted as courts with a direct link to the Crown at the county and hundred levels,[19] as local courts with jurisdiction conferred by royal franchise, as manorial courts on a feudal pattern, as city and borough courts, and as courts merchant exercising jurisdiction in connection with trade fairs and markets.[20] These local courts, constituted by sheriffs, bailiffs, nobles, knights, freeholders, clerics and prominent merchants on a part-time basis, performed both judicial and administrative functions mainly by reference to local customary practices: 'Laws as well as institutions were local, and the differences between one district and another sometimes reflected not different answers to the same problem but different ways of life.'[21]

[1-19] Perhaps the most significant aspect of Henry II's eventful reign was his reform of the system of justice. From the itinerant and cumbersome curia regis, he carved out royal courts 'in eyre'[22] which toured the counties and boroughs on horseback auditing local administration and determining litigation between subjects. Also from the curia regis emerged the permanent and professional royal courts of justice stationed at Westminster that eventually evolved into the Exchequer Chamber, the Common Bench (or Common Pleas), and the King's Bench.[23] These stationary royal courts were to overtake the eyres in significance by about 1300.[24]

[1-20] Access to the Common Bench, which determined litigation between private parties largely in actions we would today refer to as contractual or tortious, was by writ issued by the Exchequer upon payment of a fee.[25] The

19 The hundreds were geographical subdivisions of the counties dating from pre-Conquest times. A county court was convened by the local Sheriffs ('shire reeve') who was a royal appointee. Bailiffs, appointed by the Sheriff, convened the hundred court in a royal hundred. The local Lord would appoint a Bailiff in a private hundred. 'By royal grant, by usage and usurpation, or by the continuance of a state of affairs sometimes older than the counties and hundreds themselves, many hundreds—at the accession of Edward I [1100] it was more than half of all those in England—were in private hands': Milsom (1981), ibid p 15.

20 Milsom (1981), n 18 above, pp 16, 18–23.

21 Ibid p 11.

22 'Eyre' is a Middle English word deriving from the Old French 'eire', in turn deriving from the Latin 'iter', meaning 'journey'.

23 It took longer for the King's Bench, which originally accompanied the King on his travels around the country, to become stationary. It finally settled at Westminster only in the fifteenth century, although in the fourteenth century its movements had become less frequent and more predictable: Milsom (1981), n 18 above, p 52.

24 Milsom (1981), ibid pp 31–33.

25 Access to the King's Bench, while it remained itinerant with the King, was also by writ if the defendant was in a county other than that in which the bench was sitting. No writ was necessary to give the king's own court jurisdiction, and the writ was for the purpose of compelling the defendant's presence. Where the defendant was in the same county, the court could simply rely on the local sheriff (a royal officer) to ensure such presence: ibid p 34.

writ was necessary not only in order to compel the defendant; the jurisdiction of the Common Bench was exceptional unless a royal interest was at stake, and the writ allowed a plaintiff to avoid the jurisdiction of local courts. It also enabled a plaintiff to have speedier royal justice than might otherwise be the case, as the eyres visited each locality only once in about seven years.[26] Each action needed to be commenced by a particular writ corresponding to the cause of action in question. As time went by, the system of writs hardened in two ways: The writs evolved into established forms that effectively determined the substance of legal actions, and they became necessary to obtain justice before the Common Bench even as local courts ceased to exercise a parallel jurisdiction.[27]

(b) Action of Debt sur contract

[1-21] In the reign of Henry II, an action of Debt lay where the claim was for restitution of a fixed sum ascertained at the time of contract or of specific chattels already belonging to the claimant. There was no clear difference between debt and detinue. In the thirteenth century a sharper distinction began to materialise, with the action of Debt lying for a specific sum of money and unascertained chattels (that is, fungibles), while Detinue crystallised into an action for the recovery of specific chattels.[28]

[1-22] In the case of Debt, where there was no agreement under seal (known as a 'bond'), an action of Debt *sur contract* lay to recover money or unascertained chattels currently owing to or owned by the claimant.

[1-23] The attraction for a claimant of an action of Debt *sur contract* was diminished by the availability to the defendant of 'wager of law' or 'compurgation', which remained regularly in use as an alternative to jury trial or trial by combat until the early seventeenth century.[29] The defendant could succeed in his wager if he swore his case on oath, and if he then procured on an appointed day other persons ('oath helpers' or 'compurgators') to swear

26 'The most regular institution of the middle ages therefore started, not as a part of the regular routine of government, but as a provision for exceptional cases': ibid p 35.

27 Ibid p 35.

28 F W Maitland, *The Forms of Action at Common Law: a Course of Lectures*, A H Chaytor and W J Whittaker (eds), (Cambridge University Press, Cambridge 1936) 48; Teeven (1990), n 18 above, p 7; J H Baker, *An Introduction to English Legal History* (Butterworths LexisNexis, London, 4th edn, 2002) pp 74, 321.

29 J H Baker, (2002), ibid pp 74, 326. There were, however, a few types of informal debts that precluded a defendant from resort to wager at law. These included most prominently debts arising from the lease of land and the taking of an account before auditors where the action was to recover the rent or for the balance found due on the account: Milsom (1981), n 18 above, p 255.

that the defendant was a credible person.[30] The number of compurgators originally varied according to the plaintiff's social status and the nature of the proceedings, but eventually eleven oath helpers became standard. It was not necessary for the compurgators to swear as to the transaction in question. They were not, in modern parlance, witnesses of fact but character witnesses. Furthermore, the compurgators could not be cross-examined.[31] This customary procedure had tribal roots among the Germanic invaders of the dark ages,[32] and was probably reasonably efficacious when actions of Debt were heard primarily by local courts or by royal courts in eyre hearing the case locally.[33] Social pressure and a fear of damnation for oath breaking may have operated to lend the procedure an adequate integrity.

[1-24] When a case of Debt was heard by the royal courts at Westminster, as increasingly occurred throughout the mediaeval and early modern periods, it was usually impractical to bring compurgators from the defendant's locality. In these circumstances, wager of law was wide open to abuse.[34] Indeed, 'a tradition was begun of hiring professional oath-helpers, called "knights of the post", who hung around Westminster and probably didn't even know the defendant, much less have any knowledge about the defendant's veracity.'[35] By the end of the sixteenth century, the court porters would provide compurgators for a fixed fee.[36] Although many defendants in an action of Debt *sur contract* chose jury trial rather than wager of law,[37] 'from the plaintiff's point of view the mere availability of the procedure was a deterrent; and it became most unwise to give substantial credit without formal security.'[38]

30 James Bradley Thayer, *A Preliminary Treatise on Evidence at the Common Law* (Little Brown & Co, Boston MA, 1898) pp 24–25, where the procedure is referred to as 'trial by oath'; Teeven (1990), n 18 above, p 9.

31 Baker (2002), n 28 above, pp 74, 322–323.

32 Its origins lay specifically in the Salic law: James Bradley Thayer, *A Preliminary Treatise on Evidence at the Common Law* (Little Brown & Co, Boston MA, 1898) p 25.

33 Milsom (1981), n 18 above, 245–248; Baker (2002), n 28 above, p 74.

34 On the other hand, it was not unknown for an unscrupulous plaintiff to intimidate compurgators in order to prevent a defendant from waging his law. Baker (2002), n 28 above, p 460.

35 Teeven (1990), n 18 above, p 10; semble Milsom (1981), n 18 above, pp 245–246; Baker (2002), n 28 above, p 74.

36 Baker (2002), n 28 above, p 74.

37 Perhaps because they could not afford the price of compurgators, and perhaps because wager of law came to be seen as a dishonourable course for a defendant to adopt: see eg Teeven (1990), n 18 above, p 9, who also suggests that the defendant may have feared the interference of equity, citing S F C Milsom, *Sale of Goods in the Fifteenth Century* (1961) 77 Law Quarterly Review 257–284, 261–262, 266; David Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford University Press, Oxford, 1999) p 32; Baker (2002), n 28 above, p 323; Coke CJ was to say, in connection with wager of law, that 'experience now proves that men's consciences grow so large that the respect of their private advantage rather induces men to perjury': *Slade v Morley* (1597–1602) B & M 420, 441.

38 Baker (2002), n 28 above, p 323.

[1-25] There were, however, a few types of informal debts that precluded a defendant from resort to wager at law. These included, most prominently, debts arising from the lease of land and the taking of an account before auditors where the action was to recover the rent or for the balance found due on the account.[39]

[1-26] Apart from these instances, a defendant could always elect to wage his law. However, no man could wage another's law. A consequence was that if the defendant died, his executors could not wage law in his stead. As a jury trial could not be forced onto the executors, there was the further consequence that an action of Debt *sur contract* could not be maintained against the debtor's executors.[40] The practical result was that a debtor's unsealed debts died with him, unless they were of a variety exempted from wager of law.[41]

[1-27] In the early fourteenth century the absence of a requirement for sealing in an action of Debt *sur contract* gave rise to the idea that the plaintiff needed to demonstrate that the defendant had received *quid pro quo*; that is, some benefit (*quid*) in exchange for the subject matter of the plaintiff's claim in Debt[42] (*pro quo*):[43]

> By the middle of the 15th century the *quid pro quo* of the action of Debt had become a technical doctrine with marked similarities to executed consideration as it later evolved. … the early common law appears to have recognised as falling within the sphere of Debt a miscellaneous list of transactions common in everyday life, such as loans, sales, leases, hire and contracts of service generally. Seeking a generalisation which would link together and explain the basis of liability in these miscellaneous cases, the fathers of the common law … found it in the fact that the plaintiff in an action of Debt had handed over something in the shape of property or services to the other party (*quid pro quo*). By the 15th century the specific cases in which Debt sur contract lay had been generalised into a technical doctrine of *quid pro quo*, which may be expressed by saying that a party's obligation to pay was legally binding because the plaintiff had conferred a benefit on him.

[1-28] Thus, if a carpenter agreed to make some furniture and received payment, but then did not make the furniture, the customer could claim in Debt *sur contract* because the carpenter had received *quid pro quo* (the payment).

39 Milsom (1981), n 18 above, p 255; 'Wager was excluded in this Debt action due to the fact-finding that had already taken place during the accounting': Teeven (1990), n 18 above, pp 11–12.

40 Baker (2002), n 28 above, p 326.

41 Milsom (1961), n 37 above, p 264.

42 A W B Simpson, *A History of the Common Law of Contract*, (Clarendon, Oxford,1975) pp 153–169, 193–196, 424–426; Milsom (1981), n 18 above, pp 260–262; John Barton, *The Medieval Contract*, in John Barton (ed), *Towards a General Law of Contract*, (Duncker & Humblot, Berlin, 1990) 15–37, pp 23–37; Teeven (1990), n 18 above, pp 11–13; Ibbetson (1999), n 37 above, pp 80–83; Baker (2002), n 28 above, pp 322–323.

43 K O Shatwell, 'The Doctrine of Consideration in the Modern Law' (1954) 1 Sydney Law Review 289–331, pp 295–296.

But if the carpenter had promised to build the furniture in return merely for the customer's promise of payment, the customer would have no action of Debt *sur contract*. In those circumstances, the customer would need to bring an action of Debt *sur obligation* if the carpenter had given a sealed bond, or an action of Covenant in the royal courts or local courts if the agreement was under seal, or an action of Covenant in the local courts if the agreement was not under seal (see below). The common law thus came to recognise 'two types of clothing for pacts: a document under seal and a *quid pro quo*.'[44]

[1-29] The first recorded instance of the requirement for a *quid pro quo* in an action of Debt based on an informal agreement appears to date from 1338.[45] The requirement quickly gained traction thereafter.[46] Its emergence in the mid-fourteenth century probably reflected gradual changes to English life already detectable in the early part of the century. Certainly by the middle of the fourteenth century, 'there was a growing realization that the common law personal actions of Covenant and Debt were ineffective remedies for the money-credit economy beginning to replace feudalism.'[47] The English feudal system had entered upon its period of decline. By the early fourteenth century, England could, indeed, already be regarded as a modern State:[48]

> Magnates remained powerful, as did relationships of loyalty that functioned outside state authority. The overarching concerns nevertheless revolved around control of the bureaucratic centralized state structures. The centralization of concerns was reflected well in the fact that county courts had become inferior courts for relatively insignificant litigation. The king's courts now served as a major forum for litigation from every region of the country; Parliament processed both local and national concerns by handling petitions, passing statutes, and granting taxation in ways that made national government coherent. The emphasis in governance was on central control, even though locally important people functioned often by virtue of royal commissions and those same people still exercised little-regulated personal authority over their unfree tenants. … the king's council, … began to crystallize already prior to the Black Death into a much more professional institution involved in the day-to-day operations of running the country. Fortuitously by 1348, then, the common law already regulated the lives and fortunes of all substantial and many insignificant Englishmen …

[1-30] Significantly contributing to feudalism's decline was the general famine produced by three catastrophically bad harvests in 1315–1317 which substantially reduced the supply of unfree labour required to work the estates. Much manorial land had to be leased out to parties who could arrange for it

44 Ibbetson (1999), n 37 above, p 82.
45 *Anon* (1338) 11 & 12 E 3 (Rolls Series) 587.
46 Teeven claims that the doctrine of *quid pro quo* was recognised by about 1400: Teeven (1990), n 18 above, p 11.
47 Teeven (1990), n 18 above, p 12.
48 Robert C Palmer, *English Law in the Age of the Black Death, 1348–1381*, (University of North Carolina Press, Chapel Hill NC, 1993) pp 2–3 (footnotes omitted).

to be worked.[49] Then, within a generation, came the Black Death (or 'Great Pestilence') which further accelerated English feudalism's decline. The first outbreak in 1348–1349 of this cocktail of diseases,[50] in which bubonic and pneumonic plagues predominated,[51] resulted in a massive death toll.[52] It significantly increased the scarcity of labour and hastened the demise of serfdom, thereby further expanding the proportion of the population engaged in free economic exchange:[53]

> In a society accustomed to very slow changes in conditions of life, the market value of labour had been doubled at a stroke. The consequence was twofold. The labourer who was already free struck for higher wages, while the villein whose labour was not free struggled against the legal demands of the bailiff for customary services which were now worth more to both parties; gradually he was led on to demand his full freedom, the right to take his labour where he would, to plead in the King's court even against his own lord, and to be free of irksome feudal dues. … The activities of the lawyers and well-to-do juries on the side of the landlords exposed the learned profession and its satellites to the popular hatred, as not a few judges and jurymen learnt to their cost in the days of [the peasants' uprising of] June 1381.

[1-31] The emergence of an explicit requirement of a *quid pro quo* in an action of Debt *sur contract* can be seen as an early response to a new situation brought about by the accelerating decline of feudalism. There arose a need to place the law relating to the enforceability of informal agreements, manifested most obviously in actions on Debt, on a basis more closely corresponding to the changing customs and expectations of the people. This reinforced foundation, incorporating a bargain-oriented conception of *quid pro quo*, better reflected the continuing emergence of an increasingly commercial society and a market-orientated national economy all the more liberated from static feudal rights and obligations: 'For the first time in English history, the ordinary man had the possessing class at his mercy.'[54]

[1-32] The requirement of a *quid pro quo* can also be seen as a fairly simple adumbration of the modern doctrine of consideration.[55] It expressed the

49 Paul Johnson, *A History of the English People*, (Weidenfield & Nicolson, London, 1985) p 141.
50 There were three subsequent major outbreaks of the Black Death in the fourteenth century—1361, 1368 and 1375.
51 Johnson (1985), n 49 above, p 141.
52 The population of England was reduced, within the space of 16 months, from about 4 million to about 2½ million. Some villages and hamlets ceased to exist altogether, the whole population having perished: G M Trevelyan, *History of England* (Longmans Green & Co, London, 3rd edn, 1952) p 237; The number of beneficed clergy declined by about 40%, and tenants in chief by about 27%. The volume of litigation declined by more than 40% between 1348 and 1353: Palmer (1993), n 48 above, p 3.
53 Trevelyan (1952), ibid p 237, 240.
54 Ibbetson (1999), n 37 above, p 141.
55 'In the sixteenth century the notion of *quid pro quo* would have some tenuous and indirect influence on the development of the doctrine of consideration': Teeven (1990), n 18 above, p 11.

fundamental notion that an unsealed agreement was enforceable only if it had been concluded as part of a bargain or exchange between the parties.

[1-33] The common law thus committed itself early to a law of contract in which more than a serious promise was required; there also needed to be a bargain towards which each party had made a contribution. This reflected the accelerating emergence of a commercial spirit in English life as the feudal Middle Ages waned and England assumed a leading role in the European transition to modernity.

[1-34] That the requirement of *quid pro quo* kept, however, one foot firmly planted in a medieval framework is evidenced by the requirement that that the beneficial *quid* conferred by the plaintiff be actually executed and not merely promissory.[56]

(c) *Action of Debt sur obligation*

[1-35] A claimant could bring an action of Debt *sur obligation* where the agreement was embodied in a bond. This sealed instrument committed an 'obligor' to pay an 'obligee' a specified penalty, usually in the form of a fixed sum of money. The simplest case was where a borrower executed a bond specifying his obligation to a creditor. If the creditor brought an action of Debt on the bond, and if the debtor could not produce a sealed acquittance or establish a recognised vitiating factor such as fraud, duress or *non est factum*, the debtor would be bound to pay by virtue of the bond itself. Indeed, even if the borrower had repaid the money but could not produce a sealed acquittance he would be obliged to pay again.[57] There was no need to try the underlying transaction as such.

[1-36] Rigidly formal though Debt *sur obligation* might appear, it was nevertheless capable of serving transactions somewhat more sophisticated than simple loans. The parties to an agreed transaction might deposit parallel bonds with a stakeholder, who would then deliver both bonds to the non-breaching party in the event of the agreement's non-performance.[58] Thus, a purchaser of oxen could execute a bond obliging himself to the vendor in the agreed

56 'It was quite clear … that the benefit, whether conferred on the defendant himself or on a third person at his request, must have been actually conferred. A mere promise to confer it would not be sufficient.': Sir William Holdsworth, *A History of English Law*, (vol III, Methuen, Sweet & Maxwell, London, 1966) p 423. There was an important exception, of sorts, where sale of goods was concerned. A theory developed that ownership in the goods passed at the time of the agreement. This created a right in Detinue if the goods were not delivered to the purchaser, 'but it is clear that a right to sue in detinue is almost as substantial a benefit as performance; and therefore a contract to sell which conferred such a right would be a *quid pro quo* for the right to sue in debt': Holdsworth (1966), n 56 above, p 356.

57 Milsom (1981), n 18 above, p 250.

58 Ibid pp 250–251.

purchase price and the vendor could execute another bond obliging himself to the purchaser in the sum of a penalty (that is, for non-delivery, though this condition would not be mentioned in the bond). In the event of breach, and with the assistance of the stakeholder, the non-breaching party could bring an action on the breaching party's bond claiming the sum therein specified.

[1-37] At a slightly higher level of sophistication, and dispensing with the need of a stakeholder, there was the 'conditioned' or 'conditional' bond.[59] Such a bond would state that the obligor was bound to pay the obligee a specified sum unless a specified condition was satisfied.

[1-38] Thus, the vendor of oxen could bind himself to pay a sum of money (*de facto*, a penalty) to the purchaser unless he delivered them to the purchaser in accordance with the terms of the condition. Also, the purchaser could bind himself to pay a sum of money (*de facto*, the purchase price and possibly an additional penalty) unless the oxen were not delivered in accordance with the terms of the condition. In the event of the transaction's non-performance, the non-breaching party could bring an action of Debt on the defendant's bond, and the defendant would be obliged to pay the sum specified unless he could prove that the condition had been fulfilled.

[1-39] The conditional bond was 'the form in which most important transactions were made and sued upon until the sixteenth century, and it accounts for a considerable proportion of the business of the court of common pleas.'[60]

[1-40] Nevertheless, there were some serious limitations on actions of Debt from the perspective of a sophisticated law of contract. Neither variety of Debt action would succeed if the price of goods the subject of the action was not fixed or if the goods were not in existence at the time of the agreement's conclusion.[61] The action of Debt was also structurally unable to assist with the non-performance of executory promises of future performance—the underlying transaction needed to be executed on one side. The utility of Debt *sur obligation* as a general contract remedy was limited by the requirement of a sealed bond, and Debt *sur contract* was usually not available against the debtor's executors.

(d) *Action of Covenant*

[1-41] In the twelfth century, a claimant who could not (or preferred not to) satisfy the requirements of an action of Debt might instead have sought some satisfaction in an action of Trespass. The trespassory wrong asserted

59 Ibid p 251.

60 Ibid p 251; Baker (2002), n 28 above, p 324.

61 Teeven (1990), n 18 above, pp 7–9; Baker (2002), n 28 above, p 326.

by such an action was the defendant's breach of the agreement. During the thirteenth century, this species of Trespass action evolved into the distinct action of Covenant. This new action existed for the enforcement of obligations in the form of executory promises of future performance, originally to protect certain lessees of land. By the early thirteenth century actions in Covenant had become well established,[62] the action extending also to a wide range of promises beyond leases of land:[63] 'And let there be writs of Covenant according to the complaints of the contracting parties and the diversity of the cases.'[64]

[1-42] By the close of the reign of Edward I (1272–1307), however, access to the action of Covenant was narrowed by a rule that where an action of Debt lay, it was to provide the exclusive remedy.[65] Claims for sums certain conferred by deed were therefore beyond the reach of Covenant. Thus, the primacy of Debt over Covenant was established by the turn of the fourteenth century, a position to be enjoyed by the action of Debt in the realm of contract law until Stuart times.

[1-43] Further cementing Debt's position of primacy was another restriction on Covenant imposed at about the same time. In the royal courts there arose a rule, already well-established by not later than 1321, requiring that an action of Covenant could succeed only if the agreement had been embodied in a deed.[66] Covenant was an essentially contractual action which was available to enforce executory agreements. The requirement of sealing forestalled the possible future emergence of *quid pro quo* in actions of Covenant before

62 Simpson (1975), n 42 above, p 9; Ibbetson (1999), n 37 above, p 21.

63 C H S Fifoot, *History and Sources of the Common Law: Tort and Contract* (Stevens, London, 1949) pp 255–256; Teeven (1990), n 18 above, p 5; Ibbetson (1999), n 37 above, pp 21–22; Baker (2002), n 28 above, p 74.

64 Statute of Wales, 12 Edw I, Cap 6. Cap 10 of the same Statute.

65 Fifoot (1949), n 63 above, pp 258–259.

66 As to the immediate causes of this change in the royal courts, see: D J Ibbetson, 'Words and Deeds: The Action of Covenant in the Reign of Edward I' (1986) 4 Law and History Review 71–94; R C Palmer, 'Covenant, Justices Writs, and Reasonable Showings' (1987) 31 American Journal of Legal History 97–117; Ibbetson (1999), n 37 above, pp 24–28; Teeven (1990), n 18 above, p 6; Baker (2002), n 28 above, pp 318–320. In 1321, an action of Covenant before a royal court in eyre sitting in the Tower of London against a carrier who had not honoured his promise to convey a cartload of hay from Waltham to London failed for lack of a deed embodying the agreement. In reply to the plaintiff's protest that a deed could not be expected for such an agreement, Herle J replied that 'for a cartload of hay we shall not undo the law' (*Anon* [*Case of the Waltham Carrier*] (1321) B & M 285, 286). A deed was not required in the local courts, but by the later middle ages many local courts had ceased to function either effectively or at all so that for many plaintiffs the royal courts were the only courts available. Nevertheless, it is probably more accurate to say that the requirement of a deed 'was not … a change in the law so much as a demarcation of jurisdiction': Baker (2002), n 28 above, p 320. Furthermore, Covenant actions for sums above 40 shillings were forced into the royal courts and monetary inflation gradually had the practical effect of depriving local courts of jurisdiction: Teeven (1990), n 18 above, pp 6–7. Nevertheless, it was not a requirement of the common law that a covenant be sealed if the action was brought in a borough court: *Welshe v Hoper* (1533) B & M 286.

the royal courts. Hitherto, Covenant was an action which had permitted the enforcement of informal gratuitous promises:[67]

> This insistence upon formality stopped the growth of Covenant; but it is interesting to reflect that, had the decision been otherwise, the common law would have enjoyed, at the beginning of the fourteenth century, a general remedy for breach of contract based, not, as ultimately evolved, upon a bilateral bargain, but upon a unilateral promise.

[1-44] The consequence of requiring a deed was that 'informal agreements were shut out from the central courts, and the development of a law of consensual contracts was therefore stifled by the formal requirement of a seal.'[68]

[1-45] The distinction between sealed and unsealed agreements was fundamental in early English law at least insofar as the jurisdiction of royal courts were concerned.[69] The matter was essentially one of proof. The key to unlocking the distinction lies in the etymology of 'deed' as an act or conduct, as distinct from mere words:[70]

> A covenant or grant consisted in fleeting words, and no action was allowed in the royal courts for mere breath. A sale, a loan, a hiring, on the other hand, were all visible conduct 'of which knowledge may be had'; the act generated the duty to pay, which therefore did not depend merely on words. The deed likewise was an act (*factum*), in that the specialty was sealed and delivered before witnesses as an 'act and deed'. The distinction between words and deeds ran deep in English law.

[1-46] The restrictive character of the requirement of a deed 'made excellent sense in the eyres which were unable to cope with the volume of business brought to them.'[71]

[1-47] It also made sense in the central royal courts. When an action of Covenant was to be tried, there were two principal questions to be answered; was there an agreement in terms asserted by the plaintiff, and did the defendant breach that agreement? If the matter went to trial, the answers could be determined by wager of law or by jury. Wager was regarded as a suspect procedure at Westminster because the compurgators frequently did not know the defendant. Jury trial was also problematic for a similar reason. Medieval juries were not judges of fact in the modern sense. They consisted of men who were expected to use their knowledge of local affairs and personalities in order to establish the facts; in other words, they were required to use

67 Fifoot (1949), n 63 above, p 258.

68 Baker (2002), n 28 above, p 320.

69 'Contemporaries would not have viewed this as a drastic denial of justice, when local courts were quite competent to deal with informal agreements. It was true that one could not put every covenant into writing; but then one should not be able to bother the king's central courts with every unwritten covenant.': Baker (2002), n 28 above, p 320.

70 Baker (2002), n 28 above, p 322 (citing *Loveday v Ormesby* (1310) B & M 250).

71 Ibid p 320.

CHAPTER 5

Contractual Intention

5.1 Introduction to Intention

[5-1] Not all agreements are enforceable. Even where an offer has been accepted, the terms are certain, and the promises are supported by consideration, the agreement will not be enforceable as a contract if the parties lacked an intention to be legally bound.

[5-2] As the range of things which could be regarded as consideration expanded during the course of the nineteenth century, the usefulness of consideration diminished in providing a sign of contractual intention. It became increasingly easy to identify the existence of consideration, but there were many situations where reasonable expectations indicated that no intention to create legal relations existed. This was particularly true in relation to agreements of an essentially domestic or social character.

[5-3] In order to deal with this development, there emerged in the common law of the late nineteenth and early twentieth centuries a separate requirement of contractual intention as an essential element of contract validity. The requirement of an intention to be contractually bound plays, however, a less important role in the common law of contract than it does in most civil law systems. In the case of commercial agreements, the common law will readily imply an intention to be contractually bound (*animus contrahendi*) where consideration is present.

[5-4] Where, however, there are reasonable grounds to suppose that an intention to create legal relations was absent in an agreement's conclusion (most notably in the case of domestic or social agreements) common law courts will not infer the existence of contractual intention from the mere presence of consideration. Rather, the party asserting the existence of a contract must furnish separate evidence of *animus contrahendi*.

[5-5] In contrast to most civil law systems, the role of intention to be legally bound plays an auxiliary role to that of consideration in establishing the existence of a contract at common law. Most of the juridical load which is borne by intention in the contract law of civil law systems is borne, in the common law of contracts, by consideration.

[5-6] There is often a substantial practical overlap between the requirements of contractual intention and certainty of terms. It will frequently be the case that a lack of contractual intention can explain an apparent uncertainty in the agreement's essential terms, and conversely that apparent uncertainty can indicate a lack of intention.[1]

[5-7] At common law, this area of contract doctrine is dominated by two rebuttable presumptions. The first of these is the presumption that parties to an agreement of a domestic or social character do not intend their agreement to be contractually binding. The second presumption is a mirror image of the first; parties to an agreement of a commercial character do intend their agreement to be contractually binding. In each case, the presumption can be displaced by evidence indicating that reasonable persons in the position of the parties would have possessed a contrary intention at the time the agreement was concluded. As with all rebuttable presumptions, they will stand unless displaced.

5.2 Domestic Agreements

(a) Presumption against intention

[5-8] Among the most common types of agreements are those made among family members residing together. Every day, countless agreements are made by which cohabiting family members undertake to do things for each other, often in exchange for reciprocal undertakings. A husband might promise to collect the children from school today in return for a promise by the wife to perform the task tomorrow. A parent might offer to pay a child some pocket money in exchange for the child performing some chores. A child might offer to buy his parent a meal if the parent will quit smoking. In each case, the terms may be sufficiently certain, and there is consideration for the promises—but can it reasonably be said that the parties intended that the law might be used to enforce the agreements?

Sun Er Jo v Lo Ching

High Court
[1996] 1 HKC 1; [1995–2000] HKCLRT 14

The plaintiff was a 90-year-old mother of five adult children. After a falling out with her children concerning certain financial and property transactions, she commenced proceedings against them primarily for breach of trust. One of her claims, however, was for repayment of expenses in raising her youngest son while the family resided in Shanghai. Although it was not clear whether this part of the claim was based in contract (none of the parties were legally represented), the trial judge disposed of it on contract grounds.

Yeung J

(judgment delivered in Chinese): In relation to Madam Sun's claim for rearing expenses from Lo Kun, it was right and proper that parents bring up their children and this did not form a basis for a compensation claim. Family arrangements made between parents and children, husband and wife, or brothers and sisters were generally not legally binding, unless it was shown that they have clearly intended to enter into legal relations. Therefore, Madam Sun could not claim back the RMB100,000 from Lo Kun. *Balfour v Balfour*[2] applied.

[5-9] As Yeung J elected to treat the plaintiff's claim against her youngest son as one based in contract, he could just as easily have disposed of it on the basis that there had been no offer, no acceptance, no certainty of terms and no consideration. He chose, instead, to base his finding on a lack of intention to create legal relations. In so doing he recognised that agreements between close family members are 'generally' not legally binding unless a clear intention to the contrary is shown (that is, they are rebuttably presumed not to be legally binding).

(b) Married couples

[5-10] Why should agreements between 'close family members' not generally be legally binding? The answer lies in the English authority to which Yeung J referred.

Balfour v Balfour

Court of Appeal (England and Wales)
[1919] 2 KB 571; [1918–1919] All ER Rep 860; 88 LJKB 1054; 121 LT 346

The defendant was a British imperial civil servant based in Ceylon, where he lived with his wife. In November 1915, they returned to England for a visit. Some ten months later at the end of his leave period, the defendant returned to Ceylon but his wife remained behind on medical advice. Before departing from England, the defendant agreed to pay his wife £30 per month towards her maintenance until they could be reunited. Subsequently, the defendant wrote to his wife suggesting that they should henceforth live apart. The wife obtained a decree nisi of divorce, and commenced proceeding against the defendant for breach of his contract in respect of his non-payment of the promised maintenance. The wife succeeded at trial, and the defendant appealed.

Atkin LJ:

The defence to this action on the alleged contract is that the husband says he entered into no contract with his wife, and for the determination of that it is necessary to remember that there are agreements between parties which do not

1 Eg, in *J H Milner & Son v Percy Bilton Ltd* [1966] 2 All ER 894, [1966] 1 WLR 1582, the deliberate use of 'somewhat vague and equivocal' language in formulating an agreement to establish a solicitor's retainer was held to indicate a lack of contractual intention.

2 [1919] 2 KB 571, [1918–1919] All ER Rep 860.

result in contracts within the meaning of that term in our law. The ordinary example is where two parties agree to take a walk together, or where there is an offer and an acceptance of hospitality. Nobody would suggest in ordinary circumstances that those agreements result in what we know as a contract, and one of the most usual forms of agreement which does not constitute a contract appears to me to be the arrangements which are made between husband and wife. It is quite common, and it is the natural and inevitable result of the relationship of husband and wife, that the two spouses should make agreements between themselves, agreements such as are in dispute in this action, agreements for allowances by which the husband agrees that he will pay to his wife a certain sum of money per week or per month or per year to cover either her own expenses or the necessary expenses of the household and of the children, and in which the wife promises either expressly or impliedly to apply the allowance for the purpose for which it is given.

To my mind those agreements, or many of them, do not result in contracts at all, and they do not result in contracts even though there may be what as between other parties would constitute consideration for the agreement. The consideration, as we know, may consist either in some right, interest, profit, or benefit accruing to one party, or some forbearance, detriment, loss, or responsibility given, suffered, or undertaken by the other. That is a well-known definition, and it constantly happens, I think, that such arrangements made between husband and wife are arrangements in which there are mutual promises, or in which there is consideration in form within the definition that I have mentioned. Nevertheless they are not contracts, and they are not contracts because the parties did not intend that they should be attended by legal consequences. It would be the worst possible example to hold that agreements such as this resulted in legal obligations which could be enforced in the courts. It would mean that when a husband made his wife a promise to give her an allowance of 30s or £2 per week, whatever he could afford to give her for the maintenance of the household and children, and she promised so to apply it, not only could she sue him for his failure in any week to supply the allowance, but he could sue her for non-performance of the obligation, express or implied, which she had undertaken upon her part. The small courts of this country would have to be multiplied one hundredfold if these arrangements did result in fact in legal obligations. They are not sued upon, and the reason that they are not sued upon is not because the parties are reluctant to enforce their legal rights when the agreement is broken, but they are not sued upon because the parties in the inception of the arrangement never intended that they should be sued upon. Agreements such as these, as I say, are outside the realm of contracts altogether. The common law does not regulate the form of agreements between spouses. Their promises are not sealed with seals and sealing wax. The consideration that really obtains for them is that natural love and affection which counts for so little in these cold courts. The terms may be repudiated, varied, or renewed as performance proceeds, or as the disagreements develop, and the principles of the common law as to exoneration and discharge and accord and satisfaction are such as find no place in the domestic code. The parties themselves are advocates, judges, courts, sheriff's officer and reporter. In respect of these promises each house is a domain into which the King's writ does not seek to run, and to which his officers do not seek to be admitted.

The only question in the present case is whether or not this promise was of such a class or not. … I think it is plainly established that the promise here was not intended by either party to be attended by legal consequences. I think the onus was upon the wife, and that the wife has not established any contract. The parties were living together, the wife intending to return to Ceylon. The suggestion is that she bound herself to accept, as he bound himself to pay £30 per month under all circumstances, and that she bound herself to be satisfied with that sum under all circumstances, and, although she was in ill-health and in this country, that out of

that sum she undertook to defray the whole of the medical expenses that might fall upon her whatever might be the development of her illness, and in whatever expenses it might involve her. To my mind neither party contemplated such a result. … For these reasons I think that the judgment of the learned judge in the court below was wrong, and that this appeal should be allowed.

Warrington and Duke LJJ agreed that the appeal should be allowed.

[5-11] Atkin LJ in *Balfour v Balfour* advanced one principal and two ancillary justifications for rejecting the contractual force of the husband's promise to pay maintenance of £30 per month to his wife. The principal justification was that the parties did not intend their agreement to create contractual relations. This justification has been criticised as being unrealistic on the facts of the case,[3] but it possesses considerable force as a general proposition. When the agreement was reached, the parties were living together as a married couple. Agreements between spouses to provide money for domestic expenses are a common feature of married life, and it surely flies in the face of reality to suggest that the parties anticipated the possibility of litigation in the event of breach. The unreality of such a suggestion is highlighted by Atkin LJ's observation that, if the arrangement were a binding contract, the husband would have had an action against the wife if she had failed to maintain herself on the monthly allowance agreed. The principal justification was also, in Atkin LJ's view, supported by the empirical fact that parties to such agreements do not in practice sue each other for breach:

> … and the reason that they are not sued upon is not because the parties are reluctant to enforce their legal rights when the agreement is broken, but they are not sued upon because the parties in the inception of the arrangement never intended that they should be sued upon.

[5-12] Both ancillary justifications are based on policy considerations. First, were agreements concerning domestic affairs between husband and wife to be actionable as contracts, the courts would be overwhelmed by the resulting litigation. This concern is perhaps exaggerated as it is unlikely that many such actions would materialise even were they well-founded in contract (except, perhaps, in the case of actions brought by estranged or former spouses). The other ancillary justification is one based upon respect for the sanctity of marriage, home and private life: 'In respect of these promises each house is a domain into which the King's writ does not seek to run, and to which his officers do not seek to be admitted.' Thus framed, the court's refusal to

3 Eg *Pettitt v Pettitt* [1970] AC 777, [1969] 2 All ER 385, [1969] 2 WLR 966, in which Lord Upjohn remarked ([1970] AC 777 at 816) that *Balfour*:

> … illustrates the well-known doctrine that in their ordinary day-to-day life spouses do not intend to contract in a legally binding sense with one another, though I am bound to confess that in my opinion the facts of that case stretched that doctrine to its limits.

See also Hedley, 'Keeping Contract in its Place: *Balfour v Balfour* and the Enforceability of Informal Agreements' (1985) 5 OJLS 391.

regard the private dealings between married couples as material suitable for interference by the State is a reflection of a fundamental value of the common law.

(c) Estranged couples

[5-13] The presumption against contractual intention in respect of domestic agreements between spouses does not apply where the parties are no longer living together in amity. In *Merritt v Merritt*[4] a husband and wife reached an agreement, after they had separated, whereby the husband would pay £40 per month in maintenance. The wife agreed to meet the monthly mortgage repayments out of that sum, and the husband promised to transfer title to her once the obligations to the mortgagee had been discharged. The English Court of Appeal held the agreement to be an enforceable contract. According to Lord Denning MR, whereas it is appropriate to presume that domestic agreements between spouses living in amity are not intended to be legally binding:[5]

> It is altogether different when the parties are not living in amity but are separated, or about to separate. They then bargain keenly. They do not rely on honourable understandings. They want everything cut and dried. It may safely be presumed that they intend to create legal relations.

(d) Other family relationships

[5-14] The presumption against contractual intention extends also to other family relationships, such as those between parent and child in *Sun Ex Jo*.

[5-15] In *Jones v Padavatton*,[6] a mother promised her daughter that if the daughter gave up a well-paying job in the United States and moved to London in order to study for the bar, she would pay the daughter a monthly allowance of $200. The idea was that the daughter would eventually qualify for the bar, then move back to Trinidad to practise law and live near her mother. The daughter agreed and moved to London in 1962, but after the daughter had spent some time in London the arrangement changed; instead of paying a monthly allowance, the mother bought a house in London in which the daughter lived rent-free and from which she derived income from the rent paid by boarders. After five years, the daughter had made very slow progress in her bar exams, and the mother sought possession of the house. The daughter resisted on the grounds that she was entitled to possession of the house pursuant to a contract with her mother. The English Court of Appeal held unanimously that there was no enforceable contract. Salmon LJ took the view that the terms of the

4 [1970] 2 All ER 760, [1970] 1 WLR 1211.
5 [1970] 2 All ER 760 at 762, [1970] 1 WLR 1211 at 1213.
6 [1969] 2 All ER 616, [1969] 1 WLR 328.

agreement lacked sufficient certainty. Danckwerts and Fenton-Atkinson LJJ rested their judgments primarily on a lack of intention to create legal relations. According to Danckwerts LJ:[7]

> There is no doubt that this case is a most difficult one, but I have reached a conclusion that the present case is one of those family arrangements which depend on the good faith of the promises which are made and are not intended to be rigid, binding agreements. *Balfour v Balfour* was a case of husband and wife, but there is no doubt that the same principles apply to dealings between other relations, such as father and son and daughter and mother. This, indeed, seems to me a compelling case. The mother and the daughter seem to have been on very good terms before 1967. The mother was arranging for a career for the daughter which she hoped would lead to success. … What was required was an arrangement which was to be financed by the mother and was such as would be adaptable to circumstances, as it in fact was. The operation about the house was, in my view, not a completely fresh arrangement, but an adaptation of the mother's financial assistance to the daughter due to the situation which was found to exist in England. It was not a stiff contractual operation any more than the original arrangement.

[5-16] That the decision in *Jones v Padavatton* was, as Danckwerts LJ acknowledged, a difficult one was because of the subject matter of the agreement, and the extensive consequences for each party in its execution. The agreement involved serious commitments on each side which went well beyond the payment of a modest maintenance allowance, and tended to suggest an arrangement that was not of a purely domestic character. The daughter, in particular, gave up a well-paying job and changed her country of residence for a period of years in reliance on the agreement. The mother, for her part, purchased a house in London. The factor which tipped the balance in the judgments of Danckwerts and Fenton-Atkinson LJJ was the vagueness in the terms of the mother's promises. This lack of contractual clarity contributed to their Lordships' findings that no binding contract was intended.

(e) Non-domestic subject matter

[5-17] Indeed, it seems that the existence of a family relationship between the parties, while important to the existence of a presumption against contractual intention, is less significant than the subject matter of the agreement itself.

[5-18] In *Fong Huen v Anthony Wong*,[8] an agreement between the plaintiff and his son-in-law by which the plaintiff delivered his daughter's title deeds into the daughter's possession in exchange for a promissory note from the son-in-law was held to be enforceable (the son-in-law needed his wife's title

7 [1969] 2 All ER 616 at 620.
8 [1975] HKLR 21, [1975] HKCU 4 (HKSC).

deeds as security for a bank loan in order to start a new business). In *Yang Foo-Oi v Wai Wai Chen*, it was held that an agreement to effect an *inter vivos* distribution of billions of dollars' worth of assets by a father to his wife and two daughters was intended to be legally binding, because the parties must have realised that the exercise 'could lead to litigation' between them.[9] In *Pearce v Merriman*,[10] it was held that a tenancy agreement under which a husband paid rent to his wife was a legally enforceable contract. In *Errington v Errington and Woods*,[11] an agreement between a property owner on the one hand, and his son and daughter-in-law on the other, by which the property owner agreed to transfer title to the couple if they met all the monthly mortgage repayments, was held to be an enforceable contract. In *Snelling v John G Snelling Ltd*,[12] an agreement among three brothers concerning the finances of their family-owned company was held to be an enforceable contract.

[5-19] The thread connecting all these authorities is that, although the agreements were between family members, they were not of an essentially domestic nature. They concerned matters of an essentially commercial character, or involved substantial interests in money or property. This emphasises the point that the presumption against contractual intention exists in relation to agreements of a domestic nature, and not simply to agreements among family members. As Deputy Judge Muttrie observed in *Ma Chi Wing Wendy v Estate of Ma Vincent (deceased)*:[13]

> Of course, a family arrangement to look after aged parents may never be intended as a legal contract. The parties may never intend to enter into a legal relationship. Very often that is what happens. Where that happens, the courts will not enforce the agreement. See *Balfour v. Balfour* [1919] 2 KB 571. But there is no presumption that this must be so, simply because the agreement is within the family. The intention of the parties is a question of fact and to be inferred from the terms of the agreement and the surrounding facts and circumstances.

[5-20] Agreements of a domestic nature will typically involve family members, but not all agreements between family members are of a domestic nature and subject to the presumption against contractual intention.

9 [2016] HKCU 2874 (unreported, HCA 1739 & 1739C/2010, 29 November 2016), para 187 (Anthony Chan J, HKCFI).

10 [1904] 1 KB 80.

11 [1952] 1 KB 290, [1952] 1 All ER 149, [1952] 1 TLR 231. In *Hardwick v Johnson* [1978] 2 All ER 935, [1978] 1 WLR 683, per Roskill and Browne LJJ, an agreement by which a property owner agreed to let her son and daughter-in-law reside in the house in return for £7 per week towards paying off the purchase price was held to be an enforceable contractual licence.

12 [1973] QB 87, [1972] 1 All ER 79.

13 [2005] HKCU 638 (unreported, HCA 3913/2001, 20 May 2005) (HKCFI), para 21.

(f) *Rebutting presumption in domestic agreements*

[5-21] Even where the subject matter of the agreement is essentially domestic or social in character, it is still possible to rebut the presumption against contractual intention.

[5-22] Relevant factors in determining whether the presumption affecting domestic and social agreements has been rebutted are: **(1)** whether the agreement is executory or executed; and **(2)** if executed, the seriousness of the consequences for the non-breaching party should the agreement be breached. The greater the extent to which the domestic or social agreement has been executed, and the more its breach entails serious consequences for the non-breaching party, the more it is likely that the presumption against contractual intention will be rebutted.

Parker v Clark

Exeter Assizes
[1960] 1 All ER 93; [1960] 1 WLR 286

Mrs Parker was Mrs Clark's niece. She and her husband, Commander Parker (a retired naval officer), were on good terms with Mrs Clark and her husband. The Clarks were in their 70s and lived in a commodious house (*Cramond*) in the seaside resort town of Torquay. The Parkers were some 20 years younger and lived in a cottage in another part of England. The Clarks felt they had reached an age where they could no longer look after themselves in their large house, and invited the Parkers to come and live with them. The proposal was contained in a detailed letter from the Clarks to the Parkers. The Clarks proposed that the Parkers move out of their cottage (*The Thimble*), the Clarks would leave *Cramond* to the Parkers at death, the two couples would share household expenses, the Clarks would acquire a new television set (a significant luxury in the 1950s) and a new car, and hire daily help for the running of the large house. The proposal also suggested that the Parkers might sell *The Thimble*. The Parkers sold *The Thimble*, and gave the proceeds to their daughter to buy herself a residence. They moved in with the Clarks, but the arrangement quickly led to disharmony between the two couples. About 18 months after the Parkers had moved in, the Clarks asked them to leave. The Parkers left soon thereafter, fearing that they would otherwise be evicted. After moving out, the Parkers commenced proceedings against the Clarks for breach of contract. The Clarks defended by pleading, *inter alia*, that there had never been an intention to create legal relations.

Devlin J:

...

The question must, of course, depend on the intention of the parties to be inferred from the language which they use and from the circumstances in which they use it. On the plaintiff's side, I accept his evidence that he considered that he was making a binding contract. An important factor in this was that he disposed of his own residence. It does not matter for this purpose whether it was or was not a term of the contract that he should sell *The Thimble*; the important thing is that the contract required him to give up his occupation of *The Thimble* and that he was always quite clear, and made it quite clear, that he would not give up occupation unless he also gave up the ownership and parted with the property. He would not have done

that, he says (and I believe it), unless he thought that he was securing another permanent home. There is, undoubtedly, in the arrangement a lack of formality on which counsel for the defendants greatly relies. This, I think, is largely explained by the relationship between the parties; it is easier to demand formal documents from a stranger than it is from a relative and friend. It is clear that the plaintiff constantly relied on the letter of 25 September 1955 as a sort of title to his rights; he kept it and referred to it whenever his rights were called in question. When, on 24 October 1957, they were seriously threatened, he went forthwith and consulted a solicitor. He is not, in my judgment, the sort of man who would "think up" a legal action as an afterthought when he found that he was not getting what he wanted.

The plaintiff is not a moneyed man. On the strength of the defendant's promise he, so to speak, put down £672 10s. That is the figure which is agreed as the expense which he incurred in giving up *The Thimble*, on the assumption that he could re-purchase *The Thimble* or a cottage like it. In addition to that, he tied up £2,000, so that he has never since been in a position to buy another property like *The Thimble* and has never in fact bought one. The defendant knew this and had plenty of time to reflect on it between 25 September 1955, when he wrote his letter, and 1 March 1956, when the plaintiffs arrived. If he had thought that all that his letter involved was an amicable arrangement terminable at will, I cannot believe that he would not have enlightened the plaintiff and, as a cautious man himself, have warned him against the folly of what he was doing. I cannot believe either that the defendant really thought that the law would leave him at liberty, if he so chose, to tell the plaintiffs when they arrived that he had changed his mind, that they could take their furniture away and that he was indifferent whether they found anywhere else to live or not. Yet this is what the defence means. The defendant gave several answers which show that this was not really his state of mind. He said that the object of the letter was to induce the plaintiffs to come to *Cramond*; and he agreed also that he made the will in fulfillment of the promise. I am satisfied that an arrangement binding in law was intended by both sides.

The defendants' second submission is that the agreement is not sufficiently clear in its terms to be capable of constituting a legal contract. No doubt, if the letter had been drafted by a lawyer, he would have gone into much more detail and would, for example, have specified how the running expenses were to be determined and matters of that sort. An agreement of this kind, made in general terms, requires good will and co-operation from both sides if it is to be successfully worked. But it was, in fact, made to work for more than a year and a half, and the defendants fulfilled all its terms even to the point of the making of a will to the required effect. Counsel for the defendants has not argued that the contract was too imprecise in detail to be enforceable; but he contended that two of the terms pleaded in the statement of claim were not sufficiently clearly set out in the letter of 25 September 1955. The former of these is the first pleaded term which alleges that the plaintiffs should cease to occupy and should dispose of their interest in *The Thimble*. Counsel for the defendants argues that there is nothing express or to be implied in the letter which requires the plaintiffs to sell *The Thimble*. Counsel for the plaintiffs accepts this and agrees that the only term to be implied from the letter about *The Thimble* is that the plaintiffs should cease to occupy it. But the elimination of part of the term pleaded does not affect the relief for which the plaintiffs are asking. The main consideration for the defendants' promise was that the plaintiffs should come and live at *Cramond*. This they have done. It may be that the request was also dependent on *The Thimble* being sold; but, if it was, they have done that also.

Judgment for Plaintiffs.

[5-23] The arrangement between the Parkers and the Clarks was certainly one of a predominantly domestic character, yet the consequences of non-performance for the claimants were serious. This was compounded by the fact that the agreement was substantially executed. In such circumstances, courts will be more reluctant to hold either that the parties lacked contractual intention or that the terms of the agreement were insufficiently certain to found an enforceable contract.

(g) Partly performed agreements

[5-24] It would seem to follow that some executory agreements which would be regarded as unenforceable either for lack of contractual intention or uncertainty of terms, would be regarded as enforceable once they have been at least partially executed by one party. Indeed, *Parker v Clark* appears to be one such example.

[5-25] As *Jones v Padavatton* illustrates, a lack of certainty in the agreement's terms can be an independent basis for denying it contractual force, and simultaneously a reason for concluding that the parties lacked contractual intention. Where, however, the agreement is at least partially executed on one side, the courts will be more willing to regard apparent uncertainties in the agreement's terms as resolved by reference to the way in which the parties have actually given effect to the agreement. This will in turn tend to dispel doubts concerning the related issue of contractual intention.

(h) Agreements to marry

[5-26] At common law, an agreement to marry is enforceable as a contract, and actions for breach of promise to marry were once not uncommon.[14] Legislation enacted in 1971 now deprives such agreements of their contractual force.

Law Amendment and Reform (Consolidation) Ordinance

(Cap 23)

23. Engagements to marry not enforceable at law

(1) An agreement between 2 persons to marry one another shall not have effect as a contract giving rise to legal rights and no action shall lie for breach of such an agreement.

14 Eg, *Tang Ho Foon v Leung Sek* [1953–1955] HKDCLR 152 (HKDC).

5.3 Social Agreements

(a) Presumption against intention

[5-27] There is a rebuttable presumption against an intention to create legal relations also where the agreement is social in nature, such as 'where two parties agree to take a walk together, or where there is an offer and an acceptance of hospitality.'[15] The presumption can extend even to social agreements made within the context of paid employment.

Coward v Motor Insurers Bureau

Court of Appeal (England and Wales)
[1963] 1 QB 259; [1962] 1 All ER 531; [1962] 2 WLR 663;
[1962] 1 Lloyd's Rep 583

Cole had been in the habit of giving his workmate, Coward, a lift to work as a pillion passenger on his motorcycle. Coward had paid Cole for the service. On one such journey, the motorcycle was involved in a traffic accident in which both Cole and Coward were killed. Coward's widow obtained judgment against Cole's administratrix, but the judgment was unsatisfied because Cole's insurance did not cover pillion passengers. On the asserted basis that Cole was required by law to have taken out insurance in respect of pillion passengers whom he had a contractual obligation to carry,[16] Coward's widow then brought proceedings against the Motor Insurers Bureau (a government agency from whom compensation could be obtained in respect of unlawfully uninsured traffic accidents). The widow failed at trial, and appealed.

Upjohn LJ:

...

... [T]he fact that both parties are dead, we believe matters little, for if the question had been posed to Coward or Cole: 'Did you intend to enter into a legal relationship?' each would probably have answered 'I never gave it a thought.' The practice whereby workmen go to their place of business in the motor car or on the motor cycle of a fellow- workman on the terms of making a contribution to the costs of transport is well known and widespread. In the absence of evidence that the parties intended to be bound contractually, we should be reluctant to conclude that the daily carriage by one of another to work on payment of some weekly (or it may be daily) sum involved them in a legal contractual relationship. The hazards of everyday life, such as temporary indisposition, the incidence of holidays, the possibility of a change of shift or different hours of overtime, or incompatibility arising, make it most unlikely that either contemplated that the one was legally bound to carry and the other to be carried to work. It is made all the more improbable in this case by reason of the fact that alternative means of transport seem to have been available to Coward.

15 *Balfour v Balfour* [1919] 2 KB 571 at 578, per Atkin LJ.

16 In *Albert v Motor Insurers Bureau* [1972] AC 301, [1971] 2 All ER 1345, [1971] 3 WLR 291, the House of Lords held that, in actions of this kind, it was not necessary to prove the existence of a contract, and *Coward* was disapproved. This does not, however, invalidate the *Coward* court's analysis on the existence of a contract.

On the probabilities of the case, therefore, we reach the conclusion that, while admitting the evidence rejected by the learned judge which, in our judgment, clearly proved an arrangement whereby Coward paid a weekly sum to Cole for transporting him to and from his work, neither party intended to enter into a legal contract.

Appeal dismissed. Upjohn LJ gave the judgment of the Court, the other members of which were Sellers LJ and Diplock LJ.

[5-28] The critical question in *Coward* was the hypothetical one posed to the two deceased workmates. The court hypothesised whether the two men would have agreed, had they been asked, that they had a binding contract. The experience of daily life and the customs and expectations of the people, which provide the sinews of the common law, compelled an answer in the negative.

(b) Rebuttal of presumption

[5-29] It is, however, possible to rebut the presumption against contractual intention in social agreements where reasonable persons in the position of the parties would regard their arrangements as involving legal obligations.

Wu Chiu Kuen v Chu Shui Ching

High Court
[1992] HKCU 29 (unreported, HCA 4081/1991, 28 February 1992)

Patrick Chan, Deputy Judge:

This is a claim by the plaintiff against the defendant for a half share in the winnings of a Mark Six ticket which came out in a Lottery on 3 April 1990. The plaintiff claims that he and the defendant contributed equally towards the buying of four Mark Six tickets one of which won a First Prize and six Third Prizes, with a total winning of $1,118,000 and that he was entitled to $559,000.

The plaintiff was a casual worker or messenger at the Chuen Shek Mahjong Amusement Company in Castle Peak Road. It was a place where people would go to play mahjong and was commonly called a Mahjong School. The plaintiff's work consisted of doing odd jobs in the Mahjong School and running errands for patrons. Most of the time, he would run these errands on the instructions of his superiors and supervisors, but occasionally, he would receive instructions directly from regular patrons whom he had befriended. Whenever he went out, he would either seek the permission of his supervisors or notify them first.

The defendant was a regular patron of this Mahjong School and went there two or three times a week. In April 1990, he had known the plaintiff for about one year. It is the plaintiff's case that in the past, on as many as 30 occasions the two had shared in the buying of Mark Six tickets. Sometimes, he kept the tickets and at other times the defendant did. ... They had never won before. On 3 April 1990, at around 4 pm, the defendant went to the Mahjong School to play mahjong. ... The plaintiff said that while playing mahjong, the defendant called him to the table, took out a few $10 notes from the drawer, gave them to him and asked him to share in the buying of Mark Six tickets for the Lottery that evening. ... The plaintiff did not count the money at that stage but merely said that the defendant could leave the matter to him. He then left the Mahjong School and went to the Off-course Betting Centre in Castle Peak Road. He ...bought two computer quick-pick tickets of $10 each, one computer quick-pick multi-bet ticket and another multi-bet ticket with seven

numbers of his own choice … Each multi-bet ticket cost $14. For these four tickets, he paid $48 using the notes given to him by the defendant (which he found out to be $30) and $20 of his own money. Each of them therefore had contributed $24. … When he returned to the Mahjong School, he handed the four tickets to the defendant together with, he said, the change of $6 and told the defendant to keep the tickets well. According to him, the defendant said: 'All right. If the tickets win, you just wait for the sharing of money.'

Later in the evening, the plaintiff rang up the Jockey Club and found out that the multi-bet ticket which he selected had won a First Prize with a winning of $990,000 odd. At that stage he did not know it had also won six Third Prizes. He said he was very happy and could not get to sleep the whole night. Early next morning, he went to a nearby Police Post and wanted to report this to the Police. He said he did that because he did not know where the defendant lived and he feared that the defendant might not share the winnings with him. He subsequently spoke to the Police Officer at the Post but was told that it was still early, that he should wait until the Jockey Club opened and that the defendant might be looking for him there. So the plaintiff went to the Jockey Club. He told the Manager there that he had shared the winning ticket with another and he gave his particulars. The Manager told him to wait. Later, the defendant arrived with his wife and son at the Jockey Club. The plaintiff said that the defendant offered to pay him $100,000 but he refused to accept claiming for half of the winnings. A dispute ensued. The plaintiff dialed 999 and called for the police. They then went together to the Happy Valley Police Station. However, the officer there, he said, abused him. So he left the Police Station.

Thereafter, the plaintiff tried to look for the defendant who did not go to that Mahjong School any more. …

Some time in October 1990, while he was at work, the plaintiff received a telephone call from a friend telling him that the defendant was then playing mahjong in a Mahjong School near Temple Street. He went there immediately and located the defendant. He asked the defendant to go to have tea in a nearby cafe. There he demanded for the money. An unpleasant exchange followed. In the spur of the moment, he said, he picked up a broomstick and hit the defendant with it. It was put to him that in fact he went there with a friend and armed with a hammer and that he blackmailed and injured the defendant. The plaintiff denied this. But in any event, the matter was reported to the Police. He was arrested, charged with assault and later fined $1,000. Having failed to obtain any money from the defendant, he commenced this action. …

A lot of the evidence is clearly in dispute. But both parties accept that:

(1) on 3 April 1990, at the Mahjong School, the defendant asked the plaintiff to buy some Mark Six tickets and gave him some money;

(2) the plaintiff did go and buy the 4 tickets and handed them to the defendant;

(3) on 4 April 1990, the plaintiff first went to the Police in the early morning, then went to the Jockey Club and finally reported the matter to the Happy Valley Police Station;

(4) at the end of April 1990, the plaintiff sought the assistance of the Legal Aid Department and he asked these four witnesses to support him, and

(5) in October 1990, the plaintiff demanded money from the defendant and when this failed to get anything, he assaulted the defendant with a hammer.

The main issue I have to decide is whether the plaintiff and the defendant had agreed to share in the buying of the four Mark Six tickets both contributing equally for these tickets. The plaintiff said they did. The burden is on the plaintiff to satisfy

me on a balance of probabilities that this was the case. From the preceding paragraph, it is quite clear that his behaviour after the incident was to say the least rather unusual. In my view, there can only be three possible situations. First, there was indeed such an agreement in which case, the plaintiff is entitled to a share of the winnings. He has a legitimate interest in the tickets and must therefore succeed. Second, there was no such agreement and the plaintiff was merely trying to get as much money as possible out of the defendant by lawful or unlawful means in which case the plaintiff must fail. Third, there was no such agreement but the defendant had made a gratuitous promise to the plaintiff to share the winnings, if any, with him. This somehow gave the plaintiff a reasonable expectation that he would get a substantial share in the winnings. In such a case, he would also fail because there was no consideration for the defendant's gratuitous promise. It is not the plaintiff's case that going out to buy the tickets was a consideration for a share in the winnings. I have to analyse the evidence, particularly the plaintiff's behaviour, in the light of these 3 possible situations.

[Deputy Judge Chan then engaged in a detailed analysis of the evidence, and continued]

Having heard all the evidence and watched the demeanour of all the witnesses including the plaintiff and the defendant, I must say I do not find their evidence to be entirely satisfactory. There are clearly exaggerations on some matters and evasiveness on other matters. The plaintiff was repetitive and grudging while the defendant was surprisingly detailed in respect of some conversations and yet could not remember other matters. I would however give allowance for their background and emotional involvements in this matter. The crucial issue here is whether the plaintiff and the defendant had, on 3 April, agreed and intended to share in the buying of the four Mark Six tickets. The burden of proof is clearly on the plaintiff. After a careful consideration of all the evidence, I take the view that the series of conduct of the plaintiff at the material time and after the incident, are more consistent with a person having a legitimate interest and that if he did not have any share in the tickets, he would not have behaved in the way he did afterwards. I am therefore more inclined to accept the plaintiff's version of what happened at the Mahjong School in the afternoon of 3 April 1990. I find, on a balance of probabilities, that there had been previous occasions when the plaintiff and the defendant had shared in the buying of Mark Six tickets, that on that day, the defendant asked the plaintiff to do the same and gave the plaintiff $30 telling him to buy either computer quick-pick tickets or tickets of his own selection, that both the plaintiff and the defendant intended to share in the buying of Mark Six tickets leaving the plaintiff to make the decision, that the plaintiff then bought the four tickets in question and contributed $24 towards the total stake of $48 and that one of the tickets won the First and Third Prizes. It is true that the arrangement at the Mahjong School was rather informal, but it is also clear that both of them intended to share and acting on this arrangement, the plaintiff contributed his share and bought the tickets. I am satisfied that the plaintiff had an equal half share in the tickets including the winning ticket and is therefore entitled to share equally in the total winnings. I would give judgment for the plaintiff in the sum of $559,000.

[5-30] The arrangement between the plaintiff and defendant in *Wu Chiu Kuen* was certainly of a social nature. They were acquaintances who shared a semi-regular bet in a popular lottery competition. The plaintiff had, *prima facie*, a significant hurdle to surmount. The court started with the presumption that the social arrangement was not intended by the parties to be legally binding. The plaintiff was required to demonstrate that, on the balance

of probabilities, the social arrangement was intended to result in a legally binding contract. On the facts, the court was satisfied that the presumption should be set aside and that the parties had intended contractually enforceable relations to result from the arrangement. Once one accepts the facts as found by the court in *Wu Chiu Kuen*, it would seem that reasonable persons in the position of the parties would have intended their arrangements to create legally enforceable obligations.

[5-31] Most reasonable parties would regard a regular arrangement by which friends or acquaintances contributed funds for the purchase of a lottery ticket to result in a legal entitlement to a share of any winnings for the contributors. In *Simpkins v Pays*,[17] the plaintiff resided with the defendant as her boarder. The plaintiff, the defendant and the defendant's granddaughter entered a newspaper competition every week over a period of seven or eight weeks. The competition required entrants to make certain forecasts about fashions. The three of them contributed their own weekly forecast, and shared equally in the entrance fee and the postage, although the entry coupon always recorded the defendant's name. On one occasion, the parties' entry won a prize of £750 which was paid to the defendant. Her refusal to pay the plaintiff a one-third share of the winnings resulted in litigation. The defendant maintained, *inter alia*, that the arrangement between her and the plaintiff was social in nature and they did not intend to create contractual relations. Sellers J rejected the defendant's submission:[18]

> It may well be there are many family associations where some sort of rough and ready statement is made which would not, in a proper estimate of the circumstances, establish a contract which was contemplated to have legal consequences, but I do not so find here. I think that in the present case there was a mutuality in the arrangement between the parties. It was not very formal, but certainly it was, in effect, agreed that every week the forecast should go in in the name of the defendant, and that if there was success, no matter who won, all should share equally. It seems to be the implication from, or the interpretation of, what was said that this was in the nature of a very informal syndicate so that they should all get the benefit of success.

[5-32] The factor that was decisive in *Simpkins v Pays* was the 'mutuality' of the arrangement. This is a somewhat unusual way of describing it, but the word almost certainly refers to the fact that each party contributed consideration[19] in the form of an equal share of the entry fee and postage costs.

17 [1955] 3 All ER 10, [1955] 1 WLR 975.
18 [1955] 3 All ER 10 at 13.
19 Unger, 'Intention to Create Legal Relations, Mutuality and Consideration' (1956) 19 MLR 96 at 98.

5.4 Commercial Agreements

(a) Presumption in favour of intention

[5-33] In the case of agreements of a commercial nature a different presumption prevails. In the words of Ng J in *Lo Yuk Sui v Fubon Bank (HK) Ltd*:[20]

> The starting point is that parties reaching an express agreement of a commercial character are presumed to intend it to have legal effect, unless the contrary is shown. The onus of proving that there was no such intention is on the party who asserts that no legal effect is intended, and the onus is a heavy one. In deciding whether the onus has been discharged, the court will be influenced by the importance of the agreement to the parties, and by the fact that one of them acted in reliance on it.

[5-34] The presumption in favour of contractual intention in making commercial agreements is the opposite of that which applies in domestic or social agreements.

New World Development Co Ltd v Sun Hung Kai Securities Ltd

Court of Final Appeal
(2006) 9 HKCFAR 403; [2006] 3 HKLRD 345; [2006] HKCU 1122

For the facts, see para **[4-35]** above. SHKS defended by submitting, *inter alia*, that the oral agreement between the two managing directors was not intended to create contractual relations concerning such a major project. NWD was successful at trial, and SHKS's appeal to the Court of Appeal was dismissed. SHKS brought this final appeal.

Ribeiro PJ:

...

13. Mr Thomas [counsel for SHKS] endeavoured to argue that the evidence dictates a finding that in their dealings with each other in April 1990 and thereafter, the parties lacked any intention to bring a contract into existence but were 'merely talking about possible future business.' I cannot accept that contention.

14. Parties reaching an express agreement of a commercial character are presumed to intend it to have legal effect unless the contrary is shown: *Rose and Frank Company v J R Crompton & Bros Ltd*.[21] In such cases, assuming that the other requirements for constituting a contract are present, it is clear that 'the onus is on the party who asserts that no legal effect was intended, and the onus is a heavy one': *Edwards v Skyways Ltd*.[22] 'In deciding whether the onus has been discharged, the courts will be influenced by the importance of the agreement to the

20 [2016] 1 HKC 462, para 47 (HKCFI) (citing *New World Development Ltd v Sun Hung Kai Securities Ltd* (2006) 9 HKCFAR 403, [2006] 3 HKLRD 345, [2006] HKCU 1122 (HKCFA)).
21 [1923] 2 KB 261 at 288, [1924] All ER Rep 245 at 249.
22 [1964] 1 All ER 494 at 500, [1964] 1 WLR 349 at 355.

parties, and by the fact that one of them acted in reliance on it': *Chitty on Contracts*, 29th ed, (Sweet & Maxwell) §2–154; and see *Kingswood Estate Co v Anderson*.[23]

15. The Judge found that in April 1990 the parties entered into an express agreement which was obviously commercial in nature. Its terms were much in dispute at the trial. But the evidence … clearly shows that both sides acted throughout on the basis that their agreement had given rise to enforceable contractual obligations at the very least for SHKS to pay for and hence to acquire an interest in GUP shares. SHKS falls far short of discharging the heavy onus of showing that the parties lacked contractual intention, the evidence being all the other way.

Ribeiro PJ dismissed the appeal. The other members of the court (Bokhary PJ, Chan PJ, Mortimer NPJ and Sir Gerard Brennan NPJ) agreed with Ribeiro PJ's judgment.

[5-35] Indeed, the presumption in favour of intention in commercial agreements is so strong that it is rarely challenged.

(b) Rebuttal of presumption

Expressed negation of intention

[5-36] The presumption will be rebutted, however, where the commercial agreement states that it does not create legally binding obligations.

Rose and Frank Co v JR Crompton and Brothers Ltd

Court of Appeal (England and Wales)
[1923] 2 KB 261; [1924] All ER Rep 245; (1923) 14 Ll L Rep 519

Rose and Frank Company were a New York-based corporation which dealt in carbonizing paper. JR Crompton and Brothers Ltd ('Crompton') were an English company which manufactured carbonizing paper. The two parties and another English manufacturer entered into an agreement by which Rose and Frank would act as sole agent for Crompton and the other English manufacturer in the United States. The agreement was terminable on six months' notice. It also contained the following clause: *'This arrangement is not entered into, nor is this memorandum written, as a formal or legal agreement, and shall not be subject to legal jurisdiction in the law courts either in the United States or England, but it is only a definite expression and record of the purpose and intention of the three parties concerned to which they each honourably pledge themselves with the fullest confidence, based on past business with each other, that it will be carried through by each of the three parties with mutual loyalty and friendly co-operation.'* Crompton terminated the agreement without giving the prescribed notice, and Rose and Frank brought proceedings for breach of contract and non-delivery of ordered goods. Rose and Frank succeeded at trial, and Crompton appealed.

Atkin LJ:

… To create a contract there must be a common intention of the parties to enter into legal obligations, mutually communicated expressly or impliedly. Such an intention ordinarily will be inferred when parties enter into an agreement which in other

23 [1963] 2 QB 169 at 181, [1962] 3 All ER 593.

respects conforms to the rules of law as to the formation of contracts. It may be negatived impliedly by the nature of the agreed promise or promises, as in the case of offer and acceptance of hospitality, or of some agreements made in the course of family life between members of a family as in *Balfour v Balfour*.[24] If the intention may be negatived impliedly it may be negatived expressly. In this document, construed as a whole, I find myself driven to the conclusion that the clause in question expresses in clear terms the mutual intention of the parties not to enter into legal obligations in respect to the matters upon which they are recording their agreement. I have never seen such a clause before, but I see nothing necessarily absurd in business men seeking to regulate their business relations by mutual promises which fall short of legal obligations, and rest on obligations of either honour or self-interest, or perhaps both. In this agreement I consider the clause a dominant clause, and not to be rejected, as the learned judge thought, on the ground of repugnancy.

…

… In this case the defendants by the honourable understanding entered into the vague engagement contained in the document which had as a basis the average turnover for the last three years before the agreement. But whatever the terms of the agreement or understanding, it contemplated, as nearly all such agreements do, that the actual business done under it should be done by particular contracts of purchase and sale upon the terms of the general agreement so far as applicable. The actual business was done in this case, as in countless others, by orders for specific goods given by the 'agent' and accepted by the manufacturer or merchant. … [T]his is the common formula of acceptance in the business world which has been treated as acceptance in countless cases since merchants first wrote to one another. It would be understood as an acceptance passing between two merchants where there was no obligation at all on the part of the vendor to accept. Why it should bear a different meaning in a case where there is an honourable understanding by the merchant to accept up to some vague limit, I am unable to understand.

Atkin LJ allowed the appeal in relation to the claimed breach of the distribution agreement, but dismissed the appeal in relation to the non-supply of ordered goods. The other members of the court (Bankes LJ and Scrutton LJ) allowed the whole appeal. On further appeal to the House of Lords,[25] Atkin LJ's judgment was approved.

[5-37] The *Rose and Frank* court gave effect to the parties' express acknowledgement that the distribution agreement was not intended to be legally binding. The logic is impeccable; if contractual intention can be excluded by implication, it must also be excludable expressly. Atkin LJ nevertheless decided to uphold the contracts resulting from Rose and Frank's acceptance of Crompton's standing offer to sell, on the basis that these agreements were separate from the distribution agreement.

[5-38] Where the parties instead agree that their *legally binding* agreement is not subject to the jurisdiction of the courts, the term would be void as contrary to public policy which forbids depriving the courts of their jurisdiction to hear and determine disputes under a contract.[26]

24 [1919] 2 KB 571, [1918–1919] All ER 860, 88 LJKB 1054, 121 LT 346.
25 [1925] AC 445, [1924] All ER Rep 245.
26 See generally, *Hyman v Hyman* [1929] AC 601; *Re Wynn, Public Trustee of Newborough* [1952] Ch 271, [1952] 1 All ER 341.

Subject to contract

[5-39] The presumption in favour of contractual intention will also be rebutted where either party has stipulated in negotiations that a binding agreement is 'subject to contract', meaning that a formal contractual instrument must be prepared and executed. In the nineteenth century, Sir George Jessel MR said that 'where you have a proposal or agreement … expressed to be subject to a formal contract being prepared, it means what it says, it is subject to and dependent upon a formal contract being prepared'.[27] More recently in Hong Kong, Ribeiro PJ remarked that, '[b]y agreeing terms on a subject-to-contract basis, the parties agreed that they should each have the right to withdraw from the agreement unless and until an unconditional contract was executed'.[28]

[5-40] There is no magic in the phrase 'subject to contract'. Provided one or both negotiating parties have made it reasonably clear that a formal or written contractual instrument is required, that will suffice to suspend contractual intention until the instrument has been executed.

Union Insurance Society of Canton Ltd v The Hong Kong Land Co Ltd

High Court
[1977] HKLR 597, [1977] HKCU 71

Union Insurance Society of Canton Ltd ('Union Insurance') owned a property in Central Hong Kong known as the *Union Building*. In early October 1946 Union Insurance assigned the Crown lease to The Hong Kong Land Co Ltd ('HKL'), the assignment being registered on 9 October. There was no formal sale and purchase agreement. There was, however, a letter from HKL to Union Insurance dated 4 October 1946. In the letter, HKL promised that it would keep the name *Union Building* on the existing structure and apply it to any new building erected in its place. It also promised to lease space in the *Union Building* to Union Insurance. In the late 1950s, the site was redeveloped, during which time Union Insurance temporarily relocated its business premises. The *Union Building* was torn down and a new building erected in its place with the name *Union House*. Union Insurance moved into *Union House* when it was completed. In 1977, HKL changed the name of the building to *Swire House*. Union Insurance unsuccessfully objected to the change, and commenced legal proceedings. It claimed, *inter alia*, that HKL had breached its contractual obligation not to change the building's name.

Cons J:

…

… [T]he documents show that both companies intended and expected that an agreement would be drawn up. On the 4 October the Acting Secretary of the defendant wrote … 'I can confirm this company will be prepared to enter into a written agreement with the (plaintiff) on the following lines' and he then set out the matters I have already mentioned. … No particular document was ever drawn up by the solicitors nor were the matters in question included, as far as I know, in any of the documents that were subsequently made between the two companies. I am asked to deal with the matter informally, to accept that 'businessmen often record the most important agreements in crude and summary fashion' and to 'construe the documents fairly and broadly without being too astute or subtle in finding defects' so that 'the dealings of men may as far as possible be treated as effective, and that the law may not incur the reproach of being the destroyer of bargains': *Hillas & Co Ltd v Arcos Ltd*. I would be only too happy to do that, if I were satisfied that the companies had at any time come to an agreement. I appreciate that sometimes parties will make an agreement in a very informal way. And there may well be cases where it is difficult to decide whether they have in fact reached agreement or are still at the stage of negotiating. But I find no difficulty in this instance. Two well-established companies indicated intentions to incorporate certain ideas into a formal and future agreement. They did not do so. They were both legally advised, albeit by the same firm of solicitors. I am asked to say that in these circumstances they established binding legal obligations—and I observe in passing that this is the only effect of their conduct at the time that I am asked to deal with. On the documents before me I am not prepared to say they did. To my mind the documents point to only one conclusion, that for some reason no longer apparent, final agreement was never reached.

Judgment for defendant.

27 *Winn v Bull* (1877) 7 Ch D 29 at 32.

28 *Darton Ltd v Hong Kong Island Development Ltd* (2001) 4 HKCFAR 376, [2002] 1 HKLRD 145, [2001] HKCU 1183, para 13 (HKCFA).

[5-41] A stipulation by one or both of the parties that any agreement reached is subject to the conclusion of a formal contract will usually defeat contractual intention even where there has been substantial performance by one or both parties. The existence of such a stipulation was the principal reason preventing the creation of a promissory estoppel in *Attorney General of Hong Kong v Humphreys Estate (Queen's Garden) Ltd*,[29] notwithstanding very substantial performance of the anticipated agreement by both parties. In *World Food Fair Ltd v Hong Kong Island Development Ltd*[30] the Court of Final Appeal similarly held that, even if there had been fairly extensive performance of a settled commercial tenancy agreement, the fact that the parties had in their negotiations stipulated the arrangement to be 'subject to formal lease' meant that the agreement was not binding until the formal document had been executed.

[5-42] This is not to say that substantial performance is never relevant in a 'subject to contract' case. The parties may be taken to have waived the stipulated formality, including a 'subject to contract' formality, where; **(i)** all terms were agreed, **(ii)** those terms were varied without reiterating the stipulation, **(iii)** the agreement as varied has been substantially performed, and **(iv)** this results in an agreement by conduct which unequivocally waives the

29 [1986] HKC 592, [1987] 1 AC 114, [1987] 2 All ER 387, [1987] HKLR 427, [1987] 2 WLR 343 (PC on appeal from Hong Kong). See also the decision below in *Humphrey's Estate (Queen's Garden) Ltd v Attorney General* [1986] 4 HKLR 669, [1986] HKCU 332 (HKCA), per Fuad JA at 699–700 and Li VP at 712–713.

30 [2007] 1 HKC 387, (2006) 9 HKCFAR 735, [2007] 1 HKLRD 498 (HKCFA). See para **[4-38]** above.

Misrepresentation Ordinance (Cap 284)

4. Avoidance of provision excluding liability for misrepresentation

If a contract contains a term which would exclude or restrict—

(a) any liability to which a party to a contract may be subject by reason of any misrepresentation made by him before the contract was made; or

(b) any remedy available to another party to the contract by reason of such a misrepresentation, that term shall be of no effect except in so far as it satisfies the requirement of reasonableness as stated in section 3(1) of the Control of Exemption Clauses Ordinance (Cap 71); and it is for the person claiming that the term satisfies that requirement to show that it does.

[13-78] Thus, a contract term excluding or exempting liability or any remedy for misrepresentation must satisfy the same test of reasonableness that operates in section 3(1) of the CECO.[79]

79 Section 4, Misrepresentation Ordinance was briefly considered, in obiter, in *Cheng Kwok-Fai v Mok Yiu-Wah Peter* [1990] 2 HKLR 440, [1990] HKCU 395 (HKHC). Godfrey J reasoned that a 'complete agreement' clause, that also purported to 'withdraw' any representations that had been made, satisfied the s 4 reasonableness requirement because there had been no operative misrepresentation. The reasoning in *Cheng Kwok-Fai* is circular; if there was no misrepresentation, the effectiveness or otherwise of a clause effectively exempting liability for misrepresentation was irrelevant.

CHAPTER 14

Misrepresentation

14.1 Introduction to Misrepresentation

[14-1] During the course of negotiations but prior to the resulting contract's conclusion, things are frequently said or written which are intended to induce the other party to commit himself to an agreement. Sometimes those things are statements of fact or law which are not true.

[14-2] The classic example is a used car salesman who tells a customer that a car has been driven only a certain number of kilometres. The customer is impressed by the car's apparent low mileage and, in reliance on the salesman's statement, concludes a contract to buy the car. It turns out, however, that the salesman's statement of fact about the car's mileage was incorrect and the car has actually been driven a substantially longer distance than the salesman stated.

[14-3] The nature of the remedy, if any, available to the customer will depend on several factors. If the statement made by the salesman was a term of the contract, the customer will have an action for breach of contract involving a claim for damages.[1] The customer will also have a right to rescind for breach if the statement constituted a condition of the agreement.[2]

[14-4] Whether or not the statement was a contractual term,[3] the customer will also have a remedy for misrepresentation if the salesman's statement was a false representation of fact made with the intention of inducing the other party to conclude the contract and which did so induce the other party. Once it is established that the salesman's statement was an operative misrepresentation in this sense, an issue of the customer's remedies arises. The nature of the remedies available for misrepresentation will depend on whether the salesman's misrepresentation was fraudulent, negligent, or innocent.[4]

1 See Chapter 21.

2 See Section 11.2.

3 On whether a pre-contractual statement is to be regarded as a term of the contract or a mere (mis)representation, see Section 9.5.

4 The term 'innocent misrepresentation' has two meanings, and attention to context is necessary in order to determine, in any particular instance, what is meant. It can mean either: (1) any misrepresentation that is not fraudulent (including negligent misrepresentation); or

[14-5] It should be noted, however, that a 'representation is not like a warranty; it is not necessary that it should be strictly construed or strictly complied with; it is enough if it is substantially true; it is enough if it is substantially complied with'.[5]

14.2 Elements of Misrepresentation

(a) *False statement of fact—opinion, forecast and future intention*

[14-6] A statement cannot constitute a misrepresentation unless it was a false statement of past or present fact or, perhaps, of law. A statement is to be understood in the same sense that a reasonable person in the position of the representee would have understood it, having regard to the words employed and the context in which they were uttered.[6]

[14-7] If the statement expressed merely a mistaken opinion or forecast, it will usually not be a misrepresentation.

Bisset v Wilkinson

Privy Council
[1927] AC 177; [1926] All ER Rep 343; 42 TLR 727

Bisset owned a farm in New Zealand, which he contracted to sell to Wilkinson. The purchase price was more than £13,000, with £2,000 immediately payable and the balance payable five years later (with interest payable periodically in the meantime). During the course of pre-contractual negotiations, Bisset expressed the view that the farm could support 2,000 sheep if worked properly. Wilkinson knew that Bisset had not operated the land as a sheep farm, although he kept some sheep on it. Bisset admitted that he was aware Wilkinson was buying the land in the belief that it would support 2,000 sheep if properly worked. Wilkinson made the initial payment and entered into possession. It soon became apparent, however, that the farm could not support anything near 2,000 sheep. Bisset brought proceedings claiming payments due to him under the agreement, and Wilkinson defended and counter-claimed on the basis that the contract had been rescinded as a result of Bisset's misrepresentation. Bisset succeeded at trial, but lost on appeal. He brought this further appeal to the Privy Council.

(2) any misrepresentation that is *wholly* innocent in the sense that it is tainted neither by fraud nor negligence.

5 *With v O'Flanagan* [1936] Ch 575 at 581, [1936] 1 All ER 727 at 732, per Lord Wright MR; see also, *Avon Insurance plc v Swire Fraser Ltd* [2000] 1 All ER (Comm) 573, para 17: 'a representation may be true without being entirely correct, provided it is substantially correct and the difference between what is represented and what is actually correct would not have been likely to induce a reasonable person in the position of the claimants to enter into the contracts'.

6 *IFE Fund SA v Goldman Sachs International* [2006] EWHC 2887 (Comm), [2007] 1 Lloyd's Rep 264, para 50 (affirmed [2007] EWCA Civ 811, [2007] 2 Lloyd's Rep 449).

Lord Merrivale:

...

In an action for rescission, as in an action for specific performance of an executory contract, when misrepresentation is the alleged ground of relief of the party who repudiates the contract, it is, of course, essential to ascertain whether that which is relied on is a representation of a specific fact, or a statement of opinion, since an erroneous opinion stated by the party affirming the contract, though it may have been relied on and have induced the contract on the part of the party who seeks rescission, gives no title to relief unless fraud is established. The application of this rule, however, is not always easy, as is illustrated in a good many reported cases, as well as in this. A representation of fact may be inherent in a statement of opinion and, at any rate, the existence of the opinion in the person stating it is a question of fact. ...

In the present case ... the material facts of the transaction, the knowledge of the parties respectively, and their relative positions, the words of representation used, and the actual condition of the subject-matter spoken of, are relevant to the two inquiries necessary to be made. What was the meaning of the representation? Was it true?

In ascertaining what meaning was conveyed to the minds of the purchasers by the vendor's statement as to the 2,000 sheep, the most material fact to be remembered is that, as both parties were aware, the vendor had not and, so far as appears, no other person had, at any time carried on sheep-farming upon the unit of land in question. That land as a distinct holding had never constituted a sheep-farm. ... As was said by Sim J [at first instance]:

> In ordinary circumstances, any statement made by an owner who has been occupying his own farm as to its carrying capacity would be regarded as a statement of fact ... This, however, is not such a case. The purchasers knew all about [Bisset's farm] and knew also what sheep the farm was carrying when they inspected it. In these circumstances ... the purchasers were not justified in regarding anything said by the vendor as to the carrying capacity as being anything more than an expression of his opinion on the subject.

In this view of the matter their Lordships concur.

Whether the vendor honestly and in fact held the opinion which he stated remained to be considered. This involved examination of the history and condition of the property. If a reasonable man with the vendor's knowledge could not have come to the conclusion he stated, the description of that conclusion as an opinion would not necessarily protect him against rescission for misrepresentation, but what was actually the capacity in competent hands of the land the purchasers purchased had never been, and never was, practically ascertained. ...

[Bisset had been found at trial to be expressing a view he honestly held, and the Board saw no reason to overturn that assessment] ...

Their Lordships will humbly advise His Majesty that the appeal should be allowed, and the judgment of Sim J restored. ...

Lord Merrivale spoke for the Board, the other members of which were Viscount Dunedin, Lord Atkinson, Lord Phillimore, and Lord Carson.

[14-8] It was not reasonable for Wilkinson to rely on Bisset's expressed opinion because of the 'relative positions' of the parties. Bisset had no special knowledge, skill or experience in farming sheep, and Wilkinson was aware of

that limitation. Therefore, Bisset's expressed view that the farm could support 2,000 sheep if properly worked was reasonably understood by Wilkinson as a mere opinion and not as a statement of fact.

Special knowledge

[14-9] Sometimes a statement will be expressed in the form of an opinion, but it will be made in circumstances in which a reasonable person would nevertheless regard it as a statement of fact. Indeed, as Lord Merrivale observed in *Bisset*, a 'representation of fact may be inherent in a statement of opinion'.[7] This will be much more likely where the representor possesses greater knowledge in relation to the subject-matter of the opinion than the representee. In *Smith v Land and House Property Corporation*,[8] the purchaser of a property was entitled to rescind the contract of sale where the vendor had told him that it was let to 'a most desirable tenant' when the vendor knew that the rent was in arrears. According to Bowen LJ, 'if the facts are not equally known to both sides, then a statement of opinion by the one who knows the facts best involves very often a statement of a material fact, for he impliedly states that he knows facts which justify his opinion'.[9]

Special expertise or skill

[14-10] Similarly, an expression of opinion or forecast may amount to a statement of fact where the representor possesses greater expertise or skill than the representee.

Esso Petroleum Co Ltd v Mardon

Court of Appeal (England and Wales)
[1976] QB 801; [1976] 2 All ER 5; [1976] 2 WLR 583

Mardon negotiated a tenancy agreement with Esso Petroleum Co Ltd ('Esso') who required a tenant to operate a petrol station to be built on a new site. Esso told Mardon that they had calculated the new station would see a throughput of 200,000 gallons of petrol per annum by the third year of operation. Mardon was initially skeptical, but his doubts were allayed by Esso's vast experience in such matters. The tenancy agreement was concluded for a period of three years commencing in April 1963, but in spite of Mardon's best efforts he was able to generate a throughput of substantially less than half of Esso's forecast. After discussions with Mardon, Esso agreed to a new lease at a lower rent in September 1964. The business continued, however, to lose money and Mardon found himself unable to pay Esso for rent and petrol supplies. Finally, in December 1966, Esso brought proceedings against Mardon for possession of the premises, monies owed and mesne profits. Mardon counter-claimed for damages for breach of a collateral warranty as to the throughput, or alternatively for negligent misrepresentation as to the throughput.

7 *Bisset v Wilkinson* [1927] AC 177 at 182, [1926] All ER Rep 343 at 346.
8 (1884) 28 Ch D 7.
9 Ibid, at 15.

Lord Denning MR:

...

... It seems to me that *Hedley Byrne & Co Ltd v Heller & Partners Ltd*,[10] properly understood, covers this particular proposition: if a man, who has or professes to have special knowledge or skill, makes a representation by virtue thereof to another—be it advice, information or opinion—with the intention of inducing him to enter into a contract with him, he is under a duty to use reasonable care to see that the representation is correct, and that the advice, information or opinion is reliable. If he negligently gives unsound advice or misleading information or expresses an erroneous opinion, and thereby induces the other side to enter into a contract with him, he is liable in damages. This proposition is in line with what I said in *Candler v Crane, Christmas & Co*,[11] which was approved by the majority of the Privy Council in *Mutual Life and Citizens' Assurance Co Ltd v Evatt*[12] ...

Applying this principle, it is plain that Esso professed to have—and did in fact have—special knowledge or skill in estimating the throughput of a filling station. They made the representation—they forecast a throughput of 200,000 gallons—intending to induce Mr Mardon to enter into a tenancy on the faith of it. They made it negligently. It was a 'fatal error' and thereby induced Mr Mardon to enter into a contract of tenancy that was disastrous to him. For this misrepresentation they are liable in damages.

Cumrod and Shaw LJJ agreed that the counter-claim based on negligent misrepresentation should succeed.

[14-11] Esso's representation was in the form of a forecast or opinion. This would normally have precluded it from constituting an operative misrepresentation. However, Esso's high level of expertise or skill in the statement's subject matter as compared to the representee's relative lack of experience or skill meant that a reasonable person in the position of the representee was justified in regarding the representation as a statement of fact. Esso's failure to take reasonable care in the formulation of its opinion or forecast therefore exposed it to a successful counter-claim for negligent misrepresentation.

Similarly, in *Ko Ching Fung v Fulltin Investment Ltd*,[13] the plaintiff planned to open a Japanese restaurant at certain premises in Happy Valley. The defendant was the landlord of the premises. Upon enquiry by the plaintiff, the defendant's managing director said that the premises were suitable for the operation of a Japanese restaurant. This statement was untrue because the premises did not comply with regulations under the Building Ordinance (Cap 123), although the defendant was unaware of this legal obstacle and the premises were already leased for use as a Thai restaurant. In an action to recover $284,000 in deposits paid under a provisional tenancy agreement and citing *Esso Petroleum*, the Hong Kong Court of Appeal found for the plaintiff on the basis that the managing director's statement was a misrepresentation

10 [1964] AC 465, [1963] 2 All ER 575.
11 [1951] 2 KB 164 at 179–180, [1951] 1 All ER 426 at 433, 434.
12 [1971] AC 793, [1971] 1 All ER 150.
13 [2007] HKCU 1182 (unreported, CACV 337/2006, 13 July 2007) (HKCA).

because he had relied on 'his own experience and professional qualification as a real estate administrator'.[14]

Future intentions

[14-12] A statement by a person as to his future intentions is also not usually to be regarded as a false statement of existing fact. There is, however, an important exception to this. Where the opinion is not actually held, the forecast is not actually believed in, or the declared future conduct is not actually intended at the time of the representation, the representation will be a false statement of existing fact. The existing fact is the true state of the representor's mind at the time of the representation. If the representor states that he has an opinion that he does not really possess, or that he has confidence in a forecast in which he does not really believe, or that he intends a future course of action which he actually believes he will not pursue, he is saying something he knows to be untrue about his current set of beliefs.

[14-13] In *Edgington v Fitzmaurice*,[15] the defendants were directors of a company that needed to raise money in order to pay off a number of pressing debts. They sent a prospectus for an issue of debentures to the plaintiff. The prospectus stated that the funds raised would be used to effect improvements to the company's buildings and to purchase needed capital equipment, and to further develop the company's ability to transport goods in which it traded. On the faith of the prospectus the plaintiff purchased £1,500 worth of debentures, the proceeds of which the plaintiffs used to pay some of the company's debts. Subsequently, the company was wound up and the plaintiff was not repaid. He brought proceedings against the defendants claiming damages for fraudulent misrepresentation (the tort of deceit) on the basis of false statements contained in the prospectus. The defendants argued that there was no misrepresentation because the prospectus contained no false statement of fact, but merely a statement of future intention. The English Court of Appeal found for the plaintiff on the basis that the defendants intended, at the time they provided the prospectus to the plaintiff, to use the funds for purposes other than those disclosed in the prospectus. In a celebrated passage, Bowen LJ observed:[16]

> There must be a misstatement of existing fact: but the state of a man's mind is as much a fact as the state of his digestion. It is true that it is very difficult to prove what the state of a man's mind at a particular time is, but, if it can be ascertained, it is as much a fact as anything else. A misrepresentation as to the state of a man's mind is, therefore, a misstatement of fact.

14 The court also found that the managing director's statement was a term of the contract.
15 (1885) 29 Ch D 459, [1881–1885] All ER Rep 856.
16 (1885) 29 Ch D 459 at 483, [1881–1885] All ER Rep 856 at 861G.

[14-14] The same principle can be seen at work in *Chiu Wai Shing v Lau Chi Wai*.[17] Lau and his wife were a couple of limited means and education who owned and lived in a small flat in Sheung Shui which they had purchased from the Housing Authority. Fu was the *de facto* husband of Lau's sister-in-law, and owed debts to Chiu amounting to some $700,000. In order to settle these debts, Chiu and Fu came to an arrangement: Lau and his wife would sell their flat to Chiu for $900,000, of which $700,000 would be paid by Chiu forbearing repayment of Fu's debts. The other $200,000 would be paid by Chiu to Lau and his wife so that they could pay the premium which would be payable to the Housing Authority for transferring the property to Chiu; but Lau and his wife would be expected to repay the $200,000 to Chiu. Fu procured his de facto wife (Lau's sister-in-law) to persuade her sister and Lau to sign the agreement selling their flat to Chiu. The couple were very reluctant to execute the agreement and part with the title deeds, but the sister-in-law (acting as Chiu's agent) persuaded them to do so by saying that these steps were a mere formality in order to secure Fu's loans and that there was no danger to Lau and his wife in terms of the ownership of their flat being placed at risk. When Chiu subsequently demanded completion of the sale and purchase agreement, Lau and his wife refused. Chiu then brought proceedings in the Court of First Instance for specific performance against Lau and his wife. The claim was rejected primarily on grounds of lack of consideration. Recognising the possibility that there might indeed be consideration for Lau's promise to sell, Stone J also rested his judgment on the alternative ground of misrepresentation; Chiu's statement that execution of the sale and purchase agreement was a mere formality that did not threaten Lau's ownership of the flat was an untrue statement of fact, as it was always Chiu's intention to take ownership of the flat for himself. Because the untrue statement of fact was intended to induce, and did induce, Lau and his wife to conclude the sale and purchase agreement, it constituted an operative misrepresentation justifying rescission of the contract.

(b) False statement of law

[14-15] Sometimes, a false statement made during the course of contractual negotiations will be one of law, rather than fact. The traditional view at common law was that, subject to a number of ramified exceptions and qualifications, misrepresentations of law gave no right to rescission or damages.[18]

[14-16] In 1998, the House of Lords decided to remove the bar preventing restitution of monies paid under a mistake of law (payments were made pursuant to certain arrangements that were void as being beyond the powers

17 [2006] HKCU 1825 (unreported, HCA 3013/2002, 1 November 2006) (HKCFI).
18 *Beattie v Lord Ebury* (1871-1872) LR 7 Ch App 777 (putative misrepresentation as to powers of company directors).

of a public authority).[19] Some six years later, the English Court of Appeal expressed the view that the House of Lords decision 'now permeates the law of contract'.[20]

[14-17] The traditional view against misrepresentations of law has now probably also been displaced so that an incorrect statement of law can operate to taint a contract with misrepresentation. A representor might, for instance, state that land he is offering for sale is subject only to a licence agreement terminable on three months' notice when it is actually subject to a lease terminable on six months' notice. Such were the facts in *Pankhania v Hackney London Borough Council*, in which the court decided that the resulting contract of sale was tainted by misrepresentation and remarked:[21]

> The distinction between fact and law in the context of relief from misrepresentation has no more underlying principle to it than it does in the context of relief from mistake. Indeed, when the principles of mistake and misrepresentation are set side by side, there is a stronger case for granting relief against a party who has induced a mistaken belief as to law in another, than against one who has merely made the same mistake himself. The rules of the common law should, so far as possible, be congruent with one another, and based on coherent principle. The survival of the 'misrepresentation of law' rule following the demise of the 'mistake of law' rule would be no more than a quixotic anachronism.

[14-18] Although some caution is needed before finally concluding that there is no longer a barrier precluding pre-contractual misrepresentations of law, it seems likely that *Pankhania* will be followed in both England[22] and Hong Kong. In any event, a wilful misstatement of law will almost certainly amount to a misrepresentation.[23]

(c) Misrepresentation by conduct

[14-19] A misrepresentation may, in appropriate circumstances, be constituted by conduct as well as by words. In *Walters v Morgan*, Lord Campbell LC put it this way:[24]

> Simple reticence does not amount to legal fraud, however it may be viewed by moralists. But a single word, or … a nod or a wink, or a shake of the head, or a smile from the purchaser intended to induce the vendor to believe the existence of a non-existing fact,

19 *Kleinwort Benson Ltd v Lincoln City Council* [1999] 2 AC 349, [1998] 4 All ER 513, [1998] 3 WLR 1095.

20 *Brennan v Bolt Burdon* [2004] EWCA Civ 1017, [2005] QB 303, [2004] All ER (D) 551 (Jul), [2004] 3 WLR 1321, para 10 (Maurice Kay LJ, Sedley LJ and Bodey J sharing this view).

21 [2002] EWHC 2441, [2002] All ER (D) 22 (Aug), para 57 (Rex Tedd QC).

22 Eg, Edwin Peel, *Treitel: The Law of Contract*, 14th edn (Sweet & Maxwell, 2015) p 410.

23 *Oudaille v Lawson* [1922] NZLR 259 (wilfully false statement that rent could not be increased on premises from which business was conducted).

24 (1861) 3 De Gex, Fisher & Jones 718 at 724, 45 ER 1056.

> which might influence the price of the subject to be sold would be sufficient ground for a Court of Equity to refuse a decree for a specific performance of the agreement.

[14-20] In *Shum Kong v Chui Ting Lin Teresa*,[25] Shum and an estate agent showed Chui a village house in Sai Kung belonging to Shum, as well as an adjacent garage and surrounding garden. The garage and garden were not part of the same property as the house and were not for sale, but Chui formed the impression that they were part of the sale and concluded a sale and purchase agreement on that basis. Chui rescinded the agreement for misrepresentation upon discovering the truth. Shum sued for breach of contract, denying any misrepresentation. In finding that Chui's counterclaim based on misrepresentation was made out, Deputy Judge Muttrie said:[26]

> Here by showing him the property without telling him that it comprised the house only, both Mrs Shum and Mr Mok [the estate agent] made a misrepresentation by conduct. From merely looking at the property it was entirely reasonable for Mr Chui to conclude at both inspections that what was being offered to him, and what he was paying a deposit for, was the house, garden and garage beneath. In my view it was reasonable to conclude this from the viewing alone. The various oral representations merely served to reinforce the impression given by the sight of the property itself.

[14-21] In deciding whether conduct by the representor constitutes a misrepresentation, context is critically important. It was the context in *Shum Kong* which caused a reasonable person in the defendant's position to conclude that the estate agent's conduct amounted to a misrepresentation that the garage and garden were included in the property for sale.

[14-22] An illustrative contrast is provided by *Bank of China (Hong Kong) Ltd v Leung Wai Man*.[27] The defendant executed a legal charge of unlimited liability over his residential property as security for a loan made by a bank to a third party. When the bank sought to enforce the legal charge, the defendant argued that an employee of the bank had misrepresented the terms of the charge. There was evidence that, at a dinner meeting to discuss the arrangements prior to execution, the defendant told the employee that his financial capacity was not good and the most he could afford would be liability for $1 million. The employee's response to this, according to the same evidence, was to smile and nod his head. The defendant's evidence was that he interpreted this conduct to mean that the charge would be limited. Carlye Chu J decided that even if this evidence were true, it could not establish a misrepresentation: 'The Court cannot infer the mere smiling and nodding by [the employee] to mean that he

25 [2001] HKCU 531 (unreported, HCA16227/1999, 6 June 2001) (HKCFI).

26 Ibid at 24.

27 [2011] 4 HKLRD 693, [2011] HKCU 2537 (HKCFI).

was agreeable to what the … defendant had said, nor can the Court regard it as an implied representation'.[28]

Dishonest intention not required

[14-23] In determining whether there has been a misrepresentation by conduct, as with parol misrepresentation, it is not necessary to establish that the representor intended to mislead the representee. It is enough that the representation by conduct was, in all the circumstances, objectively misleading as to a fact which induced the representee to conclude the contract.

Green Park Properties Ltd v Dorku Ltd

Court of Appeal
[2000] 4 HKC 538; [2001] 1 HKLRD 139

Dorku Ltd owned two adjacent ground-floor shops in Nathan Road, Kowloon which had been placed on the market for sale. A real estate agent twice showed the properties to a representative of Green Park Properties Ltd ('Green Park'), which was interested in buying. The shops were both currently tenanted, and Green Park knew that any sale would be subject to the tenancies. Upon inspection, the estate agent showed Green Park a walled yard at the back which gave access to a rear lane. After Green Park expressed concern about the position of some columns inside the building, the agent also showed Green Park a copy of the tenancy plan which indicated that the walled yard was part of the larger of the two shops for sale (Portion A on the tenancy plan). Green Park concluded a sale and purchase agreement with Dorku under which Green Park agreed to pay a purchase price of $54m, including a deposit of $10.8m. After conclusion of the agreement and payment of the deposit, Green Park discovered that the walled yard was part of the building's common area and that it was not included in the sale. Green Park commenced proceedings claiming, inter alia, a return of its deposit because of rescission for misrepresentation.

Le Pichon JA:

…

Misrepresentation

Counsel for the vendor submitted that an agent showing premises does not thereby make any representation as to rights over particular parts of the land. No one raised any questions at the two inspections as to whether the yard was part of the property. The general rule of caveat emptor applied and the vendor was under no obligation to disclose the fact that the yard was not part of the property to be sold. Mr Mok [counsel for Dorku] submitted that to hold a person guilty of misrepresentation by conduct, there had to be an intention on the part of the representor to induce the other party to believe in a certain state of facts. As the agent was not himself aware of the fact that the property did not include the yard when he took the purchaser to inspect the property, the relevant intention was not present. The passage in *Chitty on Contracts* at para 6–014 to which Mr Mok referred reads:

28 Ibid at 720; A more fundamental problem with the defendant's submission was that, even if the bank employee's conduct could be reasonably interpreted as agreement with the defendant's request to limit the extent of his liability under the legal charge, it did not constitute a statement of past or present fact.

> … conduct may be intended to convey information in precisely the same way as the written or spoken word. Thus a person who goes into a shop in a university town wearing cap and gown may (if such costume is still customary) be representing that he is an undergraduate, a person who sits down in a restaurant and orders a meal impliedly represents that he has the means to pay, and more generally it has been said in a well-known dictum that 'a nod or a wink or a shake of the head or a smile' may amount to a representation if it is *intended* to induce the other party to believe in a certain state of facts. (Emphasis added.)

I do not read that passage as requiring any subjective intent on the part of the representor when making the representation. In my judgment, an objective test is to be applied in ascertaining whether or not, having regard to the conduct in question, there was a representation. See also *Chitty on Contracts* at para 6–042.

In the present case, the purchaser was taken to view the property. The purpose was plainly to show the purchaser what was for sale. Portion A had previously been used as a restaurant and was being renovated. Work was being carried out at the time. During the inspection, the parties went into the yard which, though open in the sense of not having a roof, was enclosed by a wall. In order to gain access to the toilets at the rear, one had to go through the swing doors into the yard. The natural boundary of the property was the end wall with the metal doors which separated the property from the lane. Given the physical characteristics and layout of the property, the overall impression conveyed was that the property included the yard. When asked why he thought the yard was included as part of the property to be sold, Mr Leong [who represented Green Park at the inspections] replied:

> First, at the time when I went to view the property as let by the agent I passed by the backyard, and I saw that the door in the backyard leading out to the scavenger lane was closed. Entry into the backyard could only be gained from the shop premises but not from other places, so when I was looking at it so it was in my mind that that certainly formed part of the shop premises. I would think that anyone who went there to see would not suspect that that was not part of the shop premises.

The Judge was justified in concluding that there was a representation by conduct that the yard was part of the property to be sold. Turning now to the tenancy plan, as the Judge observed, it showed the outline of the property and the area occupied by portion A. Portion A was shaded and the shaded part extended to the boundary with the lane. The Judge came to the view that 'the tenancy plan clearly gave the impression that the yard, which was located at the back of the property, was included in the property as well.'

The contention was that even if there was a misrepresentation, it did not matter because it was not operative on the purchaser's mind. Mr Leong's concern at the time was with the position of the columns. …

… What was operative on the mind of Mr Leong was the shape of the property as depicted on the tenancy plan. Since the back of the property was represented by a straight line that coincided with his visual inspection … it is hardly surprising that there was no reason for him to pay special attention to the yard.

In my view, the Judge was correct in finding that there was misrepresentation by conduct which was actionable. …

Rogers VP and Stock JA agreed with Le Pichon JA.[29]

29 An appeal to the Court of Final Appeal was dismissed on other grounds, after deciding that there was no basis for interfering with the Court of Appeal's findings on misrepresentation: *Green Park Properties Ltd v Dorku Ltd* [2002] 1 HKC 121, (2001) 4 HKCFAR 448, [2001] 3 HKLRD 760, para 25 (HKCFA).

[14-24] In showing Green Park the walled yard at the same time that it was being given an inspection of the property for sale, Dorku's agent created the reasonable impression that the yard was included in the sale. Because the yard was not included in Dorku's title, it could not pass title over that portion of the property to Green Park. That Dorku's agent did not, in showing the yard, intend to induce any belief as to a state of facts in Green Park's mind was irrelevant. The impression objectively and reasonably created by Dorku's conduct was factually false, and therefore capable of constituting a misrepresentation notwithstanding that Dorku's agents never expressly asserted title over the yard.

Concealment

[14-25] An attempt to conceal a defect can also constitute a misrepresentation by conduct. If made with the intention to mislead, the misrepresentation by concealment will be fraudulent. In *Schneider v Heath*,[30] the vendor of a vessel removed it from a dry dock and kept it afloat until the sale was concluded thereby preventing potential buyers from discovering that the keel was broken and the hull was worm-eaten. The purchaser, upon discovering the truth as to the vessel's condition, was successful in a claim to have his deposit refunded: 'it appears here that means were taken fraudulently to conceal the defect in the ship's bottom'.[31] Similarly, in *Gordon v Selico Ltd*,[32] the vendors of a flat were found to have made a misrepresentation when, prior to putting it on the market, they covered up dry rot.

(d) Misrepresentation by silence

[14-26] Generally speaking, the common law places no obligation on negotiating parties to disclose facts material to the proposed contract. Parties are not allowed to make a statement of fact which is false, but they are entitled to remain silent. This is a reflection of the common law's position that there is no general doctrine of good faith in contract.

Contracts *uberrimae fidei*

[14-27] A notable exception to this principle is that parties may be under a positive obligation to disclose material facts where they are negotiating contracts *uberrimae fidei* ('of utmost faith'). The main example of this class of contract is contracts of insurance. The insured must disclose such facts, known

30 (1813) 3 Campbell 506, 170 ER 1462.

31 (1813) 3 Campbell 506 at 509, per Mansfield CJ. Semble, *Gordon v Selico Ltd* [1986] 1 EGLR 71 in which the vendors of a flat were found to have made a misrepresentation when, prior to putting it on the market, they covered up dry rot.

32 [1986] 1 EGLR 71.

to him but not the insurer, as a reasonable insurer would regard as material to a decision to conclude the particular insurance contract; it is not enough that the insured honestly believed that the information was not material.[33] Another class of contracts which involve a duty to disclose relevant facts are contracts where one party stands in a fiduciary relationship to the other, eg lawyer and client, medical practitioner and patient, guardian and ward, priest and confessor: The party in whom trust and confidence is reposed may be subject to a duty of disclosure of relevant facts, and silence about such facts may constitute misrepresentation.

Changed circumstances

[14-28] An issue of misrepresentation by silence will also arise where a party makes a statement of fact about a continuing state of affairs intended to induce the representee to conclude the contract, but before the contract is concluded circumstances change rendering the statement untrue. The representor is under an obligation to correct the earlier statement if he is aware of the changed circumstances.

With v O'Flanagan

Court of Appeal (England and Wales)
[1936] Ch 575; [1936] 1 All ER 727

O'Flanagan was a medical practitioner who wished to sell his practice. In January 1934 O'Flanagan's agent told With, who was interested in purchasing the practice, that it was bringing in £2,000 per annum. This was a substantially true representation in so far as it related to the previous two-year period. In April, With learned that the practice was being managed by a locum in O'Flanagan's absence, but O'Flanagan's solicitors assured him that the practice was in good hands. On 1 May, With concluded an agreement to buy the practice for £4,000. He took possession that evening, and discovered that the practice's income for the preceding three weeks had been only £15, of which £10 had come from a single patient. No patients at all arrived the next day. With also learned that O'Flanagan had been away from the practice since January because of illness, and that it had in the meantime been managed by a number of different locums. On 4 May, With issued a writ seeking rescission of the agreement on grounds of misrepresentation and return of his purchase money. O'Flanagan took the point that there had been no misrepresentation; the statement about the practice's income was substantially true at the time it was made, and silence cannot constitute a misrepresentation. O'Flanagan succeeded at trial, and With appealed.

Lord Wright MR:

...

33 *The United Insurance Co Ltd v Chan Park Sang* [1960] 3 HKLR 267, [1960] HKCU 52 (HKSC); *Lai Chui Kar Poa Helen v American International Assurance Co (Bermuda) Ltd* [1985] 2 HKC 689 (HKHC); *Lam Charn Yung v AXA China Region Insurance Co (Bermuda) Ltd* [2007] 1 HKLRD 770, [2007] HKCU 355 (HKDC).

… I think that the change in circumstances ought to have been communicated to the plaintiffs before they were allowed to close the transaction. Instead of that, they were thrown off the scent and induced not to pursue, and did not pursue, their doubts any further. That is not in a sense essential; the essential and material representation remained unqualified and uncontradicted and in truth it was acted upon eventually when the bargain was concluded on 1 May. …

… A representation is not like a warranty; it is not necessary it should be strictly construed or strictly complied with; it is enough if it is substantially true; it is enough if it is substantially complied with. If it is not substantially complied with then the Court finds itself in the range of misrepresentation and must give effect to that position if it is satisfied that the plaintiffs acted upon the representation in concluding a bargain, about which there can be no doubt in this case. …

…

… a representation made as a matter of inducement to enter into a contract is to be treated as a continuing representation. That view of the position was put in *Smith v Kay*[34] by Lord Cranworth. He says of a representation made in negotiation some time before the date of a contract:

> It is a continuing representation. The representation does not end for ever when the representation is once made; it continues on. The pleader who drew the bill, or the young man himself, in stating his case, would say, Before I executed the bond I had been led to believe, and I therefore continued to believe, that it was executed pursuant to the arrangement.

The underlying principle is also stated again in a slightly different application by Lord Blackburn in *Brownlie v Campbell*.[35] I need only quote a very short passage. Lord Blackburn says:

> [W]hen a statement or representation has been made in the *bona fide* belief that it is true, and the party who has made it afterwards comes to find out that it is untrue and discovers what he should have said, he can no longer honestly keep up that silence on the subject after that has come to his knowledge, thereby allowing the other party to go on, and still more, inducing him to go on, upon a statement which was honestly made at the time when it was made, but which he has not now retracted when he has become aware that it can be no longer honestly persevered in.

The learned Lord goes on to say that would be fraud, though nowadays the Court is more reluctant to use the word 'fraud' and would not generally use the word 'fraud' in that connection because the failure to disclose, though wrong and a breach of duty, may be due to inadvertence or a failure to realize that the duty rests upon the party who has made the representation not to leave the other party under an error when the representation has become falsified by a change of circumstances. This question only occurs when there is an interval of time between the time when the representation is made and when it is acted upon by the party to whom it was made, who either concludes the contract or does some similar decisive act; but the representation remains in effect and it is because that is so, and because the Court is satisfied in a proper case on the facts that it remained operative in the mind of the representee, that the Court holds that under such circumstances the representee should not be bound.

…

34 (1859) 7 HLC 750 at 769.
35 (1880) 5 App Cas 925 at 950.

On these grounds, with great respect to the learned judge, I think he ought to have come to the conclusion that the plaintiffs have established their case and there ought to be a declaration rescinding the contract with the consequences which follow upon such a declaration.

Romer LJ:

I agree. The only principle invoked by the appellants in this case is as follows. If A. with a view to inducing B. to enter into a contract makes a representation as to a material fact, then if at a later date and before the contract is actually entered into, owing to a change of circumstances, the representation then made would to the knowledge of A. be untrue and B. subsequently enters into the contract in ignorance of that change of circumstances and relying upon that representation, A. cannot hold B. to the bargain. There is ample authority for that statement and, indeed, I doubt myself whether any authority is necessary, it being, it seems to me, so obviously consistent with the plainest principles of equity.

…

… it appears to me that the plaintiffs are entitled to succeed in the action and that this appeal should be allowed.

Clauson J agreed with Lord Wright MR and Romer LJ.

[14-29] Thus, a representation made with the intention of inducing the representee to conclude a contract is a thing with an ongoing existence; it lives beyond the moment it is uttered and continues to function until it is withdrawn or altered by the representor.

[14-30] The impact of misrepresentation by silence is ameliorated by Lord Wright MR's observation in *With* that a representation 'is not like a warranty' and does not stand to be construed in the same manner as a contractual term. Whereas strict compliance with a contractual term is generally required, it is enough if a representation is 'substantially true'. It follows that a less than substantial inaccuracy in a representation, whether present at the time it was uttered or produced by a subsequent change of circumstances, would not operate to transform that representation into a misrepresentation. The obligation to correct an earlier representation does not, however, arise unless the changed circumstances defeat the continuing accuracy of an earlier pre-contractual representation that was made.

Half-truths

[14-31] Sometimes a statement of fact will be incomplete, ie it represents only a part of the truth that a reasonable person in the position of the representee would consider relevant in deciding whether to conclude a contract. Such a statement is sometimes referred to as a 'half-truth'. Subject to the exception relating to contracts *uberrimae fidei*, a half-truth can constitute a misrepresentation only if it gives an objectively misleading impression that falsifies stated facts. In *Peek v Gurney*, Lord Cairns said: 'There must, in my opinion, be some active misstatement of fact, or, at all events, such a partial

and fragmentary statement of fact that the withholding of that which is not stated makes that which is stated absolutely false.'[36] That a half-truth does not amount to a misrepresentation unless it falsifies a stated fact has been more recently affirmed in Hong Kong.

Aktieselskabet Dansk Skibsfinansiering v Brothers

Court of Final Appeal
[2000] 1 HKC 511; (2000) 3 HKCFAR 70; [2000] 1 HKLRD 568

Lord Hoffmann NPJ:

1. A liquidity crisis

In 1982 the Wheelock Marden group was one of the great commercial houses of Hong Kong. It was involved in shipping, insurance, transport, retailing and property and had assets of over HK$6bn. But the shipping subsidiary, Wheelock Maritime International Ltd (WMI), was in trouble. At a time when freight rates were high, it had ordered 22 new ships. In 1982 rates fell sharply and the company had difficulty in finding the cash to meet its commitments. By February 1983 it was facing a liquidity crisis.

The director principally responsible for the conduct of the business of WMI was Mr Robert Brothers. It fell to him to try to negotiate a moratorium with banks that had lent money for the purchase of existing vessels and to negotiate cancellations, deferral of deliveries or better financial terms with the yards from which new ships had been ordered and the institutions that had agreed to finance them.

2. Danish ship finance

The crisis coincided with the imminent delivery of a ship which had been ordered from a Danish yard. The financing was complicated because it included a substantial subsidy from the Danish government structured in a way which was thought not to offend the prohibition on state aid under European law. Putting the matter briefly, a state owned corporation called Aktieselskabet Dansk Skibsfinansiering (ADS), which is now the plaintiff in this action, agreed to lend WMI the full purchase price at a concessionary rate of interest, repayable in half-yearly instalments over 81/2 years. The loan was to be fully secured by a back to back deposit of a smaller sum by WMI, which carried a commercial rate of interest.

In March 1983 Mr Brothers negotiated a revision of these terms. … ADS agreed to … [accept] a smaller deposit as security. The rest of its loan, amounting to about US$8m, would be left substantially unsecured and repayable in a single instalment at the end of the 81/2 year period. On these terms the vessel, called the 'Sealock', was delivered on 7 April 1983. A similar arrangement was made to allow the delivery of a second vessel ('Annalock') on 22 March 1984 except that the amount of the loan which ADS left deferred and unsecured was about US$4m.

3. Insolvency and litigation

In the event, WMI was unable to trade out of its difficulties. In February 1985 there was a take-over bid for the Wheelock Marden group by Wharf, a group controlled by Sir YK Pao which had shipping interests of its own. WMI was allowed to go into creditors' voluntary liquidation. Unsecured creditors like ADS were paid 16 cents in the dollar. In 1988 ADS commenced proceedings against the directors of WMI. … It also claimed that Mr Brothers had induced ADS to enter into the revised

36 (1873) LR 6 HL 377 at 403, [1861-1873] All ER Rep 116 at 129.

arrangements by certain fraudulent representations about WMI's financial position

…

…

8. The misrepresentation appeal

The Judge found that Mr Brothers had been guilty of fraudulent misrepresentation during the negotiations in March 1983 by dishonestly concealing a cash flow projection. A failure to provide information is of course not in itself a representation at all. Unless there is a duty of disclosure, such as exists in contracts of insurance, an omission to provide information, for whatever motive, does not give rise to any liability. However, as Lord Macnaghten remarked in *Gluckstein v Barnes*,[37] 'everybody knows that sometimes a half truth is no better than a downright falsehood'. A statement that is literally true may give a misleading impression. It may imply a state of affairs that other facts would show to be false. Those facts may exist at the time of the statement, in which case the statement is, upon its true construction, false at the time it is made. Or the facts which falsify the representation may come into existence later, but before the representation has been relied upon. In such a case the representor is under a duty to correct what he said and not allow the other party to rely upon a statement which has become false.

In the present case, the Judge said that Mr Brothers should have disclosed the cash flow to correct a misleading impression given by the financial information that he had previously given ADS. The facts disclosed by the cash flow made the earlier statements about WMI's financial position false.

What Mr Brothers had done was to divide the cash flow projection into two parts. The first part dealt only with liabilities secured on WMI's existing ships. This showed that if there were a moratorium, the relevant cash flow would be positive or neutral until mid-1986. The second dealt with payments to unsecured creditors and for new buildings. This showed that US$4.5m would be required in 1983 and US$7.5m in 1984. Thereafter, if nothing further were done, increasingly large sums of cash would have to be found each year. On the footing that interest was payable on the cumulative deficit, it showed that in 1992 some US$60m would have to be found. It was prepared on the assumption that certain 'remedial measures' in relation to new buildings had been taken …

The first projection was ready at the beginning of March and Mr Brothers sent it to the banks from whom he was seeking a moratorium and to Mr Edelmann of ADS. The second was not ready until 18 March, just as Mr Brothers was about to set off for Europe. He sent it to the banks and took a copy to a meeting with Mr Edelmann in London on 24 March.

Mr Brothers' evidence at the trial was that he had handed a copy to Mr Edelmann at the meeting. But the Judge did not believe him. He found that the implications of the cash flow were so disastrous that Mr Brothers knew that if Mr Edelmann saw it, he would break off the negotiations. So he decided to conceal it. And this meant that the information he had previously supplied to ADS gave a false impression of WMI's financial position.

The Court of Appeal was asked to reverse the Judge's finding that Mr Brothers had withheld the document. But they refused to do so. They said they might well have come to a different conclusion but could not say that there was no evidence to support the Judge's finding. But they allowed the appeal on the ground that, even so, there had been no misrepresentation. Nothing that Mr Brothers had

37 [1900] AC 240 at 250–251.

previously told ADS was falsified by the later cash flow. The first cash flow and the accompanying correspondence made it absolutely clear that it related only to existing ships. It could not have conveyed any impression about what the position in relation to unsecured creditors and new buildings was likely to be.

...

... I ... agree with the Court of Appeal that the plaintiff's case on misrepresentation failed and ought to have been dismissed.

Li CJ, Ching PJ, Bokhary PJ, and Fuad NPJ agreed with Lord Hoffmann NPJ.

[14-32] Both the Court of Appeal and the Court of Final Appeal accepted the finding of the trial judge that Brothers had concealed from ADS one of two cash flow projections. Both appeal courts differed from the trial judge on the issue as to whether this concealment constituted, on the facts, a misrepresentation. Whereas the trial judge found that the concealment was objectively and fraudulently misleading as to WMI's true financial position, the appeal courts found that no misrepresentation had occurred; the two cash flow projections related to separate aspects of WMI's business, and nothing in the concealed projection objectively falsified the information in the disclosed projection.

[14-33] The question was, therefore, not the broader one of whether the concealment created a *false overall impression* of WMI's financial position. Rather, the narrower question the appeal courts asked themselves was whether the information contained in the concealed projection *falsified the facts* asserted about the subject matter of the disclosed projection. This narrower formulation of the question indicates the relatively high threshold for any argument that silence constitutes a misrepresentation by half-truth.

(e) Inducement to conclude contract and failure to verify

Inducement

[14-34] A misrepresentation will not be material unless it was one of the inducements causing a reasonable person in the position of the representee to conclude the contract.[38] The test as to whether a misrepresentation is material was articulated by Scott J in *Museprime Properties Ltd v Adhill Properties Ltd*:[39]

> A representation is material, in my opinion, if it is something that induces the person to whom it is made, whether solely or in conjunction with other

38 *Master Yield Ltd v Ho Foon Yung Anesis* [2013] 6 HKC 520, para 22 (Lam JA, Cheung and Kwan JJA agreeing, HKCA), emphasising that the test is not the misrepresentation's effect on a reasonable bystander.

39 [1990] 2 EGLR 196 at 201–202, cited with approval in *Master Yield Ltd v Ho Foon Yung Anesis* [2013] 6 HKC 520, para 21 (Lam JA, Cheung and Kwan JJA agreeing, HKCA).

> inducements, to contract on the terms on which he does contract. I would gratefully adopt the view expressed in *Goff & Jones on the Law of Restitution* 3rd Ed, at p 168, which reads,
>
> 'In our view any misrepresentation which induces a person to enter into a contract should be a ground for rescission of that contract. If the misrepresentation would have induced a reasonable person to enter into the contract then the court will, as we have seen, presume that the representee was so induced and the onus will be on the representor to show that the representee did not rely on the misrepresentation either wholly or in part. If, however, the misrepresentation would not have induced a reasonable person to contract, the onus will be on the representee to show that the misrepresentation induced him to act as he did. [...] '

[14-35] A misrepresentation will, therefore, be rebuttably presumed to have induced the representee to enter into the contract if it would have so induced a reasonable person in the position of the representee. In order to rebut such a presumption, the representor must prove either that the representee knew the statement to be false, or that he otherwise placed no reliance on it in concluding the contract (because eg., the misrepresentation had not come to his notice,[40] was made after the contract was concluded,[41] or he relied on his own information[42]).

Failure to verify

[14-36] A misrepresentation may, moreover, be operative notwithstanding that the representee could have checked its veracity but failed to do so.

Redgrave v Hurd

Court of Appeal (England and Wales)
(1881) LR 20 Ch D 1; [1881–1885] All ER Rep 77

Redgrave was a solicitor who placed an advertisement in the *Law Times* seeking a partner for his practice who would not object to buying his residence. Hurd replied to the advertisement. Redgrave told Hurd on two different occasions that the practice was bringing in about £300 per annum or about £300 to £400 per annum. Redgrave showed Hurd summaries of the practice's business over the three previous years which disclosed an annual income of slightly less than £200. He told Hurd that the difference could be explained by the fact that the practice also generated additional income not included in the summaries, but which he could verify for himself by going through a bundle of papers shown to him. Hurd declined the invitation to check the papers. Had he done so, he would have discovered that they disclosed virtually no additional income. Hurd concluded a contract under which he agreed

40 *Ex parte Biggs* (1859) 28 LJ Ch 50.

41 *Hunt v Optima (Cambridge) Ltd* [2014] EWCA Civ 714, [2014] All ER (D) 70 (Aug), [2015] 1 WLR 1346 (negligent misstatements in architects' certificates of completion not material because issued after contract of sale).

42 *Attwood v Small* [1835–1842] All ER Rep 258, (1838) 6 Clark & Finnelly 232, 7 ER 684 (misrepresentations concerning capacity of mines and ironworks not material because representee relied on his own inspections leading him to conclude the statements were true).