

# 20B

## ILLEGALITY AND PUBLIC POLICY

### CENTRAL ISSUES

1. A contract may be held to be void on the ground that it is tainted by illegality or on the ground that it is otherwise contrary to public policy. The law in this area is complex and the case-law enormous. The aim of this chapter is not to explore the rules relating to illegality in any detail. Rather, its aim is to examine a limited number of cases with a view to ascertaining the principles which are at stake.
2. Two broad issues arise. The first relates to the definitions of 'illegality' and 'public policy'. The second relates to the consequences that flow from a finding that a contract is illegal or is contrary to public policy. Neither issue is straightforward.
3. It is customary to break down the cases into different categories according to whether the contract is 'void', 'illegal', or is 'contrary to public policy'. The difficulty is that different judges and commentators draw the boundaries between these categories in different places. There is no agreed classification of the cases. No attempt will be made to impose a classificatory scheme on the cases in this chapter.
4. Rather, an attempt will be made (in section 3) to identify the various circumstances in which the courts have concluded that a contract is illegal or contrary to public policy. We shall then consider the law in relation to restraint of trade (section 4) and then finally (in section 5) discuss the remedial consequences of a finding that a contract is illegal.

### 1. INTRODUCTION

A helpful introduction to this topic has been provided by the editors of *Anson's Law of Contract* in the following terms:

***J Beatson, A Burrows and J Cartwright Anson's Law of Contract***  
(30th edn, Oxford University Press, 2016), pp. 409-410

Public policy imposes certain limitations upon the freedom of persons to contract. An ostensibly valid contract may be tainted by illegality. The source of the illegality may arise by statute

© Ewan McKendrick 2020.

or by virtue of the principles of common law. In some instances the law prohibits the agreement itself, and the contract is then by its very nature illegal, but in the majority of cases the illegality lies in the object which one or both parties have in mind or in the method of performance. As a general rule, although all the other requirements for the formation of an agreement are complied with, an agreement that is illegal in one of these ways will not be enforceable.

The subject of illegality is one of great complexity and the effects of illegality are by no means uniform. This is because the seriousness of the illegality varies. Illegal objects may range from those tainted with gross moral turpitude, for example, murder, to those where the harm to be avoided is relatively small, for example, breach of licensing requirements or cases in which a person commits an unlawful act in order to escape danger to his or her life or the life of a third party. It is not surprising, therefore, that there are differences in the attitude of the judges to those who have an illegal object in view or are parties to an illegal transaction. Attempts have been made to distinguish between 'illegal' contracts and those which are 'nugatory' or 'void'. In the former case, it is said that the law will refuse to aid in any way a person whose cause of action is founded upon such a contract; in the latter case, the law simply says that the contract is not to have legal effect. While some contracts can be classified in this way, it is both impracticable and impossible to apply this classification over the whole field of the subject. Moreover, confusion is created by the fact that judges have on many occasions treated the terms as interchangeable. It seems better to use the single word 'illegality' to cover the multitude of instances where the law, for some reason of public policy or as a result of a statutory prohibition, denies to one or both of the parties the rights under the contract to which he or she would otherwise be entitled.

## 2. ILLEGAL CONTRACTS: A SUMMARY

As the editors of *Anson* point out, illegality can affect a contract in different ways. The contract may be illegal from the outset, as in the example of a contract to commit a murder, or the illegality may arise in the course of performance of an otherwise valid contract. An example in the latter category is a contract for the carriage of goods where the vehicle that is used to transport the goods does not have a licence and so cannot lawfully be driven. Provided that the carrier has some vehicles which are properly licensed, the contract is not illegal from the outset: it is capable of being performed lawfully. It is only when the unlicensed vehicle is used in the performance of the contract that any issue of illegality arises. The courts have tended to adopt a more sympathetic stance in cases of illegality in performance, especially in the case where the party bringing a claim for damages for breach of contract did not commit the illegal act, nor did he have any knowledge of it. The sources of illegality also differ. Statute can declare contracts to be illegal but the common law also has a significant role to play. The courts have declared a range of contracts to be illegal or contrary to public policy. Thirdly, the seriousness of the illegality varies enormously between the different cases.

A contract may be illegal for the following reasons:

### (a) STATUTORY ILLEGALITY

We start with a very broad category of illegality, namely statutory illegality. Statute may declare a contract illegal, void, or unenforceable. For example, a licensing system may prohibit the making of contracts in violation of the system. In *Re Mahmoud and Ispahani* [1921] 2

KB 76 the regulations applicable to the contract were those contained in the Seeds, Oils and Fats Order 1919 which provided that 'a person shall not . . . buy or sell' linseed oil 'except under and in accordance with the terms of a licence'. The plaintiffs, who had a licence, asked the defendant if he had a licence. The defendant replied that he did when, in fact, he did not. The plaintiffs sold linseed oil to the defendant but the defendant refused to accept delivery. When sued for damages for non-acceptance the defendant took the point that the contract was illegal on account of the fact that he did not have a licence to purchase the linseed oil. The Court of Appeal held that the plaintiffs were not entitled to bring their action for damages. Atkin LJ stated (at p. 731):

When the Court has to deal with the question whether a particular contract or class of contract is prohibited by statute, it may find an express prohibition in the statute, or it may have to infer the prohibition from the fact that the statute imposes a penalty upon the person entering into that class of contract. In the latter case one has to examine very carefully the precise terms of the statute imposing the penalty upon the individual. One may find that the statute imposes a penalty upon an individual, and yet does not prohibit the contract if it is made with a party who is innocent of the offence which is created by the statute.

The Court of Appeal held that the Order expressly prohibited the making of a contract in breach of the licensing system with the consequence that the plaintiffs were not entitled to bring an action for damages. The result seems a harsh one in that the plaintiffs did inquire whether or not the defendant had a licence and the immediate cause of the illegality was the defendant's failure to answer that inquiry truthfully. The exercise in which the courts are engaged in such cases is one of statutory construction: the court must decide whether or not statute has prohibited the making of the contract. On the facts of *Mahmoud and Ispahani* the Court of Appeal concluded that the intention was to prohibit the making of the contract, whether or not the party seeking to enforce the contract was responsible for the violation of the requirements of the system.

The statutory prohibition can take different forms. In some cases statute has intervened to declare a contract void. An example, albeit one that has since been repealed, is provided by section 18 of the Gaming Act 1845 which provided:

All contracts or agreements, whether by parol or in writing, by way of gaming or wagering, shall be null and void; and . . . no suit shall be brought or maintained in any court of law and equity for recovering any sum of money or valuable thing alleged to be won upon any wager, or which shall have been deposited in the hands of any person to abide the event on which any wager shall have been made: Provided always, that this enactment shall not be deemed to apply to any subscription or contribution, or agreement to subscribe or contribute, for or towards any plate, prize, or sum of money to be awarded to the winner or winners of any lawful game, sport, pastime, or exercise.

This provision was repealed by the Gambling Act 2005 which, in section 335(1) now provides that 'the fact that a contract relates to gambling shall not prevent its enforcement.' The change in the legal regulation of gambling illustrates the point that this area of law is very much influenced by public policy and, of course, the public policy of the nineteenth century can be very different from the public policy of the twenty first century.

The courts have experienced particular difficulties in the case where the contravention of a statute occurs in the performance of a contract. This particular issue arose in the cases of

*St John Shipping Corporation v. Joseph Rank Ltd* [1957] 1 QB 267 and *Archbalds (Freightage) Ltd v. S Spanglett Ltd* [1961] 1 QB 374. These cases are discussed in more detail below.

### (b) AGREEMENTS CONTRARY TO GOOD MORALS

We now turn to consider contracts that are illegal or contrary to public policy as a result of the application of common law principles rather than the intervention of statute. The first example in this category consists of agreements that are contrary to good morals. Such agreements are illegal and unenforceable. Contracts that have been held to fall within this category include an agreement to provide a prostitute with goods for use in her trade (see *Pearce v. Brooks* (1866) LR 1 Ex 213, below) and a promise by a man to pay money to a woman if she would become his mistress (see *Benyon v. Nettlefold* (1850) 3 Mac & G 94). In general it can be said that this category encompasses agreements the aim of which is to promote sexual immorality. Some of the old cases adopt a very conservative view of the requirements of ‘good morals’, particularly in relation to extra-marital cohabitation. However, public attitudes towards extra-marital cohabitation, whether heterosexual or homosexual, have changed over the years and this is reflected in the decisions of modern courts. Agreements between cohabiting parties are now enforceable provided that the parties have an intention to create legal relations (on which see Chapter 7) and provided that the subject-matter of the agreement is not exclusively related to the provision of sexual services.

### (c) AGREEMENTS PREJUDICIAL TO FAMILY LIFE

An agreement which undermines the institution of marriage is illegal and unenforceable. Agreements within this category include an agreement the aim of which is to prevent or restrict the ability of a person to get married (*Lowe v. Peers* (1768) 4 Burr 2225) and an agreement under which one party promises to introduce a person to someone of the opposite sex with a view to marriage (*Hermann v. Charlesworth* [1905] 1 KB 123). It is debateable whether *Hermann* would be followed today, given the prevalence of dating and introduction agencies. This category can also encompass agreements relating to the way in which children are brought up. Thus a parent cannot in general contract out of his parental duties by transferring them to a third party (*Humphreys v. Polok* [1901] 2 KB 385).

### (d) AGREEMENTS PREJUDICIAL TO THE ADMINISTRATION OF JUSTICE

An agreement which is prejudicial to the administration of justice is illegal and unenforceable, such as an agreement to conceal the commission of a crime (*Initial Services Ltd v. Putterill* [1968] 1 QB 396). Similarly, a person who accepts money in return for concealing the commission of a criminal offence may be held to have committed an offence in so doing (Criminal Law Act 1967, section 5). This category has in fact given rise to some difficulties in the courts. It suffices to note three such difficulties.

The first relates to agreements to oust the jurisdiction of the court. There is authority for the proposition that an attempt to oust the jurisdiction of the court is contrary to public policy and hence void (*Czarnikow v. Roth Schmidt & Co* [1922] 2 KB 478). This proposition must, however, be qualified in its application to arbitration where it is possible for the

parties, within limits, to exclude the jurisdiction of the courts. Arbitration is frequently used as a means of dispute resolution in international business and the parties to arbitration agreements usually wish to ensure that their dispute is resolved privately, quickly, and as economically as possible. These purposes would be frustrated if the losing party to the arbitration could simply appeal to court for a re-hearing of the merits of the dispute. While there is a limited right to appeal to the court on a question of law arising out of an award, it is open to the parties to exclude that right of appeal, except in relation to challenges to the jurisdiction of the arbitral tribunal and allegations of serious irregularity affecting the tribunal (see sections 67 and 68 of the Arbitration Act 1996). It is also open to contracting parties to agree that the award of an arbitrator shall be a condition precedent to the right to bring an action on the contract (*Scott v. Avery* (1856) 5 HLC 811). Section 9 of the Arbitration Act 1996 provides that a party to an arbitration agreement against whom legal proceedings are brought in respect of a matter which under the agreement is to be referred to arbitration may apply to the court in which the proceedings have been brought to stay the proceedings so far as they concern that matter.

Secondly, the courts have experienced difficulties in defining the limits of the doctrines of ‘maintenance’ and ‘champerty’. Maintenance is defined in H Beale (ed), *Chitty on Contracts* (33rd edn, Sweet & Maxwell, 2018), para 16-078) in the following terms: ‘a person is guilty of maintenance if he supports litigation in which he has no legitimate concern without just cause or excuse’. Champerty, on the other hand, has been described as an ‘aggravated form of maintenance’ which occurs ‘when the person maintaining another stipulates for a share of the proceeds of the action or suit or other contentious proceedings where property is in dispute’ (*Chitty*, para 16-083). These doctrines have given rise to difficulty in their application to the assignment of rights of action. Where the right assigned is a claim for a liquidated sum due under a contract it can generally be assigned irrespective of the motives of the party taking the assignment. Thus debts are generally freely assignable (*County Hotel and Wine Company v. London and North Western Railway* [1918] 2 KB 251). By contrast, the law in relation to the assignment of unliquidated claims is much less clear. Particular difficulty arises where the assignment takes place after the breach of contract has occurred. Where the assignment takes place prior to the breach of contract no problem generally arises: the rights of the parties are generally assignable. The traditional view of post-breach assignments was that it was not possible to assign a mere right to claim unliquidated damages for breach of contract (*May v. Lane* (1894) 64 LJQB 236, 237–238). That view no longer holds good in the light of modern cases such as *Trendtex Trading Corporation v. Credit Suisse* [1982] AC 679 and *Giles v. Thompson* [1994] 1 AC 142. While the law has moved from its traditional stance it has not (at least as yet) taken the stance that a right to claim unliquidated damages for breach of contract can generally be assigned. Rather it has taken what Treitel (*The Law of Contract* (14th edn, Sweet & Maxwell, 2015) 15-064) has termed an ‘intermediate view’ namely that ‘a right to unliquidated damages for breach of contract may be validly assigned, so long as the assignment does not in fact savour of maintenance or champerty’. There are at least two circumstances in which the courts have held that a right to claim unliquidated damages for breach of contract can be validly assigned. The first is where the assignee has a proprietary interest in the subject-matter of the contract (*Williams v. Protheroe* (1829) 5 Bing 309) and the second is where the assignee has a genuine commercial interest in the subject-matter of the contract. Thus the assignment of a right to litigate is valid if it is incidental and subsidiary to a transfer of property. So, for example, a vendor of land can assign to the purchaser the right to claim damages for breaches of covenant committed by the vendor’s tenants prior to the sale. The modern origin of the ‘genuine commercial interest’ test is the decision of the House of Lords

in *Trendtex Trading Corporation v. Credit Suisse* [1982] AC 679. Simplifying the facts of the case somewhat, Credit Suisse provided finance for the sale of cement by one of its customers, Trendtex. Payment was to be made under a letter of credit by the Central Bank of Nigeria ('CBN'). CBN refused to honour the letter of credit and so Trendtex brought an action against CBN. However the repudiation of the letter of credit by CBN put Trendtex in a very precarious financial position and it became heavily indebted to Credit Suisse. Eventually Trendtex assigned to Credit Suisse its right of action against CBN. Trendtex subsequently sought to set aside the assignment on the ground that it was champertous. On the facts of the case it was held that the assignment was champertous because the assignment was taken for the purpose of enabling Credit Suisse to resell Trendtex's right of action to a third party so that the profit made from the enforcement of Trendtex's right of action could be divided between the bank and the third party. Lord Roskill stated (at p. 703) that such an agreement offended against the law of champerty because 'it was a step towards the sale of a bare cause of action to a third party who had no genuine commercial interest in the claim in return for a division of the spoils'. Thus it was the fact that Credit Suisse envisaged a further onward sale of the right of action that led the House of Lords to conclude that the assignment was champertous. Had there been no onward sale in contemplation but enforcement by Credit Suisse the assignment would have been valid. Thus Lord Roskill stated (at p. 703) that:

For my part I can see no reason in English law why Credit Suisse should not have taken an assignment to themselves of Trendtex's claim against CBN for the purpose of recouping themselves for their own substantial losses arising out of CBN's repudiation of the letter of credit upon which Credit Suisse were relying to refinance their financing of the purchases by Trendtex of this cement from their German suppliers.

*Trendtex* has since been followed in a number of cases. The leading case post *Trendtex* is the decision of the Privy Council in *Massai Aviation Services v. Attorney General of the Bahamas* [2007] UKPC 12 where Baroness Hale stated that it was 'essential to look at the transaction as a whole, and to ask whether there is anything in it which is contrary to public policy.' It is not entirely clear what these public policy concerns are. In general terms it would seem that the courts' concern is with speculation or trafficking in litigation (for a recent example see *Simpson v. Norfolk NHS Trust* [2011] EWCA Civ 1149, [2012] 1 All ER 1423). But the mere fact that the assignee stands to make a profit from the assignment will not of itself suffice to call into question the validity of the assignment. On the other hand, the greater the profit, the more scrutiny there may be and the more likely it is that the validity of the agreement will be challenged.

Thirdly, section 58 of the Courts and Legal Services Act 1990, as amended by section 27 of the Access to Justice Act 1999, permits lawyers and their clients, within certain limits, to enter into conditional fee agreements. It is probably the case that the courts cannot uphold the validity of such agreements in a wider range of circumstances than those set out in the statutory provisions (see *Awwad v. Geraghty & Co* [2001] QB 570, but contrast *Thai Trading Co (A Firm) v. Taylor* [1998] QB 781).

### (e) AGREEMENTS TO COMMIT A CRIME OR A CIVIL WRONG

An agreement to commit a crime is illegal and unenforceable (*Bigos v. Bousted* [1951] 1 All ER 92), as is an agreement to commit a tort, such as libel or assault (*Clay v. Yates* (1856)

1 H & N 73) and an agreement to defraud the revenue (*Alexander v. Rayson* [1936] 1 KB 169). A contract is also illegal and unenforceable where it provides for money to be paid to someone as a result of the commission by him of a criminal act or a tort (see *Beresford v. Royal Exchange Assurance* [1938] AC 586, discussed by Devlin J in *St John Shipping Corporation v. Joseph Rank Ltd* [1957] 1 QB 267, below).

#### (f) AGREEMENTS WHICH ARE INJURIOUS TO GOOD GOVERNMENT

A contract concluded with an enemy alien is illegal and unenforceable (*Ertel Bieber & Co v. Rio Tinto Co* [1918] AC 260) as is a contract which seeks to encourage action which is hostile to a friendly foreign government (*De Wütz v. Hendricks* (1824) 2 Bing 314) and an agreement to sell public offices or public honours (*Parkinson v. College of Ambulance Ltd* [1925] 2 KB 1).

#### (g) AGREEMENTS WHICH ARE IN RESTRAINT OF TRADE

These agreements will be discussed in more detail in section 5 below.

#### (h) CAN THE COURTS DEVELOP PUBLIC POLICY?

The categories of public policy which may invalidate a contract are not fixed in stone. They are capable of adaptation to accommodate the changing values of society. But, at the same time, the courts are slow to create new heads of public policy (see *Richardson v. Mellish* (1824) 2 Bing 229). In general the courts leave it to Parliament to formulate new heads of public policy but at the same time cases can be found in which the courts have been prepared to develop the categories of public policy (*Enderby Town FC v. The Football Association Ltd* [1971] Ch 591, 606; *Nagle v. Fielden* [1966] 2 QB 633, 650). The current state of the law in this regard is summed up in H Beale (ed), *Chitty on Contracts* (33rd edn, Sweet & Maxwell, 2018), para 16-007 in the following terms:

there is some doubt as to whether the courts can create new heads of public policy rather than merely apply existing doctrines to new situations. This is an area where the precedents hunt in packs of two. Broadly speaking, there are two conflicting positions, that have been referred to as the 'narrow view' and the 'broad view'. According to the former, the courts cannot create new heads of public policy, whereas the latter countenances judicial law-making in this area. To a large extent this debate is verbal. There is a general agreement that the courts may extend existing public policy to new situations and rules founded on public policy 'not being rules which belong to fixed or customary law, are capable . . . of expansion and modification.' The difference between extending an existing principle as opposed to creating a new one will often be wafer-thin. There will, however, be an understandable reluctance on the part of the courts to create completely new heads of public policy because of the existence of governmental bodies charged with the specific task of law reform and a more activist legislature. However, where Parliament has clearly articulated a principle of public policy then the courts may be willing to extend it by analogy into the field of contract.

### 3. THREE ILLUSTRATIVE CASES

#### ***Pearce v. Brooks***

(1866) LR 1 Ex 213, Court of Exchequer Chamber

The defendant, a prostitute, hired a decorative brougham from the plaintiff coachbuilders as part of her display to attract men. The plaintiffs alleged that the defendant returned the brougham in a damaged condition and that she had failed to pay the instalments on the hire of the brougham. The plaintiffs brought an action to recover the instalment of 15 guineas which had not been paid or to recover in respect of the damage done to the brougham. The jury found that the plaintiffs knew that the defendant was a prostitute and that the brougham would be used in the course of her 'calling'. On this basis it was held that the plaintiffs were not entitled to recover the unpaid instalment from the defendant.

#### **Pollock CB**

I have always considered it as settled law, that any person who contributes to the performance of an illegal act by supplying a thing with the knowledge that it is going to be used for that purpose, cannot recover the price of the thing so supplied. If, to create that incapacity, it was ever considered necessary that the price should be bargained or expected to be paid out of the fruits of the illegal act (which I do not stop to examine), that proposition had been overruled . . . and has now ceased to be law. Nor can any distinction be made between an illegal and an immoral purpose; the rule which is applicable to the matter is, *Ex turpi causâ non oritur actio*,<sup>1</sup> and whether it is an immoral or an illegal purpose in which the plaintiff has participated, it comes equally within the terms of that maxim, and the effect is the same; no cause of action can arise out of either the one or the other. . . . . If, therefore, this article was furnished to the defendant for the purpose of enabling her to make a display favourable to her immoral purposes, the plaintiffs can derive no cause of action from the bargain.

#### **Bramwell B**

I am of the same opinion. There is no doubt that the woman was a prostitute; no doubt to my mind that the plaintiffs knew it; there was cogent evidence of the fact, and the jury have so found. The only fact really in dispute is for what purpose was the brougham hired, and if for an immoral purpose, did the plaintiffs know it? At the trial I doubted whether there was evidence of this, but, for the reasons I have already stated, I think the jury were entitled to infer, as they did, that it was hired for the purpose of display, that is, for the purpose of enabling the defendant to pursue her calling, and that the plaintiffs knew it.

That being made out, my difficulty was, whether, though the defendant hired the brougham for that purpose, it could be said that the plaintiffs let it for the same purpose. In one sense, it was not for the same purpose. If a man were to ask for duelling pistols, and to say: 'I think I shall fight a duel to-morrow,' might not the seller answer: 'I do not want to know your purpose; I have nothing to do with it; that is your business: mine is to sell the pistols, and I look only to the profit of trade.' No doubt the act would be immoral, but I have felt a doubt whether

<sup>1</sup> No action can be based on a disreputable cause.



it would be illegal; and I should still feel it, but that the authority of *Cannan v. Bryce* 3 B & A 179 and *M'Kinnell v. Robinson* 3 M & W 434 concludes the matter. In the latter case the plea does not say that the money was lent on the terms that the borrower should game with it; but only that it was borrowed by the defendant, and lent by the plaintiff 'for the purpose of the defendant's illegally playing and gaming therewith.' The case was argued by Mr Justice Crompton against the plea, and by Mr Justice Wightman in support of it; and the considered judgment of the Court was delivered by Lord Abinger, who says (p 441):

'As the plea states that the money for which the action is brought was lent for the purpose of illegally playing and gaming therewith, at the illegal game of 'Hazard,' this money cannot be recovered back, on the principle, not for the first time laid down, but fully settled in the case of *Cannan v. Bryce*. This principle is that the repayment of money, lent for the express purpose of accomplishing an illegal object, cannot be enforced.'

This Court, then, following *Cannan v. Bryce*, decided that it need not be part of the bargain that the subject of the contract should be used unlawfully, but that it is enough if it is handed over for the purpose that the borrower shall so apply it. We are, then, concluded by authority on the point; and, as I have no doubt that the finding of the jury was right, the rule must be discharged.

**Martin B** and **Pigott B** delivered concurring judgments

## Commentary

*Pearce* is obviously an example of a contract which was held to be contrary to good morals. On the facts both parties knew that the brougham was to be used for the purpose of prostitution. What would have been the situation if the plaintiffs had been unaware of the purposes to which the brougham was to be put? On such facts the plaintiffs might have been able to bring an action for damages, at least in respect of the damage done to the brougham. Cases can be found in which the courts have adopted a more lenient approach to claimants who were unaware of the fact that the contract was to be or had been performed in an illegal manner (see *Marles v. Philip Trant & Sons Ltd* [1954] 1 QB 29). But in such cases the lack of knowledge must relate to the use to which the goods are being put and not to the question of whether such use is in fact illegal. In the latter context ignorance of the law is generally no excuse (*Nash v. Stevenson Transport Ltd* [1936] 2 KB 128).

*Pearce* also illustrates the policy issues that underlie this area of law. On the facts of the case the prostitute appears to be the beneficiary of the decision in that she did not have to pay for the use of brougham nor did she have to pay for the damage done to the brougham. But the aim of the law is to deter parties from entering into such transactions and the plaintiffs would presumably think more carefully before entering into a contract with a prostitute in the future. By making entry into illegal contracts a hazardous matter, the law hopes to dissuade parties from entering into them in the first place. It has also been argued that justice would be tainted were the court to be required to intervene at the behest of a party to an illegal contract. This is a point of doubtful validity. Would the dignity of the courts have been undermined by a conclusion that the plaintiffs were entitled to recover damages from the defendant?

***St John Shipping Corporation v. Joseph Rank Ltd***  
 [1957] 1 QB 267, Queen's Bench Division

A ship, registered in Panama, carried grain from a US port to the UK. The ship was overloaded, so that its 'loadline' was submerged, contrary to the provisions of the Merchant Shipping (Safety and Loan Line Conventions) Act 1932. Although the overloading enabled the ship to earn an extra £2,295 in freight, the maximum statutory fine (which was levied in this case) was only £1,200, with the result that that the statute was ineffective in removing the incentive to overload. The defendants, who were owners of some of the cargo, withheld £2,000 of the freight due under the contract and another cargo-owner withheld £295. The plaintiff shipowners sued to recover the withheld freight. The defendants argued that, as the shipowners had performed the contract in an illegal manner, they were not entitled to recover any part of the freight due. Devlin J. held that the plaintiffs were entitled to recover the balance of the freight from the defendants.

**Devlin J**

The defendants' case in law is that since the plaintiffs performed the contract of carriage, evidenced by the bill of lading, in such a way as to infringe the Act of 1932, they committed an illegality which prevents them from enforcing the contract at all; the defendants say they were not obliged to pay any freight, and so cannot be sued for the unpaid balance. . . .

It is a misfortune for the defendants that the legal weapon which they are wielding is so much more potent than it need be to achieve their purpose. Believing, rightly or wrongly, that the plaintiffs have deliberately committed a serious infraction of the Act and one which has placed their property in jeopardy, the defendants wish to do no more than to take the profit out of the plaintiffs' dealing. But the principle which they invoke for this purpose cares not at all for the element of deliberation or for the gravity of the infraction, and does not adjust the penalty to the profits unjustifiably earned. The defendants cannot succeed unless they claim the right to retain the whole freight and to keep it whether the offence was accidental or deliberate, serious or trivial. The application of this principle to a case such as this is bound to lead to startling results. Mr Wilmers [counsel for the defendants] does not seek to avert his gaze from the wide consequences. A shipowner who accidentally overloads by a fraction of an inch will not be able to recover from any of the shippers or consignees a penny of the freight. There are numerous other illegalities which a ship might commit in the course of the voyage which would have the same effect. . . .

Mr Wilmers puts his case under three main heads. In the first place he submits that, notwithstanding that the contract of carriage between the parties was legal when made, the plaintiffs have performed it in an illegal manner by carrying the goods in a ship which was overloaded in violation of the statute. He submits as a general proposition that a person who performs a legal contract in an illegal manner cannot sue upon it, and he relies upon a line of authorities of which *Anderson Ltd. v. Daniel* [1924] 1 KB 138 is probably the best known. He referred particularly to the formulation of the principle by Atkin LJ *ibid* 149 in the following passage: 'The question of illegality in a contract generally arises in connexion with its formation, but it may also arise, as it does here, in connexion with its performance. In the former case, where the parties have agreed to something which is prohibited by Act of Parliament, it is indisputable that the contract is unenforceable by either party. And I think that it is equally unenforceable by the offending party where the illegality arises from the fact that the mode of performance adopted by the party performing it is in violation of some statute, even though the contract as agreed upon between the parties was capable of being performed in a perfectly legal manner.'

As an alternative to this general proposition and as a modification of it, Mr. Wilmers submits that a plaintiff cannot recover if, in the course of carrying out a legal contract made with a person of a class which it is the policy of a particular statute to protect, he commits a violation of that statute.

Secondly, he relies upon the well-known principle - most recently considered, I think, in *Marles v. Philip Trant & Sons* [1954] 1 QB 29 - that a plaintiff cannot recover money if in order to establish his claim to it, he has to disclose that he committed an illegal act. These plaintiffs, he submits, cannot obtain their freight unless they prove that they carried the goods safely to their destination, and they cannot prove that without disclosing that they carried them illegally in an overloaded ship.

Thirdly, he relies upon the principle that a person cannot enforce rights which result to him from his own crime. He submits that the criminal offence committed in this case secured to the plaintiffs a larger freight than they would have earned if they had kept within the law. A part of the freight claimed in this case is therefore a benefit resulting from the crime and in such circumstances the plaintiff cannot recover any part of it.

I am satisfied that Mr Wilmers's chief argument is based on a misconception of the principle applied in *Anderson Ltd. v. Daniel*, [1924] 1 KB 138 which I have already cited. In order to expose that misconception I must state briefly how that principle fits in with other principles relating to illegal contracts. There are two general principles. The first is that a contract which is entered into with the object of committing an illegal act is unenforceable. The application of this principle depends upon proof of the intent, at the time the contract was made, to break the law; if the intent is mutual the contract is not enforceable at all, and, if unilateral, it is unenforceable at the suit of the party who is proved to have it. This principle is not involved here. Whether or not the overloading was deliberate when it was done, there is no proof that it was contemplated when the contract of carriage was made. The second principle is that the court will not enforce a contract which is expressly or impliedly prohibited by statute. If the contract is of this class it does not matter what the intent of the parties is; if the statute prohibits the contract, it is unenforceable whether the parties meant to break the law or not. A significant distinction between the two classes is this. In the former class you have only to look and see what acts the statute prohibits; it does not matter whether or not it prohibits a contract; if a contract is deliberately made to do a prohibited act, that contract will be unenforceable. In the latter class, you have to consider not what acts the statute prohibits, but what contracts it prohibits; but you are not concerned at all with the intent of the parties; if the parties enter into a prohibited contract, that contract is unenforceable.

The principle enunciated by Atkin LJ *Ibid* 149 and cited above is an offshoot of the second principle that a prohibited contract will not be enforced. If the prohibited contract is an express one, it falls directly within the principle. It must likewise fall within it if the contract is implied. If, for example, an unlicensed broker sues for work and labour, it does not matter that no express contract is alleged and that the claim is based solely on the performance of the contract, that is to say, the work and labour done; it is as much unenforceable as an express contract made to fit the work done. The same reasoning must be applied to a contract which, though legal in form, is performed unlawfully. . . . But whether it is the terms of the contract or the performance of it that is called in question, the test is just the same: is the contract, as made or as performed, a contract that is prohibited by the statute?

Mr Wilmers's proposition ignores this test. On a superficial reading of *Anderson Ltd. v. Daniel* [1924] 1 KB 138 and the cases that followed and preceded it, judges may appear to be saying that it does not matter that the contract is itself legal, if something illegal is done under it. But that is an unconsidered interpretation of the cases. When fully considered, it is plain that they do not proceed upon the basis that in the course of performing a legal contract an

illegality was committed; but on the narrower basis that the way in which the contract was performed turned it into the sort of contract that was prohibited by the statute. . . .

Now this language - and the same sort of language is used in all the cases - shows that the question always is whether the statute meant to prohibit the contract which is sued upon. One of the tests commonly used, and frequently mentioned in the later cases, in order to ascertain the true meaning of the statute is to inquire whether or not the object of the statute was to protect the public or a class of persons, that is, to protect the public from claims for services by unqualified persons or to protect licensed persons from competition. Mr Wilmers (while saying that, if necessary, he would submit that the Act of 1932 was passed, *inter alia*, to protect those who had property at sea) was unable to explain the relevance of this consideration to his view of the law. If in considering the effect of the statute the only inquiry that you have to make is whether an act is illegal, it cannot matter for whose benefit the statute was passed; the fact that the statute makes the act illegal is of itself enough. But if you are considering whether a contract not expressly prohibited by the Act is impliedly prohibited, such considerations are relevant in order to determine the scope of the statute. . . .

The plaintiff does an illegal act, being one prohibited by the statute, but he does it in performance of a legal contract, since the statute is construed as prohibiting the act merely and not prohibiting the contract under which it is done. If in such a case it had been held that it did not matter whether the contract was legal or not since the mode of performing it was illegal, Mr Wilmers's argument would be well supported. But in fact the contrary has been held. I take as an example of cases of this type, *Wetherell v. Jones* (1832) 3 B & Ad 221. The plaintiff sued for the price of spirits sold and delivered. A statute of George IV provided that no spirits should be sent out of stock without a permit. The court held that the permit obtained by the plaintiff was irregular because of his own fault and that he was therefore guilty of a violation of the law, but that the statute did not prohibit the contract. Tenterden CJ stated the law as follows *Ibid* 225:

'Where a contract which a plaintiff seeks to enforce is expressly, or by implication, forbidden by the statute or common law, no court will lend its assistance to give it effect: and there are numerous cases in the books where an action on the contract has failed, because either the consideration for the promise or the act to be done was illegal, as being against the express provisions of the law, or contrary to justice, morality, and sound policy. But where the consideration and the matter to be performed are both legal, we are not aware that a plaintiff has ever been precluded from recovering by an infringement of the law, not contemplated by the contract, in the performance of something to be done on his part.'

The last sentence in this judgment is a clear and decisive statement of the law; it is directly contrary to the contention which Mr Wilmers advances, which I therefore reject both on principle and on authority.

So Mr Wilmers's wider proposition fails. Mr Roskill [counsel for the plaintiffs] is right in his submission that the determining factor is the true effect and meaning of the statute, and I turn therefore to consider Mr Wilmers's alternative proposition that the contract evidenced by the bill of lading is one that is made illegal by the Act of 1932. I have already indicated the basis of this argument, namely, that the statute being one which according to its preamble is passed to give effect to a convention 'for promoting the safety of life and property at sea,' it is therefore passed for the benefit of cargo owners among others. That this is an important consideration is certainly established by the authorities. But I follow the view of Parke B in *Cope v. Rowlands*, 2 M & W 149 . . . that it is one only of the tests. The fundamental question is whether the statute means to prohibit the contract. The statute is to be construed in the

ordinary way; one must have regard to all relevant considerations and no single consideration, however important, is conclusive.

Two questions are involved. The first - and the one which hitherto has usually settled the matter - is: does the statute mean to prohibit contracts at all? But if this be answered in the affirmative, then one must ask: does this contract belong to the class which the statute intends to prohibit? . . .

The relevant section of the Act of 1932, section 44, provides that the ship 'shall not be so loaded as to submerge' the appropriate loadline. It may be that a contract for the loading of the ship which necessarily has this effect would be unenforceable. It might be, for example, that the contract for bunkering at Port Everglades which had the effect of submerging the loadline, if governed by English law, would have been unenforceable. But an implied prohibition of contracts of loading does not necessarily extend to contracts for the carriage of goods by improperly loaded vessels. Of course, if the parties knowingly agree to ship goods by an overloaded vessel, such a contract would be illegal; but its illegality does not depend on whether it is impliedly prohibited by the statute, since it falls within the first of the two general heads of illegality I noted above where there is an intent to break the law. The way to test the question whether a particular class of contract is prohibited by the statute is to test it in relation to a contract made in ignorance of its effect.

In my judgment, contracts for the carriage of goods are not within the ambit of this statute at all. A court should not hold that any contract or class of contracts is prohibited by statute unless there is a clear implication, or 'necessary inference,' as Parke B put it, 2 M & W 159 that the statute so intended. If a contract has as its whole object the doing of the very act which the statute prohibits, it can be argued that you can hardly make sense of a statute which forbids an act and yet permits to be made a contract to do it; that is a clear implication. But unless you get a clear implication of that sort, I think that a court ought to be very slow to hold that a statute intends to interfere with the rights and remedies given by the ordinary law of contract. Caution in this respect is, I think, especially necessary in these times when so much of commercial life is governed by regulations of one sort or another, which may easily be broken without wicked intent. Persons who deliberately set out to break the law cannot expect to be aided in a court of justice, but it is a different matter when the law is unwittingly broken. To nullify a bargain in such circumstances frequently means that in a case - perhaps of such triviality that no authority would have felt it worth while to prosecute - a seller, because he cannot enforce his civil rights, may forfeit a sum vastly in excess of any penalty that a criminal court would impose; and the sum forfeited will not go into the public purse but into the pockets of someone who is lucky enough to pick up the windfall or astute enough to have contrived to get it. It is questionable how far this contributes to public morality. . . .

I turn now to Mr Wilmers's second point. He submitted that the plaintiffs could not succeed in a claim for freight without disclosing that they had committed an illegality in the course of the voyage; or, put another way, that part of the consideration for the payment of freight was the safe carriage of the goods, and therefore they must show that they carried the goods safely. In the passage I have quoted from the judgment in *Wetherell v. Jones*, 3 B & Ad 221. Tenterden CJ *ibid* 225 carefully distinguished between an infringement of the law in the performance of the contract and a case where 'the consideration and the matter to be performed' were illegal. There is a distinction there - of the sort I have just been considering - between a contract which has as its object the doing of the very act forbidden by the statute, and a contract whose performance involves an illegality only incidentally. It may be, therefore, that the second point is the first point looked at from another angle. However that may be, there is no doubt that if the plaintiffs cannot succeed in their claim for freight without showing that they carried the goods in an overloaded ship, they must fail.

But, in my judgment, the plaintiffs need show no more in order to recover their freight than that they delivered to the defendants the goods they received in the same good order and condition as that in which they received them. . . .

On Mr Wilmers's third point I take the law from the dictum in *Beresford v. Royal Insurance Co Ltd* [1938] AC 586 that was adopted and applied by Lord Atkin [1938] AC 586, 596: 'no system of jurisprudence can with reason include amongst the rights which it enforces rights directly resulting to the person asserting them from the crime of that person.' I observe in the first place that in the Court of Appeal in the same case Lord Wright [1937] 2 KB 197, 220 doubted whether this principle applied to all statutory offences. His doubt was referred to by Denning LJ in *Marles v. Philip Trant & Sons* [1954] 1 QB 29, 37. . . . The distinction is much to the point here. The Act of 1932 imposes a penalty which is itself designed to deprive the offender of the benefits of his crime. It would be a curious thing if the operation could be performed twice - once by the criminal law and then again by the civil. It would be curious, too, if in a case in which the magistrates had thought fit to impose only a nominal fine, their decision could, in effect, be overridden in a civil action. But the question whether the rule applies to statutory offences is an important one which I do not wish to decide in the present case. The dicta of Lord Wright [1937] 2 KB 197, 220 and Denning LJ [1954] 1 QB 29, 37 suggest that there are cases where its application would be morally unjustifiable; but it is not clear that they go as far as saying that the application would not be justified in law. I prefer, therefore, to deal with Mr Wilmers's submission in another way.

The rights which cannot be enforced must be those 'directly resulting' from the crime. That means, I think, that for a right to money or to property to be unenforceable the property or money must be identifiable as something to which, but for the crime, the plaintiff would have had no right or title. That cannot be said in this case. The amount of the profit which the plaintiffs made from the crime, that is to say, the amount of freight which, but for the overloading, they could not have earned on this voyage, was, as I have said, £2,295. The quantity of cargo consigned to the defendants was approximately 35 per cent. of the whole and, therefore, even if it were permissible to treat the benefit as being divisible pro rata over the whole of the cargo, the amount embodied in the claim against the defendants would not be more than 35 per cent. of £2,300. That would not justify the withholding of £2,000. The fact is that the defendants and another cargo owner have between them withheld money, not on a basis that is proportionate to the claim against them, but so as to wipe out the improper profit on the whole of the cargo. I do not, however, think that the defendants' position would be any better if they had deducted no more than the sum attributable to their freight on a pro rata basis. There is no warrant under the principle for a pro rata division; it would be just as reasonable to say that the excess freight should be deemed to attach entirely to the last 427 tons loaded, leaving the freight claim on all the rest unaffected. But in truth there is no warrant for any particular form of division. The fact is that in this type of case no claim or part of a claim for freight can be clearly identified as being the excess illegally earned.

In *Beresford v. Royal Insurance Co Ltd* [1938] AC 586 the court dismissed the claim of a personal representative who claimed on policies of life insurance which had matured owing to the assured committing suicide in circumstances that amounted to a crime. Mr Wilmers submitted that the only benefit which the assured or his estate derived from the claim was the acceleration of the policies and that notwithstanding that some of the policies had been in force for a considerable time and therefore, I suppose, had a surrender value before the suicide was committed, the plaintiff was not allowed to recover anything. So in the present case, he submits, the commission of the crime defeats the whole claim to freight notwithstanding that the earning of the greater part of it was irrespective of the crime.

The comparison does not seem to me to be just. In *Beresford v. Royal Insurance Co Ltd*, but for the crime committed by the assured, no part of the policy moneys could have been claimed in that form, that is to say, as money repayable on the happening of the event insured against, or at that time. That does not necessarily mean that, so far as public policy was concerned, the plaintiff could recover nothing. If the plaintiff, for example, had sued for the return of premiums, assuming the contract permitted it, I have not been referred to any observation in the case which would suggest that an action in that form would fail on the grounds of public policy. The claim which the court was considering under the policy depended entirely upon proof of death and the death was a crime. In the present case the right to claim freight from the defendants was not brought into existence by a crime; the crime affected only the total amount of freight earned by the ship.

The result is that there must be judgment for the plaintiffs for £2,000. But the defendants will not have fought the action altogether in vain if it brings to the attention of the competent authorities the fact that section 44 of the Act of 1932 is out of date and ought to be amended. I have already noted that for a similar offence a British master can be imprisoned and it must be very galling for those concerned to see a foreign master do the same thing without the law providing any effective deterrent.

## Commentary

The illegality at stake in this case is very different from that in issue in *Pearce v. Brooks* (below). Regulatory legislation of the type in issue in *St John Shipping Corporation* can be broken innocently in the course of the performance of a contract. Devlin J was acutely aware of the fact that such regulations can be broken innocently and he was anxious to avoid the conclusion that infringement of the relevant legislation would result in the inevitable unenforceability of the contract. There was no finding that the overloading in the case was in fact done innocently. Indeed, Devlin J stated that it was ‘not at all improbable’ that it was deliberate. But this was not a case in which the parties had entered into the contract with the object of committing an illegal act. As Devlin J pointed out, ‘whether or not the overloading was deliberate when it was done, there is no proof that it was contemplated when the contract of carriage was made.’ Should Devlin J have given greater consideration to the possibility that the overloading was deliberate? What would have been the outcome if it had been proved that the shipowners had deliberately overloaded the ship in order to increase their profits and, in doing so, had ignored the obvious dangers to the crew and the vessel? In such a case should the shipowners be deprived of their contractual right to recover freight? If the aim of the law is to discourage illegal activity is this not the very type of case in which contractual rights should be denied?

There were three strands to the reasoning of Devlin J. The first element was his conclusion that the statute did not prohibit the making of contracts for the carriage of goods. Its object was to impose a fine on those who violated its provisions and not to invalidate contracts. While it was true that Parliament had failed to increase the level of the fine in line with inflation that did not justify the court in refusing to enforce the contract. The inadequacy, if any, of the fine was a matter for Parliament to address, not the courts. The exercise in which Devlin J was engaged was one of statutory construction in which he sought to ascertain the effect of the statute on the contractual rights of the parties in the light of his view of the policy which underpinned the statute. The second point was that it was not necessary for the

plaintiffs to disclose their illegality in order to recover the freight. All that they had to do was to show that they had performed their contractual obligations by delivering the goods in accordance with the contract of carriage. The third point was the submission that the freight was the product of a benefit resulting from the crime and in such circumstances the plaintiff could not recover any part of the freight. Devlin J rejected this submission and, in doing so, distinguished the decision of the House of Lords in *Beresford v. Royal Insurance Co. Ltd.* [1938] AC 586. On the facts of the case no part of the excess freight could be identified with the fruits of the overloading.

The essence of the analysis of Devlin J is that it was the intention of Parliament to punish infringements of the statutory provisions by the imposition of a fine and not by invalidating contracts entered into in breach of them. As has been pointed out (*Chitty on Contracts* (33rd edn, 2018) para. 16-182

'The courts have . . . been reluctant to find contracts unenforceable because the illegality doctrine operates in an all or nothing way and there is no proportionality between the loss ensuing from non-enforcement and the breach of statute. This is to be contrasted with fines for criminal acts where some proportionality does pertain. . . . Thus, were the doctrine [of illegality] to have applied [in *St John Shipping Corporation*] it would have entitled the defendants to hold back the full freight which was 40 times the maximum fine for the offence of overloading. Coupled with this, non-enforcement may have the effect of punishing the offender twice where the statute contains its own penalty for breach.

The courts have also been sensitive to the fact that non-enforcement may also result in unjust enrichment to the party to the contract who has not performed his part of the bargain but who has benefited from the performance by the other party. As was stated by Devlin J in the *St John Shipping* case, non-enforcement of the contract may result in the forfeiting of a sum which 'will not go into the public purse but into the pockets of someone who is lucky enough to pick up the windfall or astute enough to have contrived to get it.'

---

***Archbolds (Freightage) Ltd v. S Spanglett Ltd***  
[1961] 1 QB 374, Court of Appeal

The defendants, who were furniture manufacturers in London, owned vehicles with 'C' licences, which permitted them to carry their own goods, but not the goods of others. The plaintiffs were carriers with offices in London and Leeds, whose vehicles carried 'A' licenses, enabling them to carry the goods of others as well as their own goods. One of the plaintiffs' employees in their London office arranged with a person from the defendants' office for the defendants to carry some goods for the plaintiffs to the plaintiffs' Leeds office. The plaintiffs believed that the defendants had 'A' licences for their vehicles and were not aware of the fact that the defendants' vehicles only had 'C' licenses. Having made his deliveries in Leeds, the defendants' driver, Mr Randall, told Mr Field, the plaintiffs' traffic manager in the Leeds office, that he had just brought a load for them from London and wished to take another load back to London. The driver arranged with the traffic manager to carry a load of whisky to London. That load of whisky was stolen as a result of the driver's negligence. The plaintiffs brought an action for damages against the defendants. The defendants argued that the plaintiffs were not entitled to recover damages because the contract was



illegal as a result of the fact that their van did not have an 'A' licence. The trial judge found for the plaintiffs. The Court of Appeal dismissed the defendants' appeal and held that the plaintiffs were not prevented from suing for damages as a result of the illegality because they did not know the vehicle only had a 'C' licence and, that being the case, the contract of carriage was not itself illegal under the relevant statute, nor was it *ex facie* illegal.

### **Pearce LJ** (set out the facts and continued)

It having been proved, therefore, that the plaintiffs were imposed on and believed that the goods could be lawfully carried on Randall's van, are they disentitled to sue? . . .

If a contract is expressly or by necessary implication forbidden by statute, or if it is *ex facie* illegal, or if both parties know that though *ex facie* legal it can only be performed by illegality or is intended to be performed illegally, the law will not help the plaintiffs in any way that is a direct or indirect enforcement of rights under the contract. And for this purpose both parties are presumed to know the law.

The first question, therefore, is whether this contract of carriage was forbidden by statute. The two cases on which the defendants mainly rely are *In re an Arbitration between Mahmoud and Ispahani* [1921] 2 KB 716 and *J. Dennis & Co Ltd v. Munn* [1949] 2 KB 327. In both those cases the plaintiffs were unable to enforce their rights under contracts forbidden by statute. In the former case the statutory order said:

'a person shall not . . . buy or sell . . . [certain] articles . . . except under and in accordance with the terms of a licence.'

In the latter case the statutory regulation provided

'Subject to the provisions of this regulation . . . the execution . . . of any operation specified . . . shall be unlawful except in so far as authorised.'

In neither case could the plaintiff bring his contract within the exception that alone would have made its subject-matter lawful, namely, by showing the existence of a licence. Therefore, the core of both contracts was the mischief expressly forbidden by the statutory order and the statutory regulation respectively. In *Mahmoud's* case the object of the order was to prevent (except under licence) a person buying and a person selling, and both parties were liable to penalties. A contract of sale between those persons was therefore expressly forbidden. In *Dennis's* case the object of the regulation was to prevent (except under licence) owners from performing building operations, and builders from carrying out the work for them. Both parties were liable to penalties and a contract between these persons for carrying out an unlawful operation would be forbidden by implication.

The case before us is somewhat different. The carriage of the plaintiffs' whisky was not as such prohibited; the statute merely regulated the means by which carriers should carry goods. Therefore this contract was not expressly forbidden by the statute. Was it then forbidden by implication? The Road and Rail Traffic Act, 1933, section 1, says:

'no person shall use a goods vehicle on a road for the carriage of goods . . . except under licence,'

and provides that such use shall be an offence. Did the statute thereby intend to forbid by implication all contracts whose performance must on all the facts (whether known or not) result in a contravention of that section? The plaintiffs' part of the contract could not constitute an illegal use of the vehicle by them since they were not 'using' the vehicle. If they were aware of the true facts they would, of course, be guilty of aiding and abetting the defendants, but if they acted in good faith they would not be guilty of any offence under the

statute: see *Davies, Turner & Co. Ltd. v. Brodie* [1954] 1 WLR 1364 and *Carterv. Mace* [1949] 2 All ER 714. In this case, therefore, the plaintiffs were not committing any offence.

In *St John Shipping Corporation v. Rank* [1957] 1 QB 267 Devlin J held that the plaintiffs were entitled to recover although there had been an infringement of a statute in the performance of a contract, but in that case the contract was legal when made. Though not directly applicable to the present case, it contains an observation (with which I entirely agree) on the point which arises here. He said ([1957] 1 QB 267, 287): 'For example, a person is forbidden by statute from using an unlicensed vehicle on the highway. If one asks oneself whether there is in such an enactment an implied prohibition of all contracts for the use of unlicensed vehicles, the answer may well be that there is, and that contracts of hire would be unenforceable. But if one asks oneself whether there is an implied prohibition of contracts for the carriage of goods by unlicensed vehicles or for the repairing of unlicensed vehicles or for the garaging of unlicensed vehicles, the answer may well be different. The answer might be that collateral contracts of this sort are not within the ambit of the statute.' In my judgment that distinction is valid.

The object of the Road and Rail Traffic Act, 1933, was not (in this connection) to interfere with the owner of goods or his facilities for transport, but to control those who provided the transport, with a view to promoting its efficiency. Transport of goods was not made illegal but the various licence holders were prohibited from encroaching on one another's territory, the intention of the Act being to provide an orderly and comprehensive service. Penalties were provided for those licence holders who went outside the bounds of their allotted spheres. These penalties apply to those using the vehicle but not to the goods owner. Though the latter could be convicted of aiding and abetting any breach, the restrictions were not aimed at him. Thus a contract of carriage was, in the sense used by Devlin J, 'collateral,' and it was not impliedly forbidden by the statute.

This view is supported by common sense and convenience. If the other view were held it would have far-reaching effects. For instance, if a carrier induces me (who am in fact ignorant of any illegality) to entrust goods to him and negligently destroys them, he would only have to show that (though unknown to me) his licence had expired, or did not properly cover the transportation, or that he was uninsured, and I should then be without a remedy against him. Or, again, if I ride in a taxicab and the driver leaves me stranded in some deserted spot, he would only have to show that he was (though unknown to me) unlicensed or uninsured, and I should be without remedy. This appears to me an undesirable extension of the implications of a statute. . . .

It is for the defendants to show that contracts by the owner for the carriage of goods are within the ambit of the implied prohibition of the Road and Rail Traffic Act, 1933. In my judgment they have not done so.

The next question is whether this contract though not forbidden by statute was *ex facie* illegal. Must any reasonable person on hearing the terms of the contract (which presumed knowledge of the law) realise that it was illegal? There is nothing illegal in its terms. Further knowledge, namely, knowledge of the fact that Randall's van was not properly licensed, would show that it could only be performed by contravention of the statute, but that does not make the contract *ex facie* illegal.

However, if both parties had that knowledge the contract would be unenforceable as being a contract which to their knowledge could not be carried out without a violation of the law: see *per* Lord Blackburn in *Waugh v. Morris* (1873) LR 8 QB 202, 208. But where one party is ignorant of the fact that will make the performance illegal, is it established that the innocent party cannot obtain relief against the guilty party? The case has been argued with skill and

care on both sides, and yet no case has been cited to us establishing the proposition that where a contract is on the face of it legal and is not forbidden by statute, but must in fact produce illegality by reason of a circumstance known to one party only, it should be held illegal so as to debar the innocent party from relief. In the absence of such a case I do not feel compelled to so unsatisfactory a conclusion, which would injure the innocent, benefit the guilty, and put a premium on deceit.

Such a conclusion (in cases like this where a contract is not forbidden by statute) can only derive from public policy. For the reasons given by Lord Wright above, an extension of the law in this direction would be more harmful than beneficial. No question of moral turpitude arises here. The alleged illegality is, so far as the plaintiffs were concerned, the permitting of their goods to be carried by the wrong carrier, namely, a carrier who unknown to them was not allowed by his licence to carry that particular class of goods. The plaintiffs were never in delicto since they did not know the vital fact that would make the performance of the contract illegal.

In my view, therefore, public policy does not constrain us to refuse our aid to the plaintiffs and they are therefore entitled to succeed. I would dismiss the appeal.

### Devlin LJ

The effect of illegality upon a contract may be threefold. If at the time of making the contract there is an intent to perform it in an unlawful way, the contract, although it remains alive, is unenforceable at the suit of the party having that intent; if the intent is held in common, it is not enforceable at all. Another effect of illegality is to prevent a plaintiff from recovering under a contract if in order to prove his rights under it he has to rely upon his own illegal act; he may not do that even though he can show that at the time of making the contract he had no intent to break the law and that at the time of performance he did not know that what he was doing was illegal. The third effect of illegality is to avoid the contract ab initio and that arises if the making of the contract is expressly or impliedly prohibited by statute or is otherwise contrary to public policy.

The defendants do not seek to bring this case under either of the first two heads. They cannot themselves enforce the contract because they intended to perform it unlawfully with a van that they knew was not properly licensed for the purpose: but that does not prevent the plaintiffs, who had no such intent and were not privy to it, from enforcing the contract. Nor can it be said that the plaintiffs committed any illegal act. To load a vehicle is not to use it on the road, which is what is forbidden; no doubt loading would be enough to constitute aiding and abetting if the plaintiffs knew of the defendants' purpose (*National Coal Board v. Gamble* [1959] 1 QB 11), but they did not.

So what the defendants say is that the contract is prohibited by the Road and Rail Traffic Act, 1933, s 1. In order to see whether the contract falls within the prohibition it is necessary to ascertain the exact terms of the contract and the exact terms of the prohibition. . . .

The statute does not expressly prohibit the making of any contract. The question is therefore whether a prohibition arises as a matter of necessary implication. It follows from the decision of this court in *Nash v. Stevenson Transport Ltd.* [1936] 2 KB 128 that a contract for the use of unlicensed vehicles is prohibited. . . .

On the other hand, it does not follow that because it is an offence for one party to enter into a contract, the contract itself is void. . . .

The general considerations which arise on this question were examined at length in *St John Shipping Corporation v. Joseph Rank Ltd.* [1957] 1 QB 267, 285 and Pearce LJ has set them out so clearly in his judgment in this case that I need add little to them. Fundamentally they are the same as those that arise on the construction of every statute; one must have

regard to the language used and to the scope and purpose of the statute. I think that the purpose of this statute is sufficiently served by the penalties prescribed for the offender; the avoidance of the contract would cause grave inconvenience and injury to innocent members of the public without furthering the object of the statute. Moreover, the value of the relief given to the wrongdoer if he could escape what would otherwise have been his legal obligation might, as it would in this case, greatly outweigh the punishment that could be imposed upon him, and thus undo the penal effect of the statute.

I conclude, therefore, that this contract was not illegal for the reason that the statute does not prohibit the making of a contract for the carriage of goods in unlicensed vehicles and this contract belongs to this class. I am able, therefore, to arrive at my judgment without an examination of the exact terms of the contract. It would have been natural to have begun by looking at the contract; I have not done so because it is doubtful whether the state of the pleadings permits a thorough examination. But as [counsel for the defendants' argument] turned upon its terms, I think that I should deal with them.

[he examined the terms of the contract and continued]

It is a familiar principle of law that if a contract can be performed in one of two ways, that is, legally or illegally, it is not an illegal contract, though it may be unenforceable at the suit of a party who chooses to perform it illegally. That statement of the law is meaningful if the contract is one which is by its terms open to two modes of performance; otherwise it is meaningless. Almost any contract - certainly any contract for the carriage of goods by road - can be performed illegally; any contract of carriage by road can be performed illegally simply by exceeding the appropriate speed limit. The error in the defendants' argument, I think, is that they are looking at the facts which determine their capacity to perform and not at the terms of the contract. Suppose that the contract were for a vehicle with an 'A' licence, or - what is substantially the same thing - for a specified vehicle warranted as holding an 'A' licence. That would not be an illegal contract for it would be a contract for the use of a licensed vehicle and not an unlicensed one. If those were the express terms of the contract, it would not be made illegal because all the carrier's vehicles, or the specified vehicle as the case might be, had 'C' licences. The most that that could show would be that the carrier might well be unable to perform his contract. Or suppose that the contract were for any 'A' vehicle owned by the defendant and the defendant had a fleet of five 'A' vehicles and five 'C' vehicles. That would be a legal contract and it would not be made illegal because, at the time when it was made, it was physically impossible for the defendant to get any of his 'A' vehicles to the loading place in time. If the contract is for a specified vehicle with an 'A' licence, loading to begin within a week, it is not illegal because when the contract was made the vehicle had no 'A' licence; one might be obtained in time and the court will not decide the question of legality by inquiring whether an 'A' licence could or could not have been obtained for it within the week. So in this case it is irrelevant to say that the van SXY902 had in fact not got an 'A' licence and could not conceivably have got one in time. The error in the defendants' argument is that they assume that because the parties were contracting about a specified vehicle and because that specified vehicle had in fact (a fact known to one party and not to the other) only a 'C' licence, therefore they were contracting about a vehicle with a 'C' licence. It is the terms of the contract that matter; the surrounding facts are irrelevant, save in so far as, being known to both parties, they throw light on the meaning and effect of the contract. The question is not whether the vehicle was in fact properly licensed but whether it was expressly or by implication in the contract described or warranted as properly licensed. If it was so described or warranted, then the legal position is, not that the contract could only be performed by a violation of the law, but

that unless it could be performed legally, it could not be performed at all. The fact that, as in this case, it may be known to one of the parties at the time of making the contract that he cannot perform it legally and therefore that it will inevitably be broken, does not make the contract itself illegal.

So the correct line of inquiry into the terms of the contract in this case should have been not as to whether it provided for performance by a specified vehicle or by any vehicle that the defendants chose to nominate, but as to whether the defendants warranted or agreed that the vehicle which was to do the work, whether a specified vehicle or any other, was legally fit for the service which it had to undertake, that is, that it had an 'A' licence.

I think there is much to be said for the argument that in a case of this sort there is, unless the circumstances exclude it, an implied warranty that the van is properly licensed for the service for which it is required. It would be unreasonable to expect a man when he is getting into a taxicab to ask for an express warranty from the driver that his cab was licensed; the answer, if it took any intelligible form at all, would be to the effect that it would not be on the streets if it were not. The same applies to a person who delivers goods for carriage by a particular vehicle; he cannot be expected to examine the road licence to see if it is in order. But the issue of warranty was not raised in the pleadings or at the trial and so I think it is preferable to decide this case on the broad ground which Pearce LJ has adopted and with which, for the reasons I have given, I agree.

There are many pitfalls in this branch of the law. If, for example, Mr Field had observed that the van had a 'C' licence and said nothing, he might be said to have accepted a mode of performance different from that contracted for and so varied the contract and turned it into an illegal one: see *St John Shipping Corporation v. Joseph Rank Ltd* [1957] 1 QB 267, 283, 284 where that sort of point was considered. Or, to take another example, if a statute prohibits the sale of goods to an alien, a warranty by the buyer that he is not an alien will not save the contract. That is because the terms of the prohibition expressly forbid a sale to an alien; consequently, the question to be asked in order to see whether the contract comes within the prohibition is whether the buyer is in fact an alien, not whether he represented himself as one. *In re Mahmoud* [1921] 2 KB 716 is that sort of case. The statute forbade the buying and selling of certain goods between unlicensed persons. The buyer falsely represented himself as having a licence. It is not said that he so warranted but, if he had, it could have made no difference. Once the fact was established that he was an unlicensed person the contract was brought within the category of those that were prohibited. *Strongman v. Sincock* [1955] 2 QB 525 exemplifies another sort of difficulty. It was an action brought by a builder against a building owner to recover the price of building work done. The statute forbade the execution of building operations without a licence. The building owner expressly undertook to obtain the necessary licence and failed to do so; and it was held that the builder could not recover. The builder, I dare say, might have contended that, having regard to the undertaking, the contract he made was for licensed operations and therefore legal. But unfortunately he had himself performed it illegally by building without a licence and he could not recover without relying on his illegal act because he was suing for money for work done. The undertaking might make the contract legal but not the operations. All these cases are distinguishable from the present one, where the contract is not within the prohibition and the plaintiffs themselves committed no illegal act and did not aid or abet the defendants. Apart from the pleading point, it might not matter if the last two cases were not distinguishable, since the plaintiffs could obtain damages for breach of the warranty as in *Strongman v. Sincock* [1955] 2 QB 525.

**Sellers LJ** delivered a concurring judgment.

## Commentary

*Archbolds* is a good example of illegality being taken as a technical defence by a defendant. Given that the defendants were responsible for using an unlicensed vehicle and that the plaintiffs were wholly unaware of the illegality, the defence was wholly lacking in merit. As Professor Buckley has pointed out ('Illegality in Contract and Conceptual Reasoning' (1983) 12 *Anglo-American Law Review* 280, 281-282):

'To an action for breach of contract the defendants argued that since the contract had been performed by them in an unlicensed vehicle even the innocent plaintiffs were precluded by illegality from suing on it. The trial judge and the Court of Appeal held that the contract itself did not implicitly identify a particular van for use in its performance and that the agreement was therefore not one which, contrary to the submission of the defendants, was incapable from the outset of legal performance. This in itself should have been sufficient to conclude the case in favour of the plaintiffs. Unfortunately, however, a substantial part of both of the two reasoned judgments delivered in the Court of Appeal was in fact taken up with a separate and largely irrelevant question: whether the Road and Rail Act 1933, which imposed the licensing requirement, was intended to prohibit contracts for the carriage of goods. Not surprisingly the conclusion was reached that it was not and the plaintiffs succeeded in their claim. The only effect, if any, which the Act could plausibly be said to have had upon the enforceability of contracts would have been to render contracts for the *hire* of unlicensed vehicles unenforceable by either party, or contracts for the carriage of goods unenforceable by the guilty party if performed in an unlicensed vehicle.

The proposition that legislation which did not overtly deal with contracts at all could have prevented a wholly innocent party from suing on a contract because of illegal performance by the *other* party is so bizarre that it is difficult to believe that it could have been seriously argued, let alone considered at some length by the Court of Appeal, had it not been for shadows cast by the notion of the 'illegal contract', enforceable by neither party regardless of the issues.'

One other point raised by Devlin LJ in his judgment is the question whether or not the defendants impliedly warranted that the van was properly licensed for the service for which it was required. This is a device that has been used by the courts to give an innocent party a remedy in a case in which the contract itself cannot be enforced as a result of the illegality. Notwithstanding the unenforceability of the contract, the claimant may be able to obtain a remedy in damages by suing upon the collateral warranty (see, for example, *Strongman (1945) Ltd v. Sincock* [1955] 2 QB 525, discussed by Devlin LJ above).

## 4. RESTRAINT OF TRADE

The courts have long exercised a jurisdiction to strike down covenants which are in unreasonable restraint of trade. The justifications for the existence of the doctrine, and its scope, have been the subject of some controversy. Consider the following extract (SA Smith, 'Reconstructing Restraint of Trade' (1995) 15 *OJLS* 565–567):

The doctrine of restraint of trade is a strange beast. Its role in contract law is traditionally understood to be that of denying validity to contracts that unduly restrain the freedom of one or both of the contracting parties. The doctrine appears to place non-procedural limitations

© Ewan McKendrick 2020.

on freedom of contract and, moreover, to place these limitations because of a concern for the contracting parties' freedom. A concern for freedom is being used, it appears, to limit freedom . . .

Until relatively recently, it was thought that only three types of contractual provisions could be scrutinised under restraint of trade law: (1) post-employment covenants . . . ; (2) sale of business covenants . . . ; and (3) horizontal restraints (restraints operating between competitors, such as an agreement to divide up the market..). This neat categorisation was ended in *Petrofina v. Martin*, where Lord Denning held that a solus agreement . . . fell within the doctrine. The categories of restraint of trade, Lord Denning said, 'are not closed'. Subsequent decisions extended the doctrine to other types of exclusive dealing arrangements and to 'exclusive services' arrangements (such as the contract in *Schroeder* [below] requiring a songwriter to hand over all his compositions to one publisher for a period of years).

The starting point for any consideration of the law relating to restraint of trade is the following passage from the judgment of Lord Macnaghten in *Nordenfelt v. Maxim Nordenfelt* [1894] AC 535, 565:

The public have an interest in every person's carrying on his trade freely: so has the individual. All interference with individual liberty of action in trading, and all restraints of trade of themselves, if there is nothing more, are contrary to public policy, and therefore void. That is the general rule. But there are exceptions: restraints of trade and interference with individual liberty of action may be justified by the special circumstances of a particular case. It is a sufficient justification, and indeed it is the only justification, if the restriction is reasonable—reasonable, that is, in reference to the interests of the parties concerned and reasonable in reference to the interests of the public, so framed and so guarded as to afford adequate protection to the party in whose favour it is imposed, while at the same time it is in no way injurious to the public.

From this quotation, and the passage from Professor Smith's article, it can be seen that there are three principal elements to a restraint of trade claim. The first relates to the scope of the doctrine: to which clauses or contracts does the doctrine apply? As Professor Smith makes clear, the doctrine classically applied to three particular types of contractual provisions but its scope has been extended into certain types of exclusive dealing arrangements with the result that the precise scope of the doctrine is now rather uncertain. Secondly, a clause that falls within the scope of the doctrine can be upheld if it is reasonable as between the parties and, thirdly, if it is reasonable in the public interest. The courts tend to place more emphasis on the requirement that the restraint be reasonable as between the parties than they do on the public interest requirement.

The operation of the doctrine of restraint of trade can be illustrated in its application to post-employment covenants. An employer can validly insert a post-employment restraint in a contract of employment but, in order to do so, he must demonstrate that the restraint is a reasonable one. The reasonableness requirement involves consideration of a number of issues. First, the restraint must seek to protect a legitimate interest of the employer (*Fitch v. Dewes* [1921] 2 AC 158). An employer does not have *carte blanche* to restrain the future employment prospects of his employees. In particular, an employer cannot legitimately restrain an employee from making use of his own skills and experience elsewhere. But he does have an interest in restraining an employee from making use of confidential information and trade secrets which he has acquired in the course of his employment and from soliciting customers of the employer. The extent to which information is confidential and hence capable of legitimate protection by a restraint of trade clause can be a difficult matter.

© Ewan McKendrick 2020.

Secondly, the restraint must be reasonable in terms of its geographical scope (*Forster and Sons v. Suggett* (1918) 35 TLR 87). An employer who runs a small business in a village cannot generally impose a nationwide restraint on a former employee. The restraint must be proportionate to the nature of the employer's business. Thirdly, the restraint must be reasonable in terms of its length. An indefinite restraint is highly unlikely to be reasonable, except in relation to the use of confidential information. The length of the restraint should be related to the interest that the employer is seeking to protect. An employer can restrain an employee from making use of confidential information for a far longer period of time than he can restrain an employee from soliciting customers. Fourthly, the restraint must be reasonable in relation to the nature of the employment in issue. The more senior the employee, the more likely it is that he will be the subject of a legitimate restraint. A restraint which purports to prevent the employee from taking up employment in an area of business that is unrelated to the employer's business is less likely to pass the reasonableness test (unless the restraint relates to the use by the employee of confidential information). Finally, the restraint must be reasonable in the public interest but the courts tend to be slow to invoke public interest considerations in these cases (but see *Wyatt v. Kreglinger and Fernau* [1933] 1 KB 793). In most cases the vital issue is whether or not the restraint is reasonable as between the employer and the employee.

A case which illustrates the application of the restraint of trade doctrine to post-employment covenants is:

---

***Mason v. Provident Clothing & Supply Co Ltd***  
[1913] AC 724, House of Lords

The facts of the case are set out in the judgment of Lord Moulton. The clause that was in issue between the parties was clause 8 which was in the following terms:

'And in consideration of the premises the said William Milne Mason hereby agrees that he shall not within three years after the termination of his engagement and services with the company be in the employ of, or be engaged in any manner whatsoever whether on his own account, or as partner with, or agent, or manager, or assistant, for, any person or persons, firm or firms, company or companies, carrying on or engaged in the same or a similar business to that of "The Provident Clothing and Supply Co Ltd" carried on as aforesaid or be engaged by, or assist or help (either directly or indirectly) any person or persons who shall be employed (whether for remuneration or not) by any person or persons, firm or firms, company or companies, carrying on the same or a similar business as aforesaid, or who shall be assisting or helping (either directly or indirectly) in the carrying on of the same or a similar business, or assist or help any one in the formation of such a business, society or club as aforesaid within twenty-five miles of London aforesaid where the company carry on business or within twenty-five miles of any place where the said William Milne Mason shall have been employed by the company at any time during the continuance of this agreement. And if the said William Milne Mason shall be engaged as aforesaid he shall forfeit to the company the sum of twenty-five pounds by way of liquidated damages, and not as a penalty.'

**Lord Moulton**

The law as to covenants in restraint of trade was so carefully and authoritatively formulated in this House in the *Nordenfelt Case* [1894] AC 535 that I do not think it necessary to discuss



the numerous authorities cited in the course of the argument in order to ascertain what is the critical question which the Court ought to put to itself in such a case as this. It is as follows: Are the restrictions which the covenant imposes upon the freedom of action of the servant after he has left the service of the master greater than are reasonably necessary for the protection of the master in his business?

The first task of the Court, therefore, is to ascertain with due particularity the nature of the master's business and of the servant's employment therein. The facts are not in dispute. The business of the respondents consists in inducing persons to become so-called "members", i.e., to subscribe for checks of various face values, say, for instance, of a value of 1l. These checks are paid for gradually by instalments at certain due dates, but they are delivered to the member when only a certain proportion of their face value has been paid by him, say, for instance, when 3s. has been paid on a 1l. check. So as soon as the check is received it is available for purchasing goods to its full face value, the company being answerable to the vendor for the price of the goods purchased, and itself collecting the instalments payable by the member. A list of firms willing to sell goods on these terms is set out in a printed list given to the members, and is therefore a matter as to which there is no secrecy, and the profits of the company are derived from the discounts given to them by the vendors of the goods.

The nature of the employment of the appellant in this business was solely to obtain members and collect their instalments. A small district in London was assigned to him, which he canvassed and in which he collected the payments due, and outside that small district he had no duties. His employment was therefore that of a local canvasser and debt collector, and nothing more.

Such being the nature of the employment, it would be reasonable for the employer to protect himself against the danger of his former servant canvassing or collecting for a rival firm in the district in which he had been employed. If he were permitted to do so before the expiry of a reasonably long interval he would be in a position to give to his new employer all the advantages of that personal knowledge of the inhabitants of the locality, and more especially of his former customers, which he had acquired in the service of the respondents and at their expense. Against such a contingency the master might reasonably protect himself, but I can see no further or other protection which he could reasonably demand. If the servant is employed by a rival firm in some district which neither includes that in which he formerly worked for the respondents, nor is immediately adjoining thereto, there is no personal knowledge which he has acquired in his former master's service which can be used to that master's prejudice. The respondents would be in no different position from that in which they would be if the appellant had acquired his experience in the service of some other company carrying on a like business. These, then, being the limits of the protection which the master might reasonably insist on, I turn to the covenant in order to see whether it exceeds these limits. That covenant is admittedly difficult to construe, and, moreover, it is, in my opinion, vague by reason of the extraordinary generality of the language employed. But at all events it prohibits the appellant from entering into a similar employment within twenty-five miles 'of London in the county of Middlesex' for a period of three years after leaving the respondents' service. Such an area must include something like six million persons, that is to say, that on a moderate estimate it is an area a thousand times as great as the district assigned to him when in the respondents' service. Considering the strictly local character of the employment, I have no hesitation in saying that I should be prepared to hold that such an area is very far greater than could be reasonably required for the protection of his former employers.

But this is but a small portion of the restrictions imposed by the covenant. It is very arguable that it prohibits him entering into the employ of any one carrying on a similar business without any limitations of area. But assuming in favour of the respondents that we ought to give it the more limited construction which was evidently put upon it at the trial, and to which

the evidence was directed, it restrains him for three years from entering into the employ of any firm which carries on a similar business within twenty- five miles of 'London in the county of Middlesex', wherever it be that his employment is located. To my mind, the employment of the appellant is in respect of its local character analogous to a milk-walk, where the servant is employed in distributing his master's goods in a certain defined district and not otherwise, and the portion of the covenant with which I am now dealing would amount in the case of a man so employed to prohibiting him from entering into the service of any milk distributing company that had a place of business within twenty-five miles of his former milk-walk no matter where it was that they proposed to employ him.

But even now we have not exhausted the extravagances of this restrictive covenant. Under it the appellant must not for a like period 'be engaged by or assist or help (either directly or indirectly) any person or persons who shall be employed (whether for remuneration or not) by any person or person, firm or firms, company or companies carrying on the same or a similar business as aforesaid, or who shall be assisting or helping either directly or indirectly in the carrying on of the same or a similar business'.

It is difficult to construe with any certainty words which are so intentionally wide and general. I doubt whether a covenant that is so intentionally unreasonable merits even the benefit of the general rule of construction that a Court should, if possible, construe language so as to give a reasonable meaning to the document. But however we construe it, the covenant is out of all measure wider than anything that can reasonably be required for the protection of the respondents in their business, and therefore the covenant is void in law and will not be enforced by the Courts.

It was suggested in the argument that even if the covenant was, as a whole, too wide, the Court might enforce restrictions which it might consider reasonable (even though they were not expressed in the covenant), provided they were within its ambit. My Lords, I do not doubt that the Court may, and in some cases will, enforce a part of a covenant in restraint of trade, even though taken as a whole the covenant exceeds what is reasonable. But, in my opinion, that ought only to be done in cases where the part so enforceable is clearly severable, and even so only in cases where the excess is of trivial importance, or merely technical, and not a part of the main purport and substance of the clause. It would in my opinion be pessimi exempli<sup>2</sup> if, when an employer had exacted a covenant deliberately framed in unreasonably wide terms, the Courts were to come to his assistance and, by applying their ingenuity and knowledge of the law, carve out of this void covenant the maximum of what he might validly have required. It must be remembered that the real sanction at the back of these covenants is the terror and expense of litigation, in which the servant is usually at a great disadvantage, in view of the longer purse of his master. It is sad to think that in this present case this appellant, whose employment is a comparatively humble one, should have had to go through four Courts before he could free himself from such unreasonable restraints as this covenant imposes, and the hardship imposed by the exaction of unreasonable covenants by employers would be greatly increased if they could continue the practice with the expectation that, having exposed the servant to the anxiety and expense of litigation, the Court would in the end enable them to obtain everything which they could have obtained by acting reasonably. It is evident that those who drafted this covenant aimed at making it a penal rather than a protective covenant, and that they hoped by means of it to paralyse the earning capabilities of the man if and when he left their service, and were not thinking of what would be a reasonable protection to their business, and having so acted they must take the consequences.

**Viscount Haldane LC, Lord Dunedin, and Lord Shaw of Dunfermline** delivered concurring judgments.

<sup>2</sup> A dangerous precedent.

## Commentary

*Mason* demonstrates the need to exercise great care when drafting restraint clauses. The temptation to draft widely must be resisted because the broader the clause, the less likely it is that it will pass the reasonableness test. Further the last paragraph of Lord Moulton's judgment demonstrates the unwillingness of the courts to re-write invalid restraints. While there is a doctrine of severance (below) it operates within very narrow limits.

A similar analysis to that conducted in the context of post-employment restraints is carried out in relation to restraint of trade covenants inserted in contracts for the sale of a business. The purchaser of the business must demonstrate that he has an interest which is capable of protection. This is generally not a difficult requirement to satisfy. A purchaser of a business will generally buy the goodwill of the business and so can take steps to protect that goodwill by, for example, restraining the vendor from soliciting his former customers. The purchaser is entitled to take steps to protect the value of the goodwill which he has purchased. As in the case of post-employment restraints, the restraint must be reasonable in terms of its geographical area, duration, and scope (*Nordenfelt v. Maxim Nordenfelt* [1894] AC 535). It must also be reasonable in the public interest, although, once again, the courts have been reluctant to place much reliance (at least overtly) upon public interest considerations. The primary focus is upon the reasonableness of the clause as between the parties.

The courts have also experienced some difficulty in ascertaining the scope of the doctrine of restraint of trade. This section will conclude with a consideration of two decisions of the House of Lords in which the principal issue was whether or not the doctrine of restraint of trade applied to exclusive dealing agreements. At this point we begin to enter into the regulation of anti-competitive agreements. The principal role in the regulation of such agreements is played by the Competition Act 1998.

But the doctrine of restraint of trade retains a role. In the two cases that follow the House of Lords held that the doctrine of restraint of trade applied to an exclusive dealing agreement and that the restraints were, with one exception, unreasonable.

---

### ***Esso Petroleum Co Ltd v. Harper's Garage (Stourport) Ltd*** [1968] AC 269, House of Lords

The respondent company owned and operated two garages. The first was the Mustow Green Garage near Kidderminster and the second was the Corner Garage, Stockport. It entered into two agreements (known as 'solus agreements') with the appellants, Esso, under which it bound itself to sell Esso petrol and no other type of petrol at its garages. In the case of the Mustow Green Garage the agreement was to remain in force for four years and five months, while the duration of the agreement relating to the Corner Garage was stated to be 21 years. In the case of the Corner Garage there was also a mortgage between the parties as security for the money lent to the respondents by Esso.

When cheaper petrol came on to the market the respondents began to sell it and stopped selling Esso petrol. Esso accordingly sought injunctions to restrain the respondents from buying petrol for resale at their garages from anyone other than themselves. The respondents challenged the validity of the solus agreements on the basis that they were in unreasonable restraint of trade. Esso submitted that the ties were not in restraint of trade but that, if they were, they were nevertheless valid and reasonable. The House of Lords held that the ties were subject to the restraint of trade doctrine and that, while

the tie applicable to the Mustow Green Garage was reasonable, the tie applicable to the Corner Garage was not.

**Lord Reid** [set out the facts and continued]

So I can now turn to the first question in this appeal—whether this agreement is to be regarded in law as an agreement in restraint of trade. The law with regard to restraint of trade is of ancient origin. There are references to it in the Year Books and it seems to have received considerable attention in the time of Queen Elizabeth I. But the old cases lie within a narrow compass. It seems to have been common for an apprentice or a craftsman to agree with his master that he would not compete with him after leaving his service, and also for a trader who sold his business to agree that he would not thereafter compete with the purchaser of his business. But no early case was cited which did not fall within one or other of these categories. And even in recent times there have been surprisingly few reported cases falling outside these categories in which restraint of trade has been pleaded: we were informed by counsel that there are only about 40 English cases which can be traced. On the other hand, there is an immense body of authorities with regard to the two original categories. I have not found it an easy task to determine how far principles developed for the original categories have been or should be extended.

The most general statement with regard to restraint of trade is that of Lord Parker in *Attorney-General of the Commonwealth of Australia v. Adelaide Steamship Co Ltd* [1913] AC 781, 794 (PC). He said:

‘Monopolies and contracts in restraint of trade have this in common, that they both, if enforced, involve a derogation from the common law right in virtue of which any member of the community may exercise any trade or business he pleases and in such manner as he thinks best in his own interests.’

But that cannot have been intended to be a definition: all contracts in restraint of trade involve such a derogation but not all contracts involving such a derogation are contracts in restraint of trade. Whenever a man agrees to do something over a period he thereby puts it wholly or partly out of his power to ‘exercise any trade or business he pleases’ during that period. He may enter into a contract of service or may agree to give his exclusive services to another: then during the period of the contract he is not entitled to engage in other business activities. But no one has ever suggested that such contracts are in restraint of trade except in very unusual circumstances . . .

In [t]he leading case of *Nordenfelt v. Maxim Nordenfelt Guns & Ammunition Co Ltd* [1894] AC 535 . . . Lord Macnaghten . . . only had in mind the two original kinds of case. There was no need in *Nordenfelt’s* case to attempt to define other classes of case to which the doctrine of restraint would apply.

If a contract is within the class of contracts in restraint of trade the law which applies to it is quite different from the law which applies to contracts generally. In general unless a contract is vitiated by duress, fraud or mistake its terms will be enforced though unreasonable or even harsh and unconscionable, but here a term in restraint of trade will not be enforced unless it is reasonable. And in the ordinary case the court will not remake a contract: unless in the special case where the contract is severable, it will not strike out one provision as unenforceable and enforce the rest. But here the party who has been paid for agreeing to the restraint may be unjustly enriched if the court holds the restraint to be too wide to be enforceable and is unable to adjust the consideration given by the other party.

It is much too late now to say that this rather anomalous doctrine of restraint of trade can be confined to the two classes of case to which it was originally applied. But the cases outside these two classes afford little guidance as to the circumstances in which it should be applied.

In some it has been assumed that the doctrine applies and the controversy has been whether the restraint was reasonable. And in others where one might have expected the point to be taken it was not taken, perhaps because counsel thought that there was no chance of the court holding that the restraint was too wide to be reasonable.

[he reviewed the case-law and continued]

The main argument submitted for the appellant on this matter was that restraint of trade means a personal restraint and does not apply to a restraint on the use of a particular piece of land. Otherwise, it was said, every covenant running with the land which prevents its use for all or for some trading purposes would be a covenant in restraint of trade and therefore unenforceable unless it could be shown to be reasonable and for the protection of some legitimate interest. It was said that the present agreement only prevents the sale of petrol from other suppliers on the site of the Mustow Green Garage: it leaves the respondents free to trade anywhere else in any way they choose. But in many cases a trader trading at a particular place does not have the resources to enable him to begin trading elsewhere as well, and if he did he might find it difficult to find another suitable garage for sale or to get planning permission to open a new filling station on another site. As the whole doctrine of restraint of trade is based on public policy its application ought to depend less on legal niceties or theoretical possibilities than on the practical effect of a restraint in hampering that freedom which it is the policy of the law to protect.

It is true that it would be an innovation to hold that ordinary negative covenants preventing the use of a particular site for trading of all kinds or of a particular kind are within the scope of the doctrine of restraint of trade. I do not think they are. Restraint of trade appears to me to imply that a man contracts to give up some freedom which otherwise he would have had. A person buying or leasing land had no previous right to be there at all, let alone to trade there, and when he takes possession of that land subject to a negative restrictive covenant he gives up no right or freedom which he previously had . . . . In the present case the respondents before they made this agreement were entitled to use this land in any lawful way they chose, and by making this agreement they agreed to restrict their right by giving up their right to sell there petrol not supplied by the appellants.

In my view this agreement is within the scope of the doctrine of restraint of trade as it had been developed in English law. Not only have the respondents agreed negatively not to sell other petrol but they have agreed positively to keep this garage open for the sale of the appellants' petrol at all reasonable hours throughout the period of the tie. It was argued that this was merely regulating the respondent's trading and rather promoting than restraining his trade. But regulating a person's existing trade may be a greater restraint than prohibiting him from engaging in a new trade. And a contract to take one's whole supply from one source may be much more hampering than a contract to sell one's whole output to one buyer. I would not attempt to define the dividing line between contracts which are and contracts which are not in restraint of trade, but in my view this contract must be held to be in restraint of trade. So it is necessary to consider whether its provisions can be justified . . .

Where two experienced traders are bargaining on equal terms and one has agreed to a restraint for reasons which seem good to him the court is in grave danger of stultifying itself if it says that it knows that trader's interest better than he does himself. But there may well be cases where, although the party to be restrained has deliberately accepted the main terms of the contract, he has been at a disadvantage as regards other terms: for example where a set of conditions has been incorporated which has not been the subject of negotiation—there the court may have greater freedom to hold them unreasonable.

I think that in some cases where the court has held that a restraint was not in the interests of the parties it would have been more correct to hold that the restraint was against the public

interest . . . whether or not a restraint is in the personal interests of the parties, it is I think well established that the court will not enforce a restraint which goes further than affording adequate protection to the legitimate interests of the party in whose favour it is granted. This must I think be because too wide a restraint is against the public interest. It has often been said that a person is not entitled to be protected against mere competition. I do not find that very helpful in a case like the present. I think it better to ascertain what were the legitimate interests of the appellants which they were entitled to protect and then to see whether these restraints were more than adequate for that purpose.

What were the appellants' legitimate interests must depend largely on what was the state of affairs in their business and with regard to the distribution and sale of petrol generally. And those are questions of fact to be answered by evidence or common knowledge. In the present case restraint of trade was not pleaded originally and the appellants only received notice that it was to be raised a fortnight before the trial. They may have been wise in not seeking a postponement of the trial when the pleadings were amended. But the result has been that the evidence on this matter is scanty. I think however that it is legitimate to supplement it from the considerable body of reported cases regarding solus agreements and from the facts found in the Report of the Monopolies Commission of July, 1965.

When petrol rationing came to an end in 1950 the large producers began to make agreements, now known as solus agreements, with garage owners under which the garage owner, in return for certain advantages, agreed to sell only the petrol of the producer with whom he made the agreement. Within a short time three-quarters of the filling stations in this country were tied in that way and by the dates of the agreements in this case over 90 per cent. had agreed to ties. It appears that the garage owners were not at a disadvantage in bargaining with the large producing companies as there was intense competition between these companies to obtain these ties. So we can assume that both the garage owners and the companies thought that such ties were to their advantage. And it is not said in this case that all ties are either against the public interest or against the interests of the parties. The respondents' case is that the ties with which we are concerned are for too long periods. The advantage to the garage owner is that he gets a rebate on the wholesale price of the petrol which he buys and also may get other benefits or financial assistance. The main advantages for the producing company appear to be that distribution is made easier and more economical and that it is assured of a steady outlet for its petrol over a period. As regards distribution, it appears that there were some 35,000 filling stations in this country at the relevant time, of which about a fifth were tied to the appellants. So they only have to distribute to some 7,000 filling stations instead of to a very much larger number if most filling stations sold several brands of petrol. But the main reason why the producing companies want ties for five years and more, instead of ties for one or two years only, seems to be that they can organise their business better if on the average only one-fifth or less of their ties come to an end in any one year. The appellants make a point of the fact that they have invested some £200 millions in refineries and other plant and that they could not have done that unless they could foresee a steady and assured level of sales of their petrol. Most of their ties appear to have been made for periods of between five and 20 years. But we have no evidence as to the precise additional advantage which they derive from a five-year tie as compared with a two-year tie or from a 20-year tie as compared with a five-year tie.

The Court of Appeal held that these ties were for unreasonably long periods. They thought that, if for any reason the respondents ceased to sell the appellants' petrol, the appellants could have found other suitable outlets in the neighbourhood within two or three years. I do not think that that is the right test. In the first place there was no evidence about this and I do not think that it would be practicable to apply this test in practice. It might happen

that when the respondents ceased to sell their petrol, the appellants would find such an alternative outlet in a very short time. But, looking to the fact that well over 90 per cent. of existing filling stations are tied and that there may be great difficulty in opening a new filling station, it might take a very long time to find an alternative. Any estimate of how long it might take to find suitable alternatives for the respondents' filling stations could be little better than guesswork.

I do not think that the appellants' interest can be regarded so narrowly. They are not so much concerned with any particular outlet as with maintaining a stable system of distribution throughout the country so as to enable their business to be run efficiently and economically. In my view there is sufficient material to justify a decision that ties of less than five years were insufficient, in the circumstances of the trade when these agreements were made, to afford adequate protection to the appellants' legitimate interests. And if that is so I cannot find anything in the details of the Mustow Green agreement which would indicate that it is unreasonable. It is true that if some of the provisions were operated by the appellants in a manner which would be commercially unreasonable they might put the respondents in difficulties. But I think that a court must have regard to the fact that the appellants must act in such a way that they will be able to obtain renewals of the great majority of their very numerous ties, some of which will come to an end almost every week. If in such circumstances a garage owner chooses to rely on the commercial probity and good sense of the producer, I do not think that a court should hold his agreement unreasonable because it is legally capable of some misuse. I would therefore allow the appeal as regards the Mustow Green agreement.

But the Corner Garage agreement involves much more difficulty. Taking first the legitimate interests of the appellants, a new argument was submitted to your Lordships that, apart from any question of security for their loan, it would be unfair to the appellants if the respondents, having used the appellants' money to build up their business, were entitled after a comparatively short time to be free to seek better terms from a competing producer. But there is no material on which I can assess the strength of this argument and I do not find myself in a position to determine whether it has any validity. A tie for 21 years stretches far beyond any period for which developments are reasonably foreseeable. Restrictions on the garage owner which might seem tolerable and reasonable in reasonably foreseeable conditions might come to have a very different effect in quite different conditions: the public interest comes in here more strongly. And, apart from a case where he gets a loan, a garage owner appears to get no greater advantage from a 20-year tie than he gets from a five-year tie. So I would think that there must at least be some clearly established advantage to the producing company—something to show that a shorter period would not be adequate—before so long a period could be justified. But in this case there is no evidence to prove anything of the kind. And the other material which I have thought it right to consider does not appear to me to assist the appellant here. I would therefore dismiss the appeal as regards the Corner Garage agreement.

### Lord Wilberforce

The doctrine of restraint of trade (a convenient, if imprecise, expression which I continue to use) is one which has throughout the history of its subject-matter been expressed with considerable generality, if not ambiguity. The best-known general formulations, those of Lord Macnaghten in *Nordenfelt* [1894] AC 535, 565 and of Lord Parker of Waddington in *Adelaide* [1913] AC 781, 793–797, adapted and used by Diplock LJ in the Court of Appeal in the *Petrofina* case [1966] Ch 146, 180, speak generally of all restraints of trade without any attempt at a definition. Often we find the words 'restraint of trade' in a single passage

used indifferently to denote, on the one hand, in a broad popular sense, any contract which limits the free exercise of trade or business, and, on the other hand, as a term of art covering those contracts which are to be regarded as offending a rule of public policy. Often, in reported cases, we find that instead of segregating two questions, (i) whether the contract is in restraint of trade, (ii) whether, if so, it is 'reasonable', the courts have fused the two by asking whether the contract is in 'undue restraint of trade' or by a compound finding that it is not satisfied that this contract is really in restraint of trade at all but, if it is, it is reasonable. A well-known text-book describes contracts in restraint of trade as those which 'unreasonably restrict' the rights of a person to carry on his trade or profession. There is no need to regret these tendencies: indeed, to do so, when consideration of this subject has passed through such notable minds from Lord Macclesfield onwards, would indicate a failure to understand its nature. The common law has often (if sometimes unconsciously) thrived on ambiguity and it would be mistaken, even if it were possible, to try to crystallise the rules of this, or any, aspect of public policy into neat propositions. The doctrine of restraint of trade is one to be applied to factual situations with a broad and flexible rule of reason . . .

This does not mean that the question whether a given agreement is in restraint of trade, in either sense of these words, is nothing more than a question of fact to be individually decided in each case. It is not to be supposed, or encouraged, that a bare allegation that a contract limits a trader's freedom of action exposes a party suing on it to the burden of justification. There will always be certain general categories of contracts as to which it can be said, with some degree of certainty, that the 'doctrine' does or does not apply to them. Positively, there are likely to be certain sensitive areas as to which the law will require in every case the test of reasonableness to be passed: such an area has long been and still is that of contracts between employer and employee as regards the period after the employment has ceased. Negatively, and it is this that concerns us here, there will be types of contract as to which the law should be prepared to say with some confidence that they do not enter into the field of restraint of trade at all.

How, then, can such contracts be defined or at least identified? No exhaustive test can be stated—probably no precise non-exhaustive test. But the development of the law does seem to show that judges have been able to dispense from the necessity of justification under a public policy test of reasonableness such contracts or provisions of contracts as, under contemporary conditions, may be found to have passed into the accepted and normal currency of commercial or contractual or conveyancing relations. That such contracts have done so may be taken to show with at least strong prima force that, moulded under the pressures of negotiation, competition and public opinion, they have assumed a form which satisfies the test of public policy as understood by the courts at the time, or, regarding the matter from the point of view of the trade, that the trade in question has assumed such a form that for its health or expansion it requires a degree of regulation. Absolute exemption from restriction or regulation is never obtained: circumstances, social or economic, may have altered, since they obtained acceptance, in such a way as to call for a fresh examination: there may be some exorbitance or special feature in the individual contract which takes it out of the accepted category: but the court must be persuaded of this before it calls upon the relevant party to justify a contract of this kind.

Some such limitation upon the meaning in legal practice of 'restraints of trade' must surely have been present to the minds of Lord Macnaghten and Lord Parker. They cannot have meant to say that any contract which in whatever way restricts a man's liberty to trade was (either historically under the common law, or at the time of which they were speaking) prima facie unenforceable and must be shown to be reasonable. They must have been well aware that areas existed, and always had existed, in which limitations of this liberty were not only



defensible, but were not seriously open to the charge of restraining trade. Their language, they would surely have said, must be interpreted in relation to commercial practice and common sense . . .

I turn now to the agreements. In my opinion, on balance, they enter into the category of agreements in restraint of trade which require justification. They directly bear upon, and in some measure restrain, the exercise of the respondent's trade, so the question is whether they are to be treated as falling within some category excluded from the 'doctrine' of restraint of trade. The broad test, or rather approach, which I have suggested, is capable of answering this. This is not a mere transaction in property, nor a mere transaction between owners of property: it is essentially a trade agreement between traders. It is not a mere agreement for exclusive purchase of a commodity, though it contains this element: if it were nothing more, there would be a strong case for treating it as a normal commercial agreement of an accepted type. But there are other restrictive elements. There is the tie for a fixed period with no provision for determination by notice, a combination which . . . should be considered together, and there is the fetter on the terms on which the station may be sold. Admittedly Harpers could liberate themselves by finding a successor willing to take their place: admittedly, too, being a limited company, they could trade in several places simultaneously, so that even if they remained tied to these sites, and obliged to continue trading there, they could in theory set up business elsewhere. But just as in *McEllistrim's case* [1919] AC 548 the reality of the covenantor's restraint was considered more relevant than his theoretical liberty to depart, so here, in my opinion, addition of all the ingredients takes the case into the category of those which require justification. Finally the agreement is not of a character which, by the pressure of negotiation and competition, has passed into acceptance or into a balance of interest between the parties or between the parties and their customers; the solus system is both too recent and too variable for this to be said.

**Lord Morris of Borth-y-Gest, Lord Hodson, and Lord Pearce** delivered concurring judgments.

## Commentary

There were two issues at stake before the House of Lords. The first was whether the doctrine of restraint of trade applied at all. The House of Lords answered this question in the affirmative but in doing so it has given rise to some difficulties in terms of ascertaining the scope of the doctrine. Thus it has been stated (*Atiyah's Introduction to the Law of Contract* (6th edn, Oxford University Press, 2005), p. 221):

It is not easy to determine, however, which contracts qualify as being restraints of trade. By definition, every contract involves some restriction on liberty, and indeed, most contracts involve restrictions that are of the same general kind, even if not of the same degree, as those found in recognised restraints of trade. For example, an employee is not free to work except for her employer during ordinary working hours, and a buyer who contracts to obtain all the supplies of some commodity which she needs from a particular seller (a common enough form of business agreement) is restricting her freedom to buy from someone else. At the same time, it would be wrong to conclude that *all* contracts containing restrictions are now open to challenge as contracts in restraint of trade.

Many customary and accepted forms of business agreement are probably still unchallengeable (at any rate under the common law rules), even though they may, strictly speaking,

involve a degree of business restraint. In particular, it has been held that a person who buys land (or a building) may validly agree to some restrictions on how the land is to be used without triggering the restraint of trade doctrine—in other words he cannot challenge the validity of the agreement on the ground that it is an unreasonable restraint. This limit on the scope of the doctrine has been justified on the ground that, if a seller could not validly demand from the buyer some restriction of this kind, he might choose not to sell at all, which would be even more restrictive of competition. Of course, this same argument could be made about any agreement whereby a seller of a business takes an unreasonably wide restraint from the buyer. In the end, there does not appear to be any difference *in kind* between the kinds of restraints that are subject to the doctrine and those that are not. Rather, the explanation would appear to be that various kinds of restraints are exempt simply because it is unlikely in practice that they will be found to be unreasonable.’

The application of the doctrine of restraint of trade to covenants affecting land is a topic of some controversy (see *Alec Lobb (Garages) Ltd v. Total Oil (Great Britain) Ltd* [1985] 1 WLR 173 and GH Treitel, *The Law of Contract* (edited by E Peel, 14th edn, Sweet & Maxwell, 2015), 11-100). Covenants affecting land apart, the question what is or is not a restraint of trade is a matter of substance rather than form (see further *Schroeder v. Macaulay*, below).

The second issue concerned the reasonableness of the restraints and here the House of Lords distinguished between the four-year and the twenty-one year restraint. Their Lordships had regard to a broad range of factors when deciding the reasonableness of the ties. Professor Bell (*Policy Arguments in Judicial Decisions* (Oxford University Press, 1983), p. 170) has pointed out that:

Unlike the Court of Appeal, their Lordships took a wider view of what were the legitimate interests which Esso were entitled to protect. In considering this question, they had regard to the money spent on building refineries and providing other outlets, the need for overall planning to justify such expenditure and to provide a stable system of outlets, what was reasonable in return for the advantages conferred by the agreement, what was necessary to secure the loan, and the general state of the industry. Such matters were considered questions of fact to be determined from evidence and common knowledge. Lords Reid, Hodson and Pearce relied on information provided in the report of the Monopolies Commission on Petrol and the last two used it in support of the view that a restraint of under five years was reasonable. Lords Hodson, Pearce, and Wilberforce also relied on the length of time for which Commonwealth courts had held similar agreements to be valid, and this was a major justification offered by Lord Wilberforce. Such evidence was not considered as binding upon the judges, but supported their conclusion that the restraint of four years and five months in the case of *Mustow Green* was not unreasonable.

The restrictions in respect of the Corner Garage were, however, held to be unreasonable in that they tied Harper’s for a period which was longer than could be foreseen, and could have effect in quite different conditions, so that the public interest in preserving Harper’s liberty of action applied more strongly here.

Although the arguments had centred on what tie could be reasonably imposed by [Esso] in support of their interests, the basis of the decision of the House was the injury, or potential injury, to the public of the limitations on Harper’s freedom of action. If competition is to be a generally accepted way of running the economy, then restraints have to be justified in terms of their benefits to the community as well as to individuals, and for this reason the public interest figures so importantly in the considerations of the judges.

***A Schroeder Music Publishing Co Ltd v. Macaulay (formerly Instone)***  
 [1974] 1 WLR 1308, House of Lords

The respondent, a young and unknown songwriter, entered into a contract with the appellants for his exclusive services. The agreement was made on the appellants' standard terms. The respondent agreed to give the appellants the copyright over all of his compositions for a five-year period and the agreement was renewable automatically for a further five years in the event that his royalties in the first five years exceeded £5,000. The contract gave the appellants the right to terminate the agreement at any time on giving one month's notice but did not give a right to terminate the agreement to the respondent. The appellants were entitled to assign their rights under the contract to a third party but no right to assign was given to the respondent. The appellants were under no obligation to publish any of the respondent's compositions. The respondent sought a declaration that the agreement was void on the ground that it constituted an unreasonable restraint of trade. The appellants submitted that the doctrine of restraint of trade was not applicable to the contract and that, in any event, the terms of the contract were reasonable. The House of Lords held that the doctrine of restraint of trade was applicable to the contract and further that they were an unreasonable restraint of trade. Accordingly, the respondent was entitled to the declaration which he sought.

**Lord Reid**

I think that in a case like the present case two questions must be considered. Are the terms of the agreement so restrictive that either they cannot be justified at all or they must be justified by the party seeking to enforce the agreement? Then, if there is room for justification, has that party proved justification—normally by showing that the restrictions were no more than what was reasonably required to protect his legitimate interests.

[he examined the terms of the contract and continued]

Clauses 1 and 9(a) determine the duration of the agreement. It was to last for five years in any event and for 10 years if the royalties for the first five years exceeded £5,000. There is little evidence about this extension. £5,000 in five years appears to represent a very modest success, and so if the respondent's work became well known and popular he would be tied by the agreement for 10 years. The duration of an agreement in restraint of trade is a factor of great importance in determining whether the restrictions in the agreement can be justified but there was no evidence as to why so long a period was necessary to protect the appellants' interests . . .

[he reviewed other clauses in the contract and continued]

The public interest requires in the interests both of the public and of the individual that everyone should be free so far as practicable to earn a livelihood and to give to the public the fruits of his particular abilities. The main question to be considered is whether and how far the operation of the terms of this agreement is likely to conflict with this objective. The respondent is bound to assign to the appellants during a long period the fruits of his musical talent. But what are the appellants bound to do with those fruits? Under the contract nothing. If they do use the songs which the respondent composes they must pay in terms of the contract. But they need not do so. As has been said they may put them in a drawer and leave them there.

No doubt the expectation was that if the songs were of value they would be published to the advantage of both parties. But if for any reason the appellants chose not to publish them

the respondent would get no remuneration and he could not do anything. Inevitably the respondent must take the risk of misjudgment of the merits of his work by the appellants. But that is not the only reason which might cause the appellants not to publish. There is no evidence about this so we must do the best we can with common knowledge. It does not seem fanciful and it was not argued that it is fanciful to suppose that purely commercial consideration might cause a publisher to refrain from publishing and promoting promising material. He might think it likely to be more profitable to promote work by other composers with whom he had agreements and unwise or too expensive to try to publish and popularise the respondent's work in addition. And there is always the possibility that less legitimate reasons might influence a decision not to publish the respondent's work.

It was argued that there must be read into this agreement an obligation on the publisher to act in good faith. I take that to mean that he would be in breach of contract if by reason of some oblique or malicious motive he refrained from publishing work which he would otherwise have published. I very much doubt this but even if it were so it would make little difference. Such a case would seldom occur and then would be difficult to prove.

I agree with the appellants' argument to this extent. I do not think that a publisher could reasonably be expected to enter into any positive commitment to publish future work by an unknown composer. Possibly there might be some general undertaking to use his best endeavours to promote the composer's work. But that would probably have to be in such general terms as to be of little use to the composer.

But if no satisfactory positive undertaking by the publisher can be devised, it appears to me to be an unreasonable restraint to tie the composer for this period of years so that his work will be sterilised and he can earn nothing from his abilities as a composer if the publisher chooses not to publish. If there had been in clause 9 any provision entitling the composer to terminate the agreement in such an event the case might have had a very different appearance [clause 9 gave a right to terminate to the publishers but not to the composer]. But as the agreement stands not only is the composer tied but he cannot recover the copyright of work which the publisher refuses to publish.

It was strenuously argued that the agreement is in standard form, that it has stood the test of time, and that there is no indication that it ever causes injustice. Reference was made to passages in the speeches of Lord Pearce and Lord Wilberforce in *Esso Petroleum Co Ltd v. Harper's Garage (Stourport) Ltd* [1968] AC 269 with which I wholly agree. Lord Pearce said, at p. 323:

'It is important that the court, in weighing the question of reasonableness, should give full weight to commercial practices and to the generality of contracts made freely by parties bargaining on equal terms.'

and Lord Wilberforce said, at pp. 332–333:

'But the development of the law does seem to show that judges have been able to dispense from the necessity of justification under a public policy test of reasonableness such contracts or provisions of contracts as, under contemporary conditions, may be found to have passed into the accepted and normal currency of commercial or contractual or conveyancing relations. That such contracts have done so may be taken to show with at least strong prima facie force that, moulded under the pressures of negotiation, competition and public opinion, they have assumed a form which satisfies the test of public policy as understood by the courts at the time, or, regarding the matter from the point of view of the trade, that the trade in question has assumed such a form that for its health or expansion it requires a degree of regulation.'

But those passages refer to contracts 'made freely by parties bargaining on equal terms' or 'moulded under the pressures of negotiation, competition and public opinion'. I do not find from any evidence in this case, nor does it seem probable, that this form of contract made between a publisher and an unknown composer has been moulded by any pressure of negotiation. Indeed, it appears that established composers who can bargain on equal terms can and do make their own contracts.

Any contract by which a person engages to give his exclusive services to another for a period necessarily involves extensive restriction during that period of the common law right to exercise any lawful activity he chooses in such manner as he thinks best. Normally the doctrine of restraint of trade has no application to such restrictions: they require no justification. But if contractual restrictions appear to be unnecessary or to be reasonably capable of enforcement in an oppressive manner, then they must be justified before they can be enforced.

In the present case the respondent assigned to the appellants 'the full copyright for the whole world' in every musical composition 'composed created or conceived' by him alone or in collaboration with any other person during a period of five or it might be 10 years. He received no payment (apart from an initial £50) unless his work was published and the appellants need not publish unless they chose to do so. And if they did not publish he had no right to terminate the agreement or to have copyrights re-assigned to him. I need not consider whether in any circumstances it would be possible to justify such a one-sided agreement. It is sufficient to say that such evidence as there is falls far short of justification. It must therefore follow that the agreement so far as unperformed is unenforceable.

I would dismiss this appeal.

### Lord Diplock

My Lords, the contract under consideration in this appeal is one whereby the respondent accepted restrictions upon the way in which he would exploit his earning power as a song writer for the next ten years. Because this can be classified as a contract in restraint of trade the restrictions that the respondent accepted fell within one of those limited categories of contractual promises in respect of which the courts still retain the power to relieve the promisor of his legal duty to fulfil them. In order to determine whether this case is one in which that power ought to be exercised, what your Lordships have in fact been doing has been to assess the relative bargaining power of the publisher and the song writer at the time the contract was made and to decide whether the publisher had used his superior bargaining power to exact from the song writer promises that were unfairly onerous to him. Your Lordships have not been concerned to inquire whether the public have in fact been deprived of the fruit of the song writer's talents by reason of the restrictions, nor to assess the likelihood that they would be so deprived in the future if the contract were permitted to run its full course.

It is, in my view, salutary to acknowledge that in refusing to enforce provisions of a contract whereby one party agrees for the benefit of the other party to exploit or to refrain from exploiting his own earning power, the public policy which the court is implementing is not some 19th-century economic theory about the benefit to the general public of freedom of trade, but the protection of those whose bargaining power is weak against being forced by those whose bargaining power is stronger to enter into bargains that are unconscionable. Under the influence of Bentham and of laissez-faire the courts in the 19th century abandoned the practice of applying the public policy against unconscionable bargains to contracts generally, as they had formerly done to any contract considered to be usurious; but the policy survived

in its application to penalty clauses and to relief against forfeiture and also to the special category of contracts in restraint of trade. If one looks at the reasoning of 19th-century judges in cases about contracts in restraint of trade 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 that it was not.

So I would hold that the question to be answered as respects a contract in restraint of trade of the kind with which this appeal is concerned is: 'Was the bargain fair?' The test of fairness is, no doubt, whether the restrictions are both reasonably necessary for the protection of the legitimate interests of the promisee and commensurate with the benefits secured to the promisor under the contract. For the purpose of this test all the provisions of the contract must be taken into consideration.

My Lords, the provisions of the contract have already been sufficiently stated by my noble and learned friend, Lord Reid. I agree with his analysis of them and with his conclusion that the contract is unenforceable. It does not satisfy the test of fairness as I have endeavoured to state it. I will accordingly content myself with adding some observations directed to the argument that because the contract was in a 'standard form' in common use between music publishers and song writers the restraints that it imposes upon the song writer's liberty to exploit his talents must be presumed to be fair and reasonable. Standard forms of contracts are of two kinds. The first, of very ancient origin, are those which set out the terms upon which mercantile transactions of common occurrence are to be carried out. Examples are bills of lading, charterparties, policies of insurance, contracts of sale in the commodity markets. The standard clauses in these contracts have been settled over the years by negotiation by representatives of the commercial interests involved and have been widely adopted because experience has shown that they facilitate the conduct of trade. Contracts of these kinds affect not only the actual parties to them but also others who may have a commercial interest in the transactions to which they relate, as buyers or sellers, charterers or shipowners, insurers or bankers. If fairness or reasonableness were relevant to their enforceability the fact that they are widely used by parties whose bargaining power is fairly matched would raise a strong presumption that their terms are fair and reasonable.

The same presumption, however, does not apply to the other kind of standard form of contract. This is of comparatively modern origin. It is the result of the concentration of particular kinds of business in relatively few hands. The ticket cases in the 19th century provide what are probably the first examples. The terms of this kind of standard form of contract have not been the subject of negotiation between the parties to it, or approved by any organisation representing the interests of the weaker party. They have been dictated by that party whose bargaining power, either exercised alone or in conjunction with others providing similar goods or services, enables him to say: 'If you want these goods or services at all, these are the only terms on which they are obtainable. Take it or leave it'.

To be in a position to adopt this attitude towards a party desirous of entering into a contract to obtain goods or services provides a classic instance of superior bargaining power. It is not without significance that on the evidence in the present case music publishers in negotiating with song writers whose success has been already established do not insist upon adhering to a contract in the standard form they offered to the respondent. The fact that the appellants' bargaining power vis-a-vis the respondent was strong enough to enable them to adopt this take-it-or-leave-it attitude raises no presumption that they used it to drive an unconscionable bargain with him, but in the field of restraint of trade it calls for vigilance on the part of the court to see that they did not.

**Viscount Dilhorne** concurred with the speech of Lord Reid. **Lord Simon of Glaisdale** and **Lord Kilbrandon** concurred with the speeches of Lord Reid and Lord Diplock.

## Commentary

*Schroeder* is another difficult decision. It demonstrates that the doctrine of restraint of trade can apply to terms during the currency of a relationship. It also appears to link the doctrine of restraint of trade with procedural unfairness, substantive unfairness, and inequality of bargaining power (on which see Chapter 20 of the textbook). Indeed, one of the criticisms that has been levelled against the decision is that it is very difficult to locate the basis upon which the House of Lords decided to intervene. Lord Diplock, in particular, seemed to rely upon a mix of factors. Thus Professor Smith has pointed out ('Reconstructing Restraint of Trade' (1995) 15 *OJLS* 565, 583) that:

Lord Diplock suggests, at different times and in different ways, that procedural fairness, substantive fairness and the traditional notion of reasonableness are all relevant to the validity of a restraint. Lord Diplock did not attempt to reconcile his conflicting statements, although he did give a further indication that he considered 'bargaining power' relevant. Later in his judgment he said that the type of standard form contract at issue in the case was typically 'the result of the concentration of particular kinds of business in relatively few hands' and added that the ability of more 'established' singers to negotiate individualised and more favourable contracts supported a presumption of inequality of bargaining power.

Lord Diplock's assumption that the terms were presented to Mr Macaulay on a take-it-or-leave-it basis has also been challenged on the ground that it does not appear to fit the case of the music industry at the relevant time. Professor Trebilcock (*Restraint of Trade* (Carswell, 1986), p. 168) has noted that there were 428 UK music publishers in 1975–1976, 276 record and tape manufacturers/distributors/importers, and fifty-four independent record producers. He concludes that 'these numbers appear to suggest a dynamic and highly competitive music industry, probably comprising more competing firms than several of the industries cited in Lord Diplock's first category'. Professor Collins (*The Law of Contract* (4th edn, Butterworths, 2003), pp. 28–29) has concluded as follows:

If one considers this decision from the perspective of market failure, then it seems hard to justify. As Trebilcock points out, there seems to have been a competitive market operating in this instance, with many music publishers competing for young talent. Nor can it be seriously suggested that the composer did not understand the terms of the agreement because they were too complex. In the absence of such grounds to suspect market failure, economic analysis suggests that the contract should be enforced, for any interference may disrupt the market opportunities for young composers in the future.

But these arguments, although sound in themselves, miss the real objections to this contract, which concern the dimensions of power, fairness, and co-operation, not the efficiency of the market. Because the composer's career was completely dependent upon the publisher's discretion for a period up to ten years, his degree of subordination to another represented an unjustifiable form of domination. The absence of an undertaking on the part of the publisher to publish any of his songs rendered the exchange too one-sided to be fair. In addition, because the composer could not terminate the agreement during its fixed period, he had no effective sanction against the publisher to ensure that at least it made reasonable efforts to bring the venture to fruition by publishing and promoting his work. These three themes—the concern about unjustifiable domination, the equivalence of the exchange, and the need to ensure co-operation—which seem to me to motivate the decision in *Schroeder*

© Ewan McKendrick 2020.

*Music Publishing Co Ltd v. Macaulay*, form the core of the interpretation of the law of contract presented in this book. The emphasis upon these values in the modern law signifies a new understanding and justification of the market order.

## 5. THE CONSEQUENCES OF ILLEGALITY

The general rule is that the courts will not enforce an illegal contract. More difficult is the question whether they will permit the recovery of the value of benefits conferred on another party in the performance of an illegal contract. The answer to the latter question was, until recently, that the courts would not permit the recovery of benefits conferred but that general rule must now be revised in the light of the decision of the Supreme Court in *Patel v. Mirza* [2016] UKSC 42, [2017] AC 467. Two maxims have been applied by the courts in the development of the law. The first is *ex turpi causa non oritur actio* (no action can be based on a disreputable cause) and the second is *in pari delicto potior est conditio defendentis* (where both parties are equally at fault, the position of the defendant is stronger). As we shall see, neither rule is without exceptions.

As *Archbolds (Freightage) Ltd v. S Spanglett Ltd* [1961] 1 QB 374 (above) demonstrates, an innocent party, who is unaware of an illegal act committed by the defendant in the course of performance of the contract, may be entitled to enforce the contract, notwithstanding the illegality. The court may also conclude, as a matter of construction, that the effect of a statutory provision is to impose a punishment on a party who breaches the statute but not to render unenforceable a contract the performance of which involves a breach of the statute (see, for example, *St John Shipping Corporation v. Joseph Rank Ltd* [1957] 1 QB 267). The court may also be able to sever the illegal part of the contract from the rest of the contract and enforce the remainder of the contract (see further J Beatson, A Burrows and J Cartwright *Anson's Law of Contract* (30th edn, Oxford University Press, 2016), pp. 455–461).

The biggest issue in the modern law relating to illegality is the extent to which the courts have a discretion which enables them, in an appropriate case, to enforce an illegal contract, at least in the case where the consequences of non-enforcement would be disproportionate. This dispute was resolved by the Supreme Court in *Patel v. Mirza* where it was held, by a majority, that a court considering the application of the defence of illegality should have regard to the policy factors involved and to the nature and circumstances of the illegal conduct in determining whether the public interest in preserving the integrity of the justice system should result in denial of the relief claimed. When deciding whether it is contrary to the public interest to enforce a claim on the ground that to do so would be harmful to the integrity of the legal system, the court should consider (i) the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, (ii) any other relevant public policy on which the denial of the claim would have an impact and (iii) whether denial of the claim would be a proportionate response to the illegality, bearing in mind that punishment is a matter for the criminal courts. The Supreme Court identified the principal policy reasons for declining to enforce contract rights as being that ‘a person should not be allowed to profit from his own wrongdoing’ and that ‘the law should be coherent and not self-defeating, condoning illegality by giving with the left hand what it takes with the right hand.’



In reaching its conclusion the Supreme Court also considered a proposal put forward by Professor Andrew Burrows (*A. Burrows, A Restatement of the English Law of Contract* (2016), pp 229-230) in which he set out the following list of factors which the courts might take into account when deciding whether or not to enforce rights claimed to arise out of an illegal transaction:

If the formation, purpose or performance of a contract involves conduct that is illegal (such as a crime) or contrary to public policy (such as a restraint of trade), the contract is unenforceable by one or either party if to deny enforcement would be an appropriate response to that conduct, taking into account where relevant -

- (a) how seriously illegal or contrary to public policy the conduct was;
- (b) whether the party seeking enforcement knew of, or intended, the conduct;
- (c) how central to the contract or its performance the conduct was;
- (d) how serious a sanction the denial of enforcement is for the party seeking enforcement;
- (e) whether denying enforcement will further the purpose of the rule which the conduct has infringed;
- (f) whether denying enforcement will act as a deterrent to conduct that is illegal or contrary to public policy;
- (g) whether denying enforcement will ensure that the party seeking enforcement does not profit from the conduct;
- (h) whether denying enforcement will avoid inconsistency in the law thereby maintaining the integrity of the legal system.'

In *Patel* Lord Toulson, giving the lead judgment for the majority, observed that this list, whilst 'helpful', should not be seen as being 'prescriptive or definitive because of the infinite possible variety of cases.' But at least it gives an indication of the type of factors the courts are likely to take into account when deciding whether or not a party to an illegal contract remains entitled to enforce any of its rights under the contract.

In relation to claims to recover payments made or property transferred pursuant to an illegal transaction (rather than a claim to enforce the terms of the illegal contract) the Supreme Court held that the rule to be applied in the future is that a person who satisfies the ordinary requirements of a claim in unjust enrichment will not *prima facie* be debarred from recovering money paid or property transferred by reason of the fact that the consideration which has failed was an unlawful consideration. The justification offered by the Supreme Court for the recognition of a general right of recovery is that the reversal of a transaction does not undermine the policies which lie behind the doctrine of illegality as a defence to a private law claim. Reversal of the transaction does not permit a party to benefit from his own wrongdoing, nor does it render the law incoherent or self-defeating. On the contrary, it restores the parties to their previous position as if there had been no illegal contract. However, there may still be cases in which a party will be held not to be entitled to recover a payment made or property transferred pursuant to an illegal contract. Examples which might fall into this category include payments made in respect of serious criminal activity, such as drug trafficking or a contract to murder someone. The precise scope of the general right to recover will have to be worked out on a case-by-case basis.

**FURTHER READING**

BUCKLEY, R, 'Illegality in Contract and Conceptual Reasoning' (1983) 12 *Anglo-American Law Review* 280

SMITH, S, 'Reconstructing Restraint of Trade' (1995) 15 *OJLS* 565.

**Incorporated Council of Law Reporting:** extracts from the *Law Reports: Appeal Cases* (AC), *Queen's Bench* (QB) and *Weekly Law Reports*, (WLR).