AUTONOMY AND PATERNALISM FROM A COMMON LAW PERSPECTIVE:

SETTING ASIDE DISADVANTAGEOUS TRANSACTIONS

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Abstract

English contract law has, by a variety of methods, set aside or refused to enforce transactions that are extremely disadvantageous to one of the parties. The inclusion in the Draft Common Frame of Reference of a general power to this effect suggests that many European systems have often also reached similar results. These cases might, from one perspective, be regarded as instances of paternalism and infringements of autonomy, but other considerations have been relevant, including public policy, avoidance of unjust enrichment and whether the party seeking enforcement has had a legitimate interest in doing so.

1 Introduction

The juxtaposition of autonomy and paternalism suggests an enquiry into the extent to which it is justifiable for society to restrict individual freedom in the interests of the person whose freedom is restricted. At its widest, this topic has many aspects, crossing over between public and private law. The focus of this article is on contract law. It is often supposed that principles of autonomy, allied with the concepts of freedom (or sanctity) of contract, imply that enforcement of contracts is justified, or even necessary, no matter how one-sided or disadvantageous the contract may be. It will be seen, however, that, by a variety of methods, relief has often been given from disadvantageous transactions of various kinds. The present article is mainly concerned with English law and with systems closely allied with it, but neither the perceived problem nor the shape of the plausible solutions has been peculiar to English law, as will be suggested by references to the recent European Draft Common Frame of Reference (2009). It might be true to say, as a social observation, that most contracts involve an exchange of approximately equal value, but this assertion is not true in respect of contract law. Very many – probably most – contracts that are legally significant involve the exchange of unequal values, and the effect of contract law, where the contract is enforced, is therefore to bring about an unequal exchange. A contract may make a poor person rich, and it may make a rich person poor. To him that has, contract law may give, and, more relevantly to the theme of the present article, from him that has not it may take away even that which he has.

2 Consideration

English contract law includes a requirement, known as consideration, that came to be generally understood by the eighteenth century as a requirement that value must have been given or promised in exchange for the promise sought to be enforced. Patrick Atiyah remarks that, from the point of view of liberal theory, the doctrine of consideration is ‘fundamentally paternalist’.1 In earlier times, the word ‘consideration’ had various meanings, but the modern meaning (value given or promised in exchange) was familiar in the early eighteenth century. Jeffrey Gilbert, later Chief Baron of the Exchequer, in

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an unpublished work written in the early eighteenth century entitled ‘Of Contracts’, in seeking to explain the doctrine of consideration, gives several explanations, not all consistent with each other. The first reason given in support of the doctrine, namely the need to protect potential defendants from liability for rash promises, has a decidedly paternalistic tone. Having said that some opinions favoured ‘the punctuall performance of every verbal promise’, Gilbert continues:

Others held that no obligation arises from a naked promise and that the force of the engagement doth totally depend on the consideration and they take it to be a thing of great rigour that a man should dispose of the fruits and effects of a long and painful industry and all the certain advantages and conveniences of life by the mere breath of a word and the turn of an unwary expression; they also think that the very laws of self-preservation will not permit it for what reason of conscience can oblige a man to those words that tend to his own destruction, but if a valuable consideration had been received the bargain is compleat for another man’s industry comes in the place of his own….

Gilbert continues by saying that English law ‘hath held the middle between these two extremes’, in that formal contracts are enforceable so that if a man will oblige himself under the solemnitys of law whereby his contract appears to be seriously intended, it shall ever be obligatory and the consideration shall be intended… but if the contract be verball only it binds in respect of the consideration, otherwise a man might be drawn into an obligation without any real intention by random words, ludicrous expressions, and from hence there would be a manifest inlet to perjury because nothing were more easy than to turn the kindness of expressions into the obligation of a real promise.2

Four very different ideas are manifest in this passage, all attributed by Gilbert to the concept of consideration: due deliberation, the reason for making the contract, the reason for enforcing it and reliable evidence that the promise in question had actually been made. From a later perspective, it may be remarked that, by implication, consideration in the sense of exchange also imported into English law the idea of mutual agreement, though this idea was not fully developed until the following century.

The protection of promisors from disadvantageous transactions (Gilbert’s first reason) could not, in itself, supply a wholly satisfactory explanation, either historically or functionally, of the doctrine of consideration. Consideration has not usually been thought of as a method of protecting the weak from disadvantageous bargains, because the consideration need not be of equal value with the promise that is to be enforced: a very small value – conventionally, as was said, a peppercorn – is sufficient. It is true also that courts have often shown considerable ingenuity in discovering consideration in circumstances where it might at first appear to be absent.3 But nevertheless it is also true that one effect of the doctrine of consideration has been to prevent the legal enforcement of purely gratuitous promises, even though they meet all usual tests of voluntariness or autonomy and even though the fact of the promise is convincingly proved, for example by a signed writing.4 The doctrine of consideration was also employed in the nineteenth century to prevent enforcement of one-sided modifications of obligations, and one effect of this was, in some cases, to give protection to persons who had made disadvantageous modifications of their contractual rights.5 This branch of the law was heavily criticised by courts and commentators, and more recently other approaches to the question have been advanced.6

3 Specific Performance

In English law, specific performance is regarded, conceptually, as an exceptional remedy, available only if damages are inadequate. One effect of this approach has been to enable a person who has entered into a very burdensome contract to refrain from performing

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2 J. Gilbert, Of Contracts (manuscript about 1710), British Library, Hargrave 265, folios 39-40 (some punctuation added, abbreviations expanded and capitalisation removed).
3 An example is North Ocean Shipping Co. Ltd. v. Hyundai Construction Co. Ltd. (The ‘Atlantic Baron’) [1979] QB 705.
4 Rann v. Hughes (1778) 7 TR 350n.
5 Stilk v. Myrick (1809) 2 Camp 317, 6 Esp 129; Foakes v. Beer (1884) 9 App Cas 605 (HL).
it, while offering to pay appropriate monetary compensation to the other party. This aspect of the law has been defended by economists as a recognition of ‘efficient breach’, and this concept, though criticised by some commentators, has been accepted by some courts. The phrase ‘efficient breach’ appears on its face to be paradoxical, and Daniel Friedmann has usefully suggested that ‘tolerated breach’ may be a preferable concept.

In the case of contracts for personal services, there is a more fundamental objection to specific enforcement, namely that it would be unduly restrictive of liberty. *De Francesco v. Barnum* involved an apprenticeship agreement with a dancing teacher whereby the apprentice agreed to serve for seven years and not to enter into any professional engagements without the teacher’s permission during that time. The contract was set aside primarily because the apprentice was a minor, but in discussing the availability of an injunction, Fry LJ commented generally on specific enforcement of contracts for personal services:

I have a strong impression and a strong feeling that it is not in the interest of mankind that the rule of specific performance should be extended to such cases. I think the courts are bound to be jealous, lest they should turn contracts of service into contracts of slavery; and, therefore, speaking for myself, I should lean against the extension of the doctrine of specific performance and injunction in such a manner.

Specific enforcement was refused, not only because it would have been oppressive to the individual, but because it was ‘not in the interest of mankind’. Fry, who was a treatise-writer as well as a judge, commented in the next edition of his treatise after this decision that ‘it is not for the interests of society that persons who are not desirous of maintaining continuous personal relations with each other should be compelled to do so.’ These comments, in and out of court, show that there is a public interest, as well as a purely private interest, in retention by individuals of some degree of freedom.

It is true that, in *Lumley v. Wagner*, an injunction was issued restraining an opera singer from performing for a competitor of the plaintiff, but the court recognised that a decree of specific performance actually compelling the defendant to sing for the plaintiff would have been out of the question. In addition, the restraint on the defendant’s freedom of action imposed by the injunction was comparatively slight: the injunction was only valid for a period of three months and operated only in England, which was not the defendant’s normal sphere of activity. Moreover, there were reasons for the order that are not present in most cases: the singer was a star performer for whom there was no substitute; the plaintiff had invested heavily in her appearance at his opera house; a monetary remedy would have been ineffective; and the defendant was likely (unless restrained by injunction) to confer an unjust benefit on the plaintiff’s competitor. It is these considerations that lie behind the rules, adopted in many common law jurisdictions, that an injunction will not be issued unless the defendant’s services are unique and that the plaintiff must have an interest in restraining the defendant’s conduct that is independent of the interest in inducing performance of the positive side of the contract.

A powerful reason for reluctance in granting a decree of specific performance has been that, if the promisee were entitled to specific performance in a case where the burden to the promisor greatly exceeded the benefit to the promisee of actual performance, the promisee would be in a position to extract from the promisor a sum of

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9 (1890) 45 Ch D 430.

10 Id., at 438.


12 (1852) 1 De G M & G 604.

money approaching the value to the promisor of release and possibly greatly exceeding the value to the promisee of actual performance. Whatever the terminology, it is a fair summary of the practical effect of the law to say that, where a contract imposes a burden on the promisor that is disproportionate to the legitimate interest of the promisee in actual performance, specific performance will not be granted, and the promisee will be restricted to a monetary remedy. Other legal systems that accept specific performance as a conceptually prior remedy may in practice achieve a similar result in many cases by using other concepts, such as good faith or abuse of rights. As part of recent attempts to harmonise European law, several documents have been published with a view to laying the groundwork for what may eventually become a contract code that incorporates both common law and civil law traditions. The most prominent of these, the Draft Common Frame of Reference, in seeking to harmonise English law with continental systems, provides that ‘specific performance cannot … be enforced where … performance would be unreasonably burdensome or expensive.’ In their comment on this article, the drafters observe that, despite the opposite conceptual approaches of English and civilian law, ‘there is reason to believe … that results in practice are rather similar under both theories’. In this context, another comment refers to good faith and ‘abuse of remedy’. A feature of the law that is especially relevant to the theme of the present article is that even an express contractual provision that the promisor will submit to specific performance is not binding, though it may be relevant to the exercise of the court’s discretion. Despite such an express provision, the court will only make a decree of specific performance if satisfied that it is appropriate at the time the order is made.

4 Mistake

Relief has been given against various kinds of mistake. Mistakes as to the contents of contractual documents have been dealt with by various means, including a very extensive power of the court to reform or rectify the document, techniques of interpretation and admission of extrinsic evidence to prove the understanding of the parties or to show misrepresentations or collateral contracts. These may be regarded as methods of preventing the enforcement of a transaction that would be disadvantageous to one party, in circumstances where the other party has no reasonable expectation that the document truly represents the mistaken party’s intention and therefore has no legitimate interest in enforcing the terms of the document.

Where money is paid or value given in the expectation that certain facts exist, or that certain events will occur, and where those facts or events fail to materialise, an unexpected enrichment may occur. English law has given relief from contracts where unanticipated future events cause a radical change in circumstances. In some cases of mistake as to existing facts relief has been given, though there is considerable doubt about its scope. Relief has been given from a completed gift on proof that the gift was made under the influence of a radical mistake. These cases have often had the effect of

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16 Comment B, Volume 1, at 829.
17 Comment J, Volume 1, at 833-834.
22 Lady Hood of Avalon v. Mackinnon [1909] 1 Ch 476.
granting relief from transactions that, if enforceable, would have turned out to be highly disadvantageous to one of the parties because of the unexpected facts or events.\(^\text{23}\)

5 Failure of Counter-performance

An analogous rule, though one not usually considered in this context, is that where reciprocal performance has been promised on each side, the failure of one party’s performance excuses the other. Lord Mansfield said in 1760, in what has become the leading case on unjust enrichment in English law, that money paid could be recovered back if it had been paid ‘upon a consideration which happens to fail’.\(^\text{24}\) As mentioned earlier, contract lawyers have commonly used the word ‘consideration’, as a criterion of enforceability, to mean value given or promised in exchange for the promise sought to be enforced. It is evident that Lord Mansfield was using the word in another sense, and it has often been said, by way of glossing his phrase, that consideration there meant contractual performance. However, it is very probable that Lord Mansfield was using the word in a still wider sense, to mean the reason or basis for the making of the payment. The passage was so understood by Sir William Evans, who equated it with the declaration *causa data causa non secuta* of Roman law,\(^\text{25}\) and was also understood in this sense in the mid-nineteenth century and applied outside the contractual context.\(^\text{26}\)

Birks, writing in 1985, also understood the word in this wide sense, again noting the influence of Roman law:

The link between ‘consideration’ and contracts makes it easy to suppose that ‘total failure of consideration’ must always refer to a failure in contractual reciprocation, whereas in fact that is only the most common species of the genus so described. In the law of restitution the word ‘consideration’ should be given the meaning with which it first came into the common law. A ‘consideration’ was once no more than a ‘matter considered’, and the consideration for doing something was the matter considered in forming the decision to do it. In short, the reason for the act, the state of affairs contemplated as its basis. Failure of consideration for a payment should be understood in that sense. It means that the state of affairs contemplated as the basis or reason for the payment has failed to materialise or, if it did exist, has failed to sustain itself. [The language of the Digest for the same phenomenon is *causa data causa non secuta* (things given upon a consideration, that consideration having failed)].\(^\text{27}\)

In its widest sense, the principle suggested by Lord Mansfield might be extended to the cases of mistake and frustration and to embrace the contractual and restitutionary perspectives on these questions: that money transferred on a fundamental basis that happens to fail may be recovered back and that, if in such circumstances the money has been promised but not yet paid, it ceases to be payable.\(^\text{28}\)

Opinions have differed on whether unjust enrichment is subordinate, secondary, supplementary or subsidiary to contract law.\(^\text{29}\) Where a forfeiture clause is adjudged valid, it could certainly be said that contract prevails, but unjust enrichment is not irrelevant, because the assessment of the validity of the clause itself involves considerations of unjust enrichment. The validity of the clause is judged by weighing the considerations that favour enforcement of contracts against the desirability of avoiding the unjust

\(^{23}\) E.g. Krell v. Henry [1903] 2 KB 740 (CA).

\(^{24}\) Moses v. Macferlan (1760) 2 Burr 1005.


\(^{26}\) Martin v. Andrews (1856) 7 El & Bl 1 (money paid for anticipated expenses of subpoenaed witness; expenses not incurred).


\(^{28}\) Peter Birks suggested failure of basis as the foundation of unjust enrichment in Unjust Enrichment (Oxford 2003).

enrichment that would be effected by an extravagant forfeiture. Where the claimant is entitled to restitution, whether to avoid a forfeiture or a result that is otherwise unconscionable, or for undue influence or duress, it could be said that unjust enrichment prevails over contract, because entitlement to restitution necessarily implies that the contract is unenforceable. No contract can be valid if performance of it would give rise to an immediate right to restitution.30

6 Unfairness

Since the nineteenth century, writers on English contract law have emphasised the enforceability of contracts and have tended to marginalise the instances in which contracts have been set aside for unfairness. In dealing with consideration it has been common to point out that inadequacy of consideration is not, in itself, a defence against contractual obligation, and from this it has been inferred that, if there is sufficient consideration to meet the test of contract formation, the contract must be enforceable. In the first edition of his treatise on contracts (1876), Sir Frederick Pollock wrote that it was

a distinguishing mark of English jurisprudence that the amount of the consideration is not material. ‘The value of all things contracted for is measured by the appetite of the contractors, and therefore the just value is that which they be contented to give.’ It is accordingly treated as an elementary principle that the law will not enter into an inquiry as to the adequacy of the consideration.31

Sir William Anson (1879) followed the same line, and made the point more forcefully:

So long as a man gets what he bargained for Courts of law will not ask what the value may be to him, or whether its value is in any way proportionate to his act or promise given in return. This would be ‘the law making the bargain, instead of leaving the parties to make it.’32

As both writers were aware, however, this was not the whole story, because courts of equity had often set aside contracts on a variety of grounds relating (in general terms) to unfairness. Pollock mentions this aspect of English law with a somewhat awkward side note in his chapter on consideration (Chapter IV):

Inadequacy plus other things in Equity: see chap. XI

Inadequacy of consideration coupled with other things may however be of great importance as evidence of fraud, &c., when the validity of a contract is in dispute: and it has been considered (though, it is believed, the better opinion is otherwise) to be of itself sufficient ground for refusing specific performance. This subject, which is by no means free from difficulty, will be examined under the head of Undue Influence, Ch XI., post.33

Anson, closely following both the form and the substance of Pollock’s work, deals with the matter as follows:

Equity so far takes adequacy of consideration into account in dealing with contracts, that if a contract is sought to be avoided on the ground of Fraud or Undue Influence, inadequacy of consideration will be regarded as strong corroborative evidence in support of the suit. [Reference follows to what Anson, like Pollock, considers the doubtful power of the court to deny specific performance on this ground.]

After 1875, English courts administered law and equity together, and one of the principal stated purposes of Pollock’s book was to consider English law and equity as a whole. However, his approach to this question, followed in starker form by Anson, tended to marginalise the power of the court to set aside disadvantageous contracts. The statement of the general principle of law, followed by the mention, two pages later, of a power to set aside contracts ‘in equity’ suggests that the power is exceptional. The categories of ‘fraud, &c.’ and ‘fraud or undue influence’ suggest rare and closely defined instances,
scarcey affecting the general principles of contract law. The reference to inadequacy of consideration as a matter only of evidence tends to suggest that it has little effect on substantive law, and the emphasis of both writers on the power of the court of equity to refuse specific performance (leaving the promisee with a right to full damages) tends to distract the reader from the far more significant power of the court to rescind the contract (leaving the promisee with no remedy at all). The postponement of the subject to a later chapter also tends to suggest that it is not directly relevant to the most basic principles of contract law, and that relief on the grounds of unfairness is conceptually exceptional. The tendency to marginalise the issue reached a peak in Halsbury’s Laws of England (1907-1915), in which unconscionable contracts are excluded altogether from the article on Contract and are dealt with, anomalously, in a different volume in the article on Fraudulent and Voidable Conveyances.

However, the power of English courts to set aside contracts on grounds broadly relating to unfairness and inequality of exchange was considerably wider than the extracts from Pollock’s and Anson’s books suggest. The first published treatise on English contract law (by John Joseph Powell, 1790) included a long chapter entitled ‘Of the Equitable Jurisdiction in relieving against unreasonable Contracts or Agreements’. Powell states that the mere fact of a bargain being unreasonable is not a ground to set it aside in equity, for contracts are not to be set aside, because not such as the wisest people would make; but there must be fraud to make void acts of this solemn and deliberate nature, if entered into for a consideration. However, he goes on to point out that ‘fraud’ in equity has an unusual and very wide meaning:

And agreements that are not properly fraudulent, in that sense of the term which imports deceit, will, nevertheless, be relieved against on the ground of inequality, and imposed burden or hardship on one of the parties to a contract; which is considered as a distinct head of equity, being looked upon as an offence against morality, and as unconscientious. Upon this principle, such courts will, in cases where contracts are unequal, as bearing hard upon one party … set them aside.

Powell gives as an example the very common provision in a mortgage that unpaid interest should be treated as principal and should itself bear interest until paid. Powell writes that ‘this covenant will be relieved against as fraudulent, because unjust and oppressive in an extreme degree’. The very wide meaning thus given to the concepts of ‘fraud’ and ‘fraudulent’ indicates that the power to set aside contracts was much wider than at first appears. Pollock, in his chapter on duress and undue influence, also explains to his readers that ‘fraud’ could not be taken at face value:

The term fraud is indeed of common occurrence both in the earlier and in the later authorities: but ‘fraud does not here mean deceit or circumvention; it means an unconscientious use of the power arising out of these circumstances and conditions’ and this does not come within the proper meaning of fraud, which is a misrepresentation … made with the intent of creating a particular wrong belief in the mind of the party defrauded. Perhaps the best word to use would be imposition, as a sort of middle term between fraud, to which it comes near in popular language, and compulsion, which it suggests by its etymology.

It is significant that Pollock, in elucidating the meaning of the word fraud, should consciously look for an equally ambiguous word (imposition), suggesting, on the one hand, the taking of unfair advantage and, on the other hand, actual compulsion.

7 Forfeitures

The court of equity commonly gave relief against forfeitures of all kinds. The most clearly established case was that of a mortgage. Mortgage documents usually provided that, on default in repayment, the land should be forfeited to the mortgagee. The courts

35 J.J. Powell, Essay upon the Law of Contracts and Agreements, 2 volumes (1790) Volume 2, at 143.
36 Id., at 144.
37 Id., at 145-6.
38 Id., at 146.
39 Note 31, above, at 527.
consistently refused to enforce this simple provision, despite the fact that it was well known and perfectly clear. Whatever form of words was used – even if the document evidenced an outright conveyance of the land – the court, if convinced that the substance of the transaction was a mortgage, refused to enforce the document and permitted the borrower to redeem the land:

So that in every mortgage the agreement of the parties upon the face of the deed, seems to be, that a mortgage shall not be redeemable after forfeiture ... and a mortgage can no more be irredeemable than a distress for rent-charge can be irrepleviable. The law itself will control that express agreement of the party; and by the same reason equity will let a man loose from his agreement, and will against his agreement admit him to redeem a mortgage.40

No restriction, even by express agreement, was permitted on the right to redeem. In Spurgeon v. Collier (1758), Lord Northington said that ‘a man will not be suffered in conscience to fetter himself with a limitation or restriction of his time of redemption. It would ruin the distressed and unwary, and give unconscionable advantage to greedy and designing persons’.41 This last sentence compendiously illustrates the impact of the separate but interlocking concepts that have run through the unconscionability cases: lack of consent, avoidance of unjust enrichment and deterrence of wrongdoing. A few years later, the same judge again linked the concepts of reason, justice, freedom of consent and deterrence of trickery:

The court, as a court of conscience, is very jealous of persons taking securities for a loan, and converting such securities into purchases. And therefore I take it to be an established rule, that a mortgagee can never provide at the time of making the loan for any event or condition on which the equity of redemption shall be discharged, and the conveyance absolute. And there is great reason and justice in this rule, for necessitous men are not, truly speaking, free men, but, to answer a present exigency, will submit to any terms that the crafty may impose upon them.42

The rule was that the mortgagee could stipulate for no collateral advantage, and so strict was this rule that it came to be applied so as to cause the setting-aside of agreements that were perfectly fair and reasonable. It was easier for the nineteenth-century English legal mind to accept a rigid rule that a mortgagee could in no circumstances stipulate for a collateral advantage (a rule that, for better or worse, happened to be the law) than it was to accept a general power to relieve against unfair transactions (which seemed to admit a dangerous instability). So, ironically, in the name of upholding the sanctity of contracts, transactions were set aside that were not unfair. In a decision of the House of Lords in 1904, Lord Halsbury remarked, with evident irritation, that ‘a perfectly fair bargain made between two parties to it, each of whom was quite sensible as to what they were doing, is not to be performed because at the same time a mortgage arrangement was made between them.’43 Ten years later, the House of Lords restored flexibility by appealing to the underlying original reason for the intervention of the courts:

It was, in ordinary cases, only where there was conduct which the Court of Chancery regarded as unconscientious that it interfered with freedom of contract. The lending of money, on mortgage or otherwise, was looked on with suspicion and the courts were on the alert to discover want of conscience in the terms imposed by lenders... [I]t is inconsistent with the objects for which [the rules of equity] were established that these rules should crystallise into technical language so rigid the letter can defeat the underlying spirit and purpose.44

8 Penalties

Forfeiture in its various forms has obvious advantages to the secured party, and it is not surprising that attempts were made by lenders to secure equivalent advantages without the immediate transfer of the property to be forfeited. The growth of the penal bond represented such an attempt. A common form of the bond was a covenant to pay a fixed

40 Howard v. Harris (1683) 1 Vern 190, 192. This passage from the argument of successful counsel was cited, with page reference and near quotation, as having assisted in establishing the law on the point, by R.H. Coote, A Treatise on the Law of Mortgage (1821) at 22.
41 (1758) 1 Eden 55, at 59 (Sir R. Henley).
42 Vernon v. Bethell (1762) 2 Eden 110, 113.
sum of money unless some other act was performed by a certain date. The effect was to secure the performance of the other act, which might itself be the payment of a sum of money that had been lent by the obligee to the obligor.

The court of equity gave relief from such bonds on much the same principle as in cases of mortgages. The bond was, in substance, a device to secure repayment of a loan, and the legitimate interest of the lender was in repayment of the principal (together with interest and costs) and no more. In 1880, the law on this point, out of keeping though it was with the spirit of the nineteenth century, was explained by Bramwell LJ (who, though not himself sympathetic, accepted that this was the law) as follows:

[T]he Court of Chancery said that a penalty to secure the payment of a sum of money or the performance of an act should not be enforced; the parties were not held to their agreement; equity in truth refused to allow to be enforced what was considered to be an unconscientious bargain.\(^{45}\)

In 1900, another judge said:

The Court of Chancery gave relief against the strictness of the common law in cases of penalty or forfeiture for nonpayment of a fixed sum on a day certain, on the principle that failure to pay principal on a certain day could be compensated sufficiently by payment of principal and interest with costs at a subsequent day.\(^{46}\)

Also important was the obvious factor that a borrower in urgent need was apt to sign too readily an extravagant penal bond: the need for the funds was always immediate, and the possibility of enforcement of the bond remote.

9 Future Interests in Property

The English courts of equity relieved against transactions entered into by persons expecting to own property in the future. The typical case was of the ‘expectant heir’, and this phrase, together with the otherwise obsolete phrase ‘catching bargain’, is generally used to denote this branch of English law, although the jurisdiction was not restricted to heirs: it extended to every kind of case in which the borrower expected to become the owner of property in the future. Commonly, the substance of the transaction was a loan, but the transaction took the form of a sale of the expectancy or of the reversion. The court would set aside the transaction unless the purchaser proved that he had given full value. As in the case of mortgages and penalties, the situation is one in which experience shows that a person, pressed by the immediate need for money, is apt to sell a future interest at an undervalue – sometimes at a gross undervalue: again, the need for money is immediate, and the interest given up seems remote. So ready was the court to set aside such transactions that the rule came to seem too rigid and legislative intervention was found to be necessary: a statute of 1867 provided that such transactions should not ‘be opened or set aside merely upon the ground of undervalue’.\(^{47}\) The statute, however, did not affect the general jurisdiction of the court to set aside unconscionable transactions,\(^{48}\) and this line of cases supplies an important illustration of that wider jurisdiction, before and after 1867.\(^{49}\) In the first edition of his treatise on contracts, Pollock says that ‘practically the question is whether in the opinion of the court the transaction was a hard bargain’.\(^{50}\)

10 Undue Influence

Disadvantageous contractual transactions have frequently been set aside for ‘undue influence’. This phrase covers a number of different circumstances. It may apply to an openly hostile relationship where one party threatens the other with adverse consequences

\(^{45}\) Protector Loan Co. v. Grice (1880) 5 QBD 592, 596.
\(^{46}\) Re Dixon [1900] 2 Ch 561, 576, per Rigby LJ.
\(^{47}\) 31 & 32 Vic c. 4.
\(^{48}\) Earl of Aylesford v. Morris (1873) 8 Ch 484, 490.
\(^{49}\) See the passage quoted at note 55 below.
\(^{50}\) Pollock, above note 31, at 534-535.
if the agreement is not made. This was the case in Williams v. Bayley,\(^51\) where a son had forged his father’s signature to promissory notes and the creditor threatened to prosecute the son unless the father agreed to pay the debt. More commonly, the phrase has been applied to situations related to fiduciary duties where one party reposes trust in the other. Certain categories of cases have been said to give rise to a presumption of undue influence, but it is not necessary for the weaker party to bring his or her case into a recognised category: any case in which there is a relationship of trust or confidence may qualify for relief. A recent instance of a case that does not readily fall into any pre-existing category is one where an employee guaranteed her employer’s debts. The guarantee was set aside by the English Court of Appeal. Millett LJ used strong language, very reminiscent of the older equity cases:

"This transaction cannot possibly stand … . It is an extreme case. The transaction was not merely to the manifest disadvantage of Miss Burch; it was one which, in the traditional phrase, ‘shocks the conscience of the court’. Miss Burch committed herself to a personal liability far beyond her slender means, risking the loss of her home and personal bankruptcy, and obtained nothing in return beyond a relatively small and possibly temporary increase in the overdraft facility available to her employer, a company in which she had no financial interest. The transaction gives rise to grave suspicion. It cries aloud for an explanation."\(^52\)

Closely related, and perhaps conceptually indistinguishable,\(^53\) are cases where the relationship between the parties is categorised as fiduciary.

11 Unconscionability

The courts of equity exercised a more general jurisdiction to set aside transactions that they regarded as very unfair. In 1818, it was said that

a court of equity will inquire whether the parties really did meet on equal terms; and if it be found that the vendor was in distressed circumstances, and that advantage was taken of that distress, it will avoid the contract.\(^54\)

In 1888, summarising the cases, Kay J said:

"The result of the decisions is that where a purchase is made from a poor and ignorant man at a considerable undervalue, the vendor having no independent advice, a court of equity will set aside the transaction. This will be done even in the case of property in possession, and a fortiori if the interest be reversionary. The circumstances of poverty and ignorance of the vendor and absence of independent advice throw upon the purchaser, where the transaction is impeached, the onus of proving, in Lord Selborne’s words, that the purchase was ‘fair, just and reasonable’.\(^55\)

Was undervalue alone a sufficient ground for relief? This question is not easy to answer because of the elusive meaning of ‘fraud’. There are, indeed, many statements by courts and commentators to the effect that undervalue alone was insufficient, but these cannot be taken at face value because of frequent indications that a gross undervalue created a ‘presumption of fraud’: where there was a large inequality of exchange the court could presume, without any separate proof, that the disadvantaged party must have been labouring under some sort of mistake or disability, or else must have been influenced by necessity or by some sort of pressure, or by a relationship with the stronger party.\(^56\)

Some cases suggest that the presumption was practically irrebuttable. In Morse v. Royal, Lord Chancellor Erskine said:

"The authorities, connected with this case, are not many; and the principles are perfectly clear. One class of cases is that of contracts, that may be avoided, as being contrary to the policy of the law; which are interdicted for the wisest reasons. Of that kind are a deed of gift, obtained by an Attorney while engaged in the business of the author of that gift; a deed by an heir, when of age, to his guardian; purchases of

\(^{51}\) (1866) LR 1 HL 200.

\(^{52}\) Credit Lyonnais Bank Nederland NV v. Burch [1997] 1 All ER 144, 152.


\(^{54}\) Wood v. Abrey (1818) 3 Madd 417, 423, per Leach VC.

\(^{55}\) Fry v. Lane (1888) 40 Ch D 312, 322. Lord Selborne’s words were from Aylesford v. Morris, above note 48, at 491.

\(^{56}\) Earl of Chesterfield v. Janssen (1751) 2 Ves Sen 125, Heathcote v. Paignon (1787) 2 Bro CC 167."
reversions from young heirs, when of age … . To that class of cases I shall add the case of a trustee selling to himself. Without any consideration of fraud, or looking beyond the relation of the parties, that contract is void … . The contract is interdicted by the policy of the law.57

In *Lowther v. Lowther*, the same judge said that ‘though inadequacy of Consideration is not of itself a sufficient ground for setting aside a Contract, it is, when gross, strong evidence of Fraud.’58 In a note on a case from 1790, it was said that ‘under ordinary circumstances even a considerable inadequacy of price will not invalidate a sale … still, the inadequacy may be so gross as, of itself, plainly to demonstrate fraud.’59 In this context, Joseph Story (1836) speaks of ‘the most vehement presumption of fraud’.60

Inequality of exchange was not, in itself, conclusive, but it does not follow that it was irrelevant: a large inequality of exchange often seems to have called for some sort of explanation (which might be that a part-gift was intended or that the inequality was caused by risks fairly allocated by the transaction).61 An attempt in the twentieth century by Lord Denning62 to restate a general principle in terms of unfairness and inequality of bargaining power was rejected by the House of Lords,63 but the older cases were not overruled.

## 12 Credit Transactions

Since the beginning of the twentieth century, legislation has empowered the court to set aside loan and credit transactions that are found to be (broadly speaking) very unfair.64 A common situation arising in cases of loan guarantees is that the guarantor is induced to enter into the transaction because of some kind of influence exercised by the principal debtor. The problem is whether, and in what circumstances, the lender, not having precise knowledge of the relationship between the guarantor and the principal debtor, should be precluded from enforcing the contract of guarantee. The typical case involves a guarantee given by a wife to secure her husband’s debts or those of his business. But many kinds of relationships raise the same problem. In *Credit Lyonnais v. Burch*, mentioned earlier, where an employee gave a guarantee to secure the debts of her employer, the English Court of Appeal held that the bank was precluded from enforcing the guarantee, and that it was not sufficient for the bank to recommend independent advice:

The bank had actual notice of the facts from which the existence of a relationship of trust and confidence between Mr Pelosi and Miss Burch could be inferred. It knew that they were respectively employer and junior employee working in a small business and should have ‘appreciated that the possibility of influence existed’.65

In a later case, the House of Lords laid down detailed rules for the guidance of lenders in such circumstances. Dealing with the case of a husband and wife, Lord Nicholls said:

For the future a bank satisfies these requirements if it insists that the wife attend a private meeting with a representative of the bank at which she is told the extent of her liability as surety, warned of the risks she is running and urged to take independent advice. In exceptional cases the bank, to be safe, has to insist that the wife is separately advised.66

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57 (1805) 12 Ves 355, 371-372.
58 (1806) 13 Ves 95.
60 J. Story, *Commentaries on Equity Jurisprudence as administered in England and America* (1836) at 250.
61 *Rotheram v. Browne* (1747) 8 Bro PC 297 (part gift); *Mortimer v. Capper* (1782) 1 Bro CC 156 (inherent risk).
64 Moneylenders Act 1900 (excessive harsh and unconscionable), Consumer Credit Act 1974, ss. 137-140 (extortionate, grossly exorbitant, grossly contravenes ordinary principles of fair dealing), Consumer Credit Act 2006, s. 140A (unfair).
65 Above note 52, at 155.
The House of Lords was conscious of conflicting policies, desiring, on the one hand, to protect the vulnerable guarantor and, on the other hand, not to make it practically impossible for spouses to raise money on jointly-owned property. Despite the genuine endeavours of the court to satisfy these conflicting objectives, it is difficult to avoid doubts as to the feasibility of the court’s enterprise, because a guarantor who is truly under the influence of a stronger spouse will not be effectively protected by the measures proposed. A short private meeting in an office at a bank cannot realistically be expected to displace the continuing influence of a stronger spouse in whose company the weaker spouse will be immediately before and after the meeting. Then there is the consideration that the transaction can easily be restructured in the form of a direct advance of cash to the weaker spouse. If he or she is truly under the influence of the other spouse documents can readily be prepared and executed whereby money is paid into the account of the weaker spouse and paid over, after a shorter or longer interval of time, to the other. The precautions imposed by the House of Lords would not apply in those circumstances. Moreover, there is the awkward consideration that, in the case of a guarantee secured by a mortgage on the matrimonial home, it will, if the spouses are still living together, be the stronger spouse – the very party who allegedly has been responsible for the impugned transaction – who will benefit from having it set aside, thus creating an incentive for self-serving evidence and self-serving admissions. From the public policy point of view, difficult questions arise: is it an essential aspect of freedom that persons should have unrestricted power to borrow money on security of their assets, or are some restraints acceptable or desirable, and, if so, what restraints, and on whom, and in respect of what assets? These are questions on which opinions differ widely; they are not questions that the court is well placed to determine.

13 Unfair Terms

There are several other techniques that have been used by English law to control potentially unfair contracts that cannot be discussed here in detail. One of these is the invalidation of disclaimer or exemption clauses, a topic with a long and convoluted judicial and legislative history in the twentieth century. Another is the use of implied terms, which often have the effect of importing obligations of good faith and of converting an apparently one-sided transaction into a more equal exchange. Another method is to find that insufficient consent has been given, in particular circumstances, to a burdensome contractual term. One twentieth-century judge has said that ‘we do not allow printed forms to be made a trap for the unwary’.67

The Draft Common Frame of Reference incorporates several of these concepts in its provisions on unfair terms. An unfair term, which is ‘not binding on the party who did not supply it’, is defined differently according to whether the contracting parties are consumers or businesses. The definitions refer to ‘transparency’, ‘significant disadvantage’, ‘good faith’, ‘fair dealing’ and to whether terms are individually negotiated. A list of terms presumed to be unfair in consumer-business contracts is supplied.68 The comments and notes on these articles show that this was a difficult and controversial question for the drafters.69 Although no general duty of good faith has been adopted by English law, many of the concepts mentioned in the articles and comments are also reflected in English cases.

69 Id., Volume 1, at 628-667.
14 Theoretical Basis for Relief

14.1 Consent

It has been asserted very often that the underlying reason for the refusal to enforce unfair contracts is the absence of consent on the part of the promisor which is implied by such concepts as cognitive incapacity, undue influence and coercion. Consensual capacity is, no doubt, a relevant, necessary and useful perspective on the problem, but it does not supply a complete explanation, and in certain respects it is misleading.

The principal attraction of the ‘consent’ approach is that it apparently enables relief for unfairness to be reconciled with a theory that requires enforcement of all voluntary agreements. Thus, sanctity of contracts can be maintained in theory – those contracts that are not enforced being not, truly speaking, contracts at all. The objections to this, as a complete explanation, are that this approach is fictitious, artificial and circular and that it distorts the concept of consent in cases where that concept is really needed, such as mistake.

In many cases where relief is given, consent, in every ordinary sense of the word, is present. The vendor of land who sells for a tenth of its value or the accident victim who settles a claim for a small sum in cash usually knows what the terms of the agreement are and intends to agree to those terms. Relief has regularly been given against forfeitures and penalties, even to sophisticated and knowledgeable parties. In such cases, is not plausible to argue that the party seeking to set aside the contract has not assented to its terms. The ordinary tests of assent, subjective and objective, are fully met in most such cases. If it were argued that, in cases where the contract is unfair, there is no ‘true’ assent, the answer would be that a test would then be needed of what amounts to ‘true’ assent, and this necessarily reintroduces some test of fairness.

14.2 Wrongdoing

A second general approach to unconscionability has been to focus on the wrongful conduct of the party seeking enforcement. This is suggested by concepts such as equitable fraud and duress. There is confusion regarding the usage of the word ‘unconscionable’. The older usage was to refer to the transaction as unconscionable. The attitude of the party seeking enforcement might be described as ‘unconscientious’ or ‘unconscionable’ or ‘fraudulent’, but these usages referred to the impropriety of seeking enforcement (after the transaction had been adjudged unfair) not to any wrongful conduct at the time of the transaction itself. On the other hand, a number of modern courts have suggested that it is the conduct of the party seeking enforcement that must be shown to be unconscionable, thereby implying the need to establish some kind of wrongdoing.

Many older cases cannot be explained as depending on the defendant’s wrongful conduct. In 1864, in setting aside a sale of land at a large undervalue, Turner LJ said:

I say nothing about improper conduct on the part of the appellant; I do not wish to enter into the question of conduct … . I am content to believe that in this case there has been no actual moral fraud on the part of the appellant in the transaction; but, for all that, in my judgment an improvident contract has been entered into.

In 1873, in granting relief to a plaintiff from an improvident bargain, Lord Selborne said that the defendant is not alleged or proved to have been guilty of deceit or circumvention, and the plaintiff has no merits of his own to plead. He comes into court to be relieved from the consequences of a course of very wilful and culpable folly and extravagance. I think him entitled to the relief which he asks; but I think it is not unjust that he should obtain it at his own expense.

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71 See L.A. Sheridan, Fraud in Equity: a Study in English and Irish Law (1957).
74 Earl of Aylesford v. Morris, above note 48, at 499.
Costs were refused, and in some analogous cases a successful plaintiff has actually been ordered to pay the defendant’s costs. These cases plainly show that proof of wrongdoing on the part of the stronger party was not required. Even though the party seeking enforcement has acted perfectly properly and entirely in good faith, there are cases where the transaction has been set aside. If, as in the 1873 case mentioned, the plaintiff has ‘no merits of his own’ and has caused the difficulties entirely by his own ‘wilful and culpable folly and extravagance’, he may still be entitled to relief. He should pay the expenses attributable to his folly, but this does not mean that he should suffer the consequences of full enforcement of what might be a disastrous contract; justice is sufficiently done if he pays the costs (to both parties) of the legal proceedings that his folly has made necessary.

There are many other cases in which relief has been given despite the absence of wrongful conduct on the part of the party seeking enforcement. Maritime salvage cases supply two kinds of examples. Salvage agreements were not infrequently set aside both on the ground that too small a sum had been agreed (undue advantage being taken of the salvors) and on the opposite ground that too large a sum had been agreed (undue advantage being taken of the ship in distress). Wrongdoing, in any ordinary sense, was not required in either kind of case. In one of the cases setting aside a receipt ‘in full payment’ of salvage services on the ground that the payment was too small, the judge (Dr Lushington) said: ‘I do not mean to say that this receipt was not honestly obtained, but the inclination of the court is to look at the circumstances of the case, and not to allow a paper to operate as a bar.’ In the opposite case, where a salvor took advantage of a ship’s difficulties in order to obtain what the court considered to be an extravagant payment, the agreement was again set aside. The agreement was described by the court as ‘inequitable’, ‘unjust’, ‘unreasonable’ and ‘extortionate’, but it does not appear that the salvor had committed or threatened any legal wrong. Again, undue influence may be established without proof of wrongdoing.

14.3 Unjust Enrichment

The concept of unjust enrichment has been very influential, though not under that name until the twentieth century. In a treatise published anonymously in 1737, the author, generally taken to be Henry Ballow, asserted the power of the court of equity to set aside very burdensome contracts, giving as the reason that ‘no man should be a Gainer by another’s Loss’. This phrase, like phrases in many old and modern cases, such as ‘advantage taken of weakness’ and ‘deriving immoderate gain’, strongly suggests that the principal underlying value to be weighed against the value of enforcing the contract is the avoidance of unjust enrichment. Since the middle of the twentieth century, unjust enrichment has been recognised as a source of obligations independent of contract. In this context, however, the two concepts are closely inter-related: if the contract is enforceable the enrichment is not unjust, but if the enrichment is unjust the contract is unenforceable. It is not satisfactory to say that, before unjust enrichment can be considered, the contract must first be set aside, because the concept of unjust enrichment has itself been highly relevant in determining the enforceability of the

75 L. Field and others, Daniell’s Chancery Practice (1884, 6th ed.) at 1180: ‘Where securities are ordered to be delivered up because the bargain has been unconscientious judgment is generally given for the plaintiff upon the terms that he shall repay the defendant the amount actually advanced or paid by him, with interest; and the defendant being looked upon as a mortgagee for that amount, he was treated as such, and the plaintiff ordered to pay him his costs.’
76 The Silver Bullion (1854) 2 Sp 70, 75. Also Akerblom v. Price Potter Walker & Co. (1881) 7 QBD 129 (CA).
77 The Port Caledonia and The Anna [1903] P 184.
78 Id., at 189-190 (Bucknill J).
80 [Henry Ballow,] A Treatise of Equity (1737) at 11.
contract. Nevertheless, unjust enrichment, standing alone, does not explain every case. A person who agrees to sell or to purchase property or services, even at fair market value, may be entitled to set aside the contract if it was induced by undue influence or by wrongful threats. Thus, the concepts of consent and wrongdoing cannot be entirely dispensed with.

14.4 Public Policy

Public policy has sometimes been directly invoked to set aside disadvantageous contracts. Contracts in restraint of trade, in restraint of marriage or otherwise unduly restrictive of personal liberty have been held to be unenforceable. These cases involve a mixture of public and private considerations. As Lord Diplock said, in relation to contracts struck down for restraint of trade:

If one looks at the reasoning of 19th-century judges … one finds lip service paid to current economic theories, but if one looks at what they said in the light of what they did, one finds that they struck down a bargain if they thought it was unconscionable as between the parties to it, and upheld it if they thought it was not.

There is much debate, and little consensus, about the theoretical basis of contract law. To every theory that seeks to explain why contracts are enforced, unconscionability appears as an exception, anomaly or limitation: the criteria of enforceability are apparently satisfied, yet the contract is not enforced. This is true whether the fundamental purpose of contract law is taken to be giving effect to the will of the promisor or protecting the reliance or expectation of the promisee, whether it deals with promises or bargains, whether it rests on principles of morality or social utility and whether it is primarily concerned with justice between individuals or with social welfare.

Naturally enough, theories seeking to explain the positive reasons for enforcement of contracts do not usually emphasise the excuses for non-performance, but some attempts have been made to discern in the doctrine of unconscionability the positive implementation of valuable social policy. It has been suggested that the willingness of courts to set aside contracts reflects the egalitarian values of the welfare state. There is undoubtedly some substance to this suggestion: a society that acknowledges a duty to give positive assistance to its poorest members can hardly fail to sympathise with a poor and weak person who seeks relief from a very disadvantageous contract.

Nevertheless, there are several reasons why contract law cannot be satisfactorily viewed as a primary tool for the redistribution of wealth. With some exceptions (mainly in monopoly situations), the law does not compel the making of contracts. Even where power is given to reopen or to rewrite a contract, there is usually no power to compel parties that have not dealt with each other at all to enter into a contract. Because of this, the ability of contract law to redistribute wealth in society will always be very strictly limited. Its scope of operation is restricted, on the whole, to granting relief to those who happen to have entered into disadvantageous contracts.

The extent of relief for mistake or unconscionability is usually the restoration of the status quo before the contract was made. If there was an inequality of wealth between

83 See *Griesshammer v. Ungerer* (1958) 14 DLR (2d) 599 (agreement to purchase dancing lessons).
87 *Horwood v. Miller’s Timber & Trading Co. Ltd* [1917] 1 KB 305 (CA).
the parties before the contract was made, the most that the court will do, if it grants relief, is to restore that situation. It may prevent the weaker party from throwing away some of the little wealth that he or she has, but it will not make that party wealthier.

Contract law focuses on individual transactions and not, generally, on the overall wealth of the parties. Thus, wealthy parties benefit at the expense of the poor under doctrines of mistake, as when a bank erroneously credits a customer’s account or when a wealthy party signs a contract that contains a clerical error. Even in the case of relief for unconscionability, a wealthy party may benefit at the expense of a poorer party, as in the case of a wealthy farmer who sells his farm to an impecunious speculator for one-tenth of its value. The court, if inclined to give relief, will not be deterred by the consideration that the farmer is wealthier than the buyer, and that he would remain wealthier even if the transaction were enforced. It should be noted too that the court, in a contract case, lacks the mechanism to assess the wealth of the parties. If redistribution of wealth were to become a central feature of contract law, the court would have to contemplate a full examination of both parties’ wealth, including an assessment of income and a valuation of capital assets, with opportunity for the other party to dispute the evidence. Such a process would, to say the least, be inconvenient in the course of a civil action.

Relief from contractual obligation is specific to the parties. Even if the court had the means to judge the wealth of the parties, it could not compare the plaintiff with other potential recipients of welfare, who might be more deserving, nor could it compare the defendant with other potential contributors, who might have a greater ability to pay. Apart from the fact that the court lacks the machinery to operate a means test and a system of taxation, there are grave political and institutional objections to ad hoc taxation and distribution of the proceeds by individual judges.

The beneficiaries of the relief that contract law can give are rarely the very poor. They are people with something to lose and with the means and energy to seek to regain it. As we have seen, the courts gave relief to expectant heirs who squandered their inheritance and to landowners who sold their land at an undervalue. These were deserving cases, but they were by no means representative of the poorest members of society. The greater the wealth lost, the more useful is the law to the party seeking relief. Thus, the benefit of a judicial power to set aside contracts increases with the wealth of the weaker party. Litigation is often inaccessible to the poor.

The law of insolvency must also be considered. If a debtor has many creditors, but only one is before the court, as is usual in a contract case, it cannot be right for the court to give relief against one creditor only. The effect will probably be to the benefit not of the debtor but of the other creditors. There may well be a case for consumer bankruptcy or a stay of proceedings against a needy debtor, but such a stay should bind all the creditors, and the court, in contract litigation, lacks the mechanism to achieve that result.

The considerations mentioned in the preceding paragraphs tend to suggest reasons why policy, standing alone, has not been adopted by courts as the primary criterion for setting aside unfair contracts. But it does not follow that policy has been irrelevant. The word ‘policy’ has often been used in the sense of general residual considerations of justice between the parties, and in this sense it weighs in favour of giving relief from very harsh transactions. ‘Policy’ has also been used in the sense of giving due attention to the effect that a proposed rule or principle is likely to have on future cases. In this latter sense, policy considerations have frequently been adduced not as a primary reason for granting relief but as a reason for restraint, lest, in the words of an eighteenth-century judge, the court should ‘throw every thing into confusion and set afloat all the contracts of mankind’.91 Relief given from a particular transaction will benefit the disadvantaged party in the particular case, but it may disadvantage persons in similar circumstances in the future by taking away from them the means of obtaining credit.

91 Griffith v. Spratley (1787) 1 Cox Ch 383, 388 (Eyre LCB).
15 A Common European Solution?

The Draft Common Frame of Reference (2009) includes the following provisions:

II – 7:207 Unfair exploitation

(1) A party may avoid a contract if, at the time of the conclusion of the contract:

(a) the party was dependent on or had a relationship of trust with the other party, was in economic distress or had urgent needs, was improvident, ignorant, inexperienced or lacking in bargaining skill; and

(b) the other party knew or could reasonably have been expected to have known this and, given the circumstances and purpose of the contract, exploited the first party’s situation by taking an excessive benefit or grossly unfair advantage.

(2) Upon the request of the party entitled to avoidance, a court may if it is appropriate, adapt the contract in order to bring it into accordance with what might have been agreed had the requirements of good faith and fair dealing been observed....

II – 7:208 Third persons

(1) Where a person for whose acts a party is responsible or who with a party’s assent is involved in the making of a contract:

(a) causes a mistake, or knows of or could reasonably be expected to know of a mistake; or

(b) is guilty of fraud, coercion, threats or unfair exploitation,

remedies under this Section are available as if the behaviour or knowledge had been that of the party.

(2) Where a third person for whose acts a party is not responsible and who does not have the party’s assent to be involved in the making of a contract is guilty of fraud, coercion, threats or unfair exploitation, remedies under this Section are available if the party knew or could reasonably be expected to have known of the relevant facts, or at the time of avoidance has not acted on the contract.92

The comment states that ‘the Article adopts the principle that a contract which gives one party excessive advantage and which involved unfair exploitation may be avoided at the request of the disadvantaged party.’93 Here are several concepts very familiar to English lawyers. The ‘principle’ mentioned in the comment is reminiscent of proposed tests of unconscionability along the lines of taking undue advantage of inequality of bargaining power.94 The factors mentioned in 7:207 (1)(a) (dependence, trust, economic distress, urgent needs, improvidence, ignorance, inexperience or lack of bargaining skill) largely echo expressions used in English courts and tend to suggest lack of consent. The concept in paragraph (1)(b) of ‘knew or could reasonably be expected to have known’ echoes the equitable concept of constructive notice. The requirement of the means of knowledge on the part of the stronger party tends to suggest an element of wrongdoing, but the open-ended indication of what it is that might reasonably have been known – ‘this’ referring to the list in 7:207 (1)(a) and ‘the relevant facts’ in 2:708 (2) – leaves much flexibility. The phrases ‘excessive benefit’ and ‘grossly unfair advantage’ echo phrases like ‘immoderate gain’ and ‘undue advantage’ and suggest unjust enrichment. But there is no express requirement to prove lack of consent, wrongdoing or unjust enrichment. The provision in 7:208 concerning third persons echoes the above-mentioned concerns of the English courts in attempting to deal with the responsibility of lenders to guarantors influenced by family members and others.95 The inclusion of these various elements in a carefully considered international document suggests that it may not be possible to reduce the issue to a single governing concept: several concepts, not wholly commensurable, appear to be simultaneously in play.

One interesting phrase in 7:207 (1)(b) is ‘given the circumstances and purpose of the contract’. This invites the court to look at the real substance of the transaction and ask whether the enrichment can be justified by the allocation of risks properly inherent in the particular kind of transaction. The sale of a reversionary interest in land was, on the face of it, a sale of an interest in land. If that were the real substance of the transaction,
that is, if the seller were dealing in a fair market for the purchase and sale of future property interests, a very large enrichment to either party would be wholly defensible if it arose from risks inherent in the purchase and sale of property, for example an unexpected rise in land values after the date of the contract. The allocation of that risk is the very nature of the contract, and the buyer takes a corresponding risk of a fall in values: general contractual principles give strong support for enforcement even if there is a substantial enrichment to the buyer. The buyer, in that case, would simply have made a profitable, legitimate bargain. But, if the real substance of the transaction is a loan, the court will compare the net effect of the transaction with the terms on which money could be borrowed in a fair market for the lending of money, and will not allow the lender to extract what is, in effect, an extravagant rate of interest. The point was made in an eighteenth-century case:

An annuity may be purchased at as low a rate as you can, provided it was the original negotiation to purchase and sell an annuity: but if the treaty began about borrowing and lending, and ends in the purchase of an annuity, it is evident, that it was only a method or contrivance to split the payment of the principal and usurious interest into several instalments, and consequently that it was a shift … . So, in the case of goods or merchandise it is lawful to sell as dear as you can, on a clear bargain by the way of sale; but if it is first proposed to borrow, and afterwards to sell goods beyond the market price, this is usurious.96

The fact that these provisions have been included in a draft to which European civil and common lawyers have both contributed strongly suggests that it is no less important now than it was 250 years ago to avoid transactions that would ‘ruin the distressed and unwary, and give unconscionable advantage to greedy and designing persons’.97

Another interesting phrase appears in the closing words of 7:208, allowing avoidance of a contract induced by a third party ‘if the [other contracting] party … at the time of avoidance has not acted on the contract’, even if that party had no means of knowing the relevant facts. This phrase recognises a distinction between what Anglo-American lawyers might call the ‘expectation interest’ and the ‘reliance interest’. The party seeking enforcement may be deprived of the right of full enforcement unless there has been reliance. It must follow that, if there has been limited reliance, the disadvantaged party may escape the consequences of full enforcement on compensation of the other party’s reliance, for it can scarcely be a working legal rule that a million-euro transaction becomes fully enforceable because the party seeking enforcement has incurred the cost of a postage stamp. Where the weaker party has, by its own foolishness, caused actual out-of-pocket loss, there is a strong argument for requiring the weaker party to reimburse the other party’s actual loss, as a condition of relief. But this concept does not support full enforcement of the stronger party’s expectation interest. The distinction corresponds to that made in some of the above-mentioned English equity cases,98 where the weaker party was successful in setting aside the impugned transaction but was required to pay the other party’s costs. This suggests that a choice between ‘all or nothing’ is not always necessary or desirable.

16 Conclusion

As has been seen, English law has, by a variety of methods, granted relief against very disadvantageous transactions of various kinds. It would be true to say that, taken as a whole, these methods manifest an element of what may be called paternalism, in the sense of concern for the welfare of the disadvantaged party. It may also be said that these are instances in which autonomy, in the sense of the voluntary desire of the disadvantaged party to enter into the transaction under review, has proved insufficient to justify enforcement. Autonomy and paternalism represent important and relevant considerations, but they cannot be visualised as opposite ends of a simple linear scale. Refusal to enforce an unequal transaction does not restrict the autonomy of the

96 Earl of Chesterfield v. Janssen, above note 56 (Lord Hardwicke).
97 See above note 41.
98 See above notes 74-75.
disadvantaged party at the time when enforcement comes into question. On the other hand, considerations other than paternalism have been influential in inducing courts to withhold enforcement.

First, there is a public interest in the freedom of persons not to be unduly restrained by law. This interest has been reflected in the setting-aside of transactions that are in unreasonable restraint of trade or other freedoms. These cases have reflected considerations that are specific to the contracting parties, as well as a public interest that individuals should be free of undue restraints – not only for their own good but for the good of the community. These two kinds of considerations are not entirely separable, because it has been perceived to be in the public interest that individuals should retain a certain degree of freedom. Related to public policy, but conceptually distinct, is the idea that some transactions have been held to be unenforceable because the court sees enforcement as an inappropriate use of the court. Thus, certain kinds of contracts have been held to be non-justiciable, and other kinds of contracts, such as gaming and wagering contracts – which are often highly disadvantageous to one of the parties, even though they are not illegal or directly affected by statute – have evoked a marked reluctance on the part of courts called upon to enforce them.

Second, there is the question whether the party seeking to enforce the transaction has a legitimate interest in doing so. The cases discussed here suggest that the autonomy, will or consent of the promisor has not been sufficient to justify the imposition of an obligation unless the other party also appears to have a legitimate interest in the enforcement of the transaction in question. The transaction must be looked at from both sides. The cases on forfeitures and penalties reflect the courts’ view that the legitimate interest of the party seeking to enforce such clauses is in securing performance of the primary obligation, not in obtaining an unexpected windfall from a clause that was secondary to the main purpose of the contact. Many of the cases involving written documents suggest that the party seeking enforcement must show that he or she honestly and reasonably thought that the document reflected the actual intention of the other party. In one of the leading Canadian cases on rectification, the US government sought and obtained rectification of a formal contractual document by reason of a mistaken omission in the document. This result is not easily explained as paternalism. The United States did not ask for, or require, the fatherly assistance of the Canadian courts. The US government intended to execute the document as a final expression of its agreement, and its advisers were no doubt very careless in overlooking the omission. But it is not sufficient that the defendant deserves to be made liable: it must also appear that the party seeking to enforce the terms of the document has a legitimate interest in doing so. In this case, there was no such legitimate interest, because that party was found to have agreed to the terms as understood by the United States.

Third, attention needs to be devoted to the law relating to unjust enrichment. Unjust enrichment may offer a firmer conceptual ground for judicial intervention than the concept of paternalism, which, standing alone, may seem an insufficient reason for intervention, or at least one requiring special justification. Forestalling and reversing unjustified transfers of wealth is evidently within the normal range of judicial activity. On the other hand, an unjust enrichment perspective might restrict the scope of intervention by suggesting the need to show not only that the weaker party had incurred a loss but also that the stronger party had made a corresponding gain. Two further related points may be added. One is that the questions addressed here require at least a minimal coherence between the principles of contract law and those relating to restitution for unjust enrichment, because a transaction cannot be legally enforceable if it would have caused an immediate unjust enrichment when it was executed. The other, more general point is that a legal rule might be justifiable because it tends, in general, to prevent undesirable consequences (for example, a rule against disclaimer clauses in consumer contracts, which tends to prevent unfair exclusion of liability), even though there might be no actual unfairness in individual applications of the rule. Many legal rules, once

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99 This concept was developed in respect of tort law in Ernest Weinrib’s influential The Idea of Private Law (1995).

100 USA v. Motor Trucks Ltd [1924] AC 196 (JC).
established, have operated independently of what may be thought to have been their original underlying reasons, such as the doctrine of consideration with which this article commenced. Reverting to the theme of the juxtaposition of autonomy and paternalism, we may conclude that relief from disadvantageous contracts, while restricting autonomy in one sense, has enlarged it in others. While such relief may properly be called an instance of paternalism, it has often been supported for additional and independent reasons.