17/79

No. 13 of 1977

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

ON APPEAL

FROM THE COURT OF APPEAL OF HONG KONG

BETWEEN:

PAO ON	1st Appellant
HO MEI CHUN	2nd Appellant
PAO LAP CHUNG	3rd Appellant

- and -

LAU YIU LONG	1st Respondent
BENJAMIN LAU KAM CHING	2nd Respondent

CASE FOR THE RESPONDENTS

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1. This is an appeal from the Order of the Court of Appeal of Hong Kong exercising appellate jurisdiction (Briggs, C.J., McMullin and Leonard, JJ., Briggs C.J. dissenting), dated the 5th November 1976, allowing the Respondents' appeal from the judgment of Li J., exercising Original jurisdiction, dated the 17th February 1976, thus setting aside judgment in favour of the Appellants for the sum of $5,392,800.00 together with interest thereon and costs. p 137 p 115

The Facts

2. In February 1973 the Appellants owned all the shares in a private company, Tsuen Wan Shing On Estate Company Limited ("Shing On"). The Respondents were the majority shareholders in a public company, Fu Chip Investment Company Limited ("Fu Chip"). By a written agreement ("the main Agreement") dated the 27th February 1973, between the Appellants, Shing On and Fu p 96

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Chip, Fu Chip agreed to buy all shares in Shing On, for $10,500,000. to be paid for by the allotment to the Appellants of 4.2. million newly issued $1 shares in Fu Chip, valued at $2.50. The Appellants agreed not to sell or transfer 2,520,000 of the Fu Chip shares (60%) before April 1974. By another written agreement made the same day ("the subsidiary agreement"), the Appellants agreed to sell to the First Respondent 60% of their allotment of Fu Chip shares at $2.50 on or before the 30th April 1974. The completion date for the Main Agreement was the 31st March 1973, but was postponed by mutual consent to the 30th April 1973. It was eventually completed on the 4th May 1973.

3. On the 16th March 1973 Fu Chip made a public announcement of the takeover of Shing On. On the 31st March 1973 the Far East Stock Exchange Limited approved Fu Chip's application for permission to deal in and for quotation of the new allotment. From the 19th April 1973 the Respondents pressed for the completion of the main agreement. The Trial Judge found that the Appellants prevaricated, in that the First Appellant absented himself from Hong Kong during this critical period.

p 108 lines 28-42

4. On the 4th May 1973, before the completion of the Main Agreement, the Respondents signed a document (referred to herein and in the judgments as "the guarantee") which is the subject of this appeal. The substance of the guarantee was that the Respondents guaranteed that the price of the 60% allocation of Fu Chip shares would be not less than $2.50 per share on the marketing day immediately following the 30th April 1974, and that they would indemnify the Appellants if the shares fell below that price. The consideration was expressed to be "in consideration of your [the Appellants] having at our request agreed to sell all your shares in [Shing On] .. under an Agreement for sale andpurchase ... dated the 27th day of February 1973 ... " On the same day the subsidiary agreement was cancelled and, by a further written agreement ("the indemnity agreement"), the Appellants "guaranteed" not within one year to part with the Fu Chip shares, without giving the Respondents themselves the option to purchase them.

5. On the 1st May 1974, the marketing day

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immediately following the 30th April 1974, the price of each Fu Chip share was 36 cents. Accordingly, in this action the Appellants claimed against the Respondents the difference between $2.50 and 36 cents per share on 2,520,000 shares, which amounts to $5,392,800.

6. Apart from the issues which arise in this appeal, the Appellants raised certain other contentions at the trial. The principal of these was that the subsidary agreement never truly represented the agreement between the Appellants and the Respondents and that the guarantee merely recorded in an accurate form an antecedent oral agreement. The Trial Judge rejected the Appellants' evidence of this oral agreement. p 106 lines 11-14

The Main Issues

7. In this appeal the main issues are as follows :-

(1) Whether extrinsic evidence is admissible to show a consideration other than that stated in the guarantee dated the 4th May 1973; Exh. A 37-38 pp. 224-225

(2) If so, whether performance of a pre-existing contractual obligation owed by the Appellants to a third party did amount in the circumstances of this case to good consideration for the guarantee;

(3) If so, whether the guarantee is vitiated by undue pressure, economic duress or other unconscionable conduct.

Admission of Extrinsic Evidence

8. The Respondents' case was throughout, and is, that extrinsic evidence is not admissible to show a consideration other than that stated in the guarantee.

9. The statement of consideration in the guarantee is clear. It refers to the Appellants having at the Respondents' request agreed to sell their shares "under an Agreement for sale and purchase made between the parties thereto and dated the 27th day of February 1973". This pp 224-225

Exhibit C2 pp256-259

Agreement, i.e., the Main Agreement, pre-dated the guarantee by some two months. The case is thus distinguishable from Goldshede v Swan (1847) 1 Ex. 154 where the words used were "in consideration of your having this day advanced to our client £750". At page 160, Pollock C.B. observed:

> "The expression 'this day' may mean something which has been done or which is to be done this day. Evidence may therefore be properly admitted to explain its meaning, though not to contradict it."

pp 155-161 pp 157 lines 30-31 pp 157 lines 23-25 p 159 lines 20-24 p 159 line 23 p 160 line 1 et seq

10. McMullin J. therefore held that the extrinsic evidence was wrongly admitted by the Trial Judge. He found nothing ambiguous about the stated consideration. There is, in his view, no rule of law which says that, where a stated consideration is for any reason bad, then evidence is admissible to show a different one. He observed that on the Appellants' case, upon the signing of the guarantee, there remained something to be done by the Appellants, that is, the transfer of the shares and this, he said, the Appellants might never have done. To say, therefore, that the transfer of the shares was the consideration for the gaurantee would be to introduce an idea "wholly different" from that expressed in the guarantee, namely, a plain promise to do something in return for something which had already been done. This is not the same as a promise to do something "if" something in return is done. McMullin J. further rejected the suggestion that extrinsic evidence is admissible to explain the terms of the guarantee. The terms, he said, are perfectly straightforward and require no explation. The only part of the evidence which might be said to explain the terms of the guarantee in a sense other than that which the words themselves clearly convey is that very part which the Trial Judge expressly rejected, namely, the Appellants' story of a preliminary oral agreement by the Respondents to give a guarantee in relation to the price of the shares. McMullin J. allowed the Respondents' appeal.

11. Briggs C.J., however, following the reasoning of the Trial Judge, held that in the context of the facts known to both parties (as revealed by extrinsic evidence) the words "to sell" could only mean "to complete the sale" and that under the guarantee the parties

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were "agreeing to complete the sale". But he went on to say that the consideration was the completion or performance of the sale. He said: (p 141 lines 29-30; p 141 lines 34-35)

> "..."the extrinsic evidence was rightly admitted in this case to explain the surrounding circumstances of the guarantee, and the background to it. It was adding to and explaining the terms contained in the instrument. It is proving the real consideration for the guarantee. It is not proving a consideration which is different from that contained in the instrument itself." (p 142 lines 23-28)

12. Leonard J. also held that extrinsic evidence was rightly admitted but he came to that conclusion "not without very considerable hesitation". He held that the evidence had the effect of proving an additional consideration not necessarily contradictory to the stated consideration. The consideration for the guarantee, he said, was the immediate completion by the Appellants of the Main Agreement. But he also went on to say (emphasis supplied): "the true mutual consideration giving by the Plaintiffs was the agreement forthwith to complete the main contract." (p 172 line 1; p 171 lines 1-4; p 171 lines 31-33; p 171 lines 38-40)

13. The Respondents submit that Briggs C.J. and Leonard J., as well as the Trial Judge, have in effect contradicted themselves by saying or implying, on the one hand, that the consideration for the guarantee was an agreement on the part of the Appellants to perform the Main Agreement, and, on the other hand, that the consideration for the guarantee was the performance of that agreement.

14. In fact the Appellants have never pleaded nor was it otherwise ever part of their case that the consideration for the guarantee was an agreement to do an act as distinguished from the performance of an act. The Appellants had never alleged that they had bound themselves by contract vis-a-vis the Respondents to complete the Main Agreement. That they had done so vis-a-vis a third party (Fu Chip) was never in doubt, but that was a different matter. In the circumstances it was not open to their Lordships to find that, on the extrinsic evidence,

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the consideration was an agreement on the part of the Appellants vis-a-vis the Respondents to complete the Main Agreement.

15. The Respondents submit that, in any event, the consideration allegedly shown to exist by the extrinsic evidence in fact contradicts the express terms of the guarantee. The words "to sell" have a perfectly plain meaning and there is no justification whatever for substituting therefor the words "to complete the sale". No doubt, "to sell" imports an obligation to complete the sale, but that obligation was incurred, according to the express terms of the guarantee, under an agreement made between the Appellants and a third party (Fu Chip) and pre-dating the guarantee by some two months. In other words the stated consideration was a pre-existing contractual obligation, that is, past consideration.

16. Quite apart, therefore, from the fact that this was neither pleaded nor canvassed at the trial, to contend that the consideration was not the pre-existing obligation owed by the Appellants to Fu Chip, as stated in the guarantee, but a present promise to do an act made by the Appellants to the Respondents would be to contradict the stated consideration.

17. Likewise, to contend that performance of the Main Agreement was the consideration for the guarantee would also be to contradict the express terms of the guarantee. It would not only change the stated consideration from a past to an executory consideration, but it would also change the guarantee from a bilateral to a unilateral or "if" contract. Goldshede v Swan (supra) made it quite clear that, although extrinsic evidence is admissible to explain an ambiguity in the statement of consideration, it is not admissible to show a consideration inconsistent with it. This proposition is in no way contradicted by Frith v Frith [1906] A.C. 254, Clifford v Turrell (1841) 14 L.J. Ch. 390 or Turner v Forwood and another [1951] 1 All E.R. 746.

18. The Respondents submit that the rule is correctly expressed in Halsbury's Laws of England, 4th Edition, Vol 12 at paragraph 1487 and does not permit extrinsic evidence to be admitted in the present case. The rule as stated reads as follows :-

> "Where no consideration,or a nominal consideration, is expressed in the instrument, or the consideration is expressed in general terms or is ambiguously stated extrinsic evidence is admissible to prove the real consideration; and where a substantial consideration is expressed in the instrument, extrinsic evidence is admissible to prove an additional consideration, provided that this is not inconsistent with the terms of the instrument. It is not in contradiction to the instrument to prove a larger consideration than that which is stated."

19. The Respondents submit that this is not a case where there is no statement of any consideration in the instrument. Nor is this a case where the consideration stated is nominal. Nor is the consideration ambiguously stated. Further a consideration is not admisslbe as an additional consideration or as a larger consideration if in fact it contradicts the clear terms of the instrument.

20. In the present case for reasons given above (and see in particular paragraph 17) the performance of the agreement made with Fu Chip cannot be said to be a larger consideration. It was merely the doing of something which the Appellants had already agreed to do. It was the performance of a promise that was already made. The promise made to Fu Chip was the stated consideration the performance merely its execution.

21. The Respondents therefore submit that on the extrinsic evidence point McMullin J. was right and should be upheld and that Briggs C.J., and Leonard J. in following the Trial Judge were in error.

Performance of Pre-Existing Obligation

22. The question at issue here is whether or not in the circumstances of this case performance of an obligation owed by the Appellants to a third party (Fu Chip) did amount to good consideration for the guarantee. On this issue the Court of Appeal by a majority (McMullin and Leonard JJ., Briggs C.J. dissenting) ruled in favour of the Respondents holding that on the facts of this case the performance of the pre-existing obligation did not amount to good consideration to the guarantee.

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23. The Respondents do not contend that performance of an existing obligation owed to a third party can never be good consideration. They contend, however, that although it may be good consideration it is not invariably so. Whether it is good consideration in any particular case depends upon the question whether or not it is in accordance with public policy on the facts of the particular case so to regard it.

24. It is established law that, when there are only two parties, a promise to perform an existing duty or the performance of it is not good consideration. The cases of Harris v Watson (1791) Peake 102 and Stilk v Myrick (1809) 6 Esp. 128 concern sailors who had entered into articles of service on board ships and who had receivedpromises from the captains of the vessels on which they served that additional remuneration would be paid for carrying out the terms of their contracts. It was held that they were not entitled to the extra remuneration. Lord Ellenborough in Stilk v Myrick (supra), observed that the principle was founded "on just and proper policy". To hold otherwise would be to encourage economic blackmail or other improper pressure.

25. This policy factor, it is submitted, is not and should not be excluded in three-party cases, although in such cases "there is almost never any probability that the promisee has been in a position to use or has in fact used any economic coercion to induce the making of the promise": Corbin in his Treatise on Contracts paragraph 176 (and see also paragraphs 171-172, 182-184). Where, however, some degree of economic coercion or improper pressure - even if short of outright duress - is used by the promisee to exact from another a promise in return for a promise to perform or performance of an existing duty, albeit owing to a third party, there is no reason, it is submitted, why he should be held to have furnished good consideration for the promise.

26. None of the English cases on the point lay down a general rule that in three-party cases a promise to perform or the performance of an existing duty is invariably good consideration. The Privy Council in New Zealand Shipping Co.

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v Satterthwaite Ltd (Re Eurymedon) [1975] A.C. 168 did not lay down any such proposition but was content, on the facts of that case, merely to observe (emphasis supplied) that "... consideration may quite well be provided by the appellant ... even though (or if) it was already under an obligation to discharge to the carrier." The Privy Council went on to say (emphasis supplied) that "an agreement to do an act which the promisor is under an existing obligation to a third party to do, may quite well amount to valid consideration and does so in the present case: the promiseeobtains the benefit of a direct obligation which he can enforce. The proposition is illustrated and supported by Scotson v Pegg (1861) 6 H. & N. 295, which their Lordships consider to be good law".

27. The Respondents will in particular rely on the following findings of fact by the Trial Judge:

(1) The Appellants signed the subsidiary agreement with full knowledge of the nature of its contents: there never was any oral agreement to give a guarantee as alleged by the Appellants or at all; — p 106 lines 11-18

(2) There was, therefore, nothing to form the basis of the Appellants' demand for the guarantee; — p 108 line 4

(3) Yet the Appellants, well knowing the detrimental effect on the price of the Fu Chip shares and on the Respondents' financial position if they refused to honour the Main Agreement with Fu Chip, threatened to repudiate the Main Agreement unless the Respondents signed the guarantee. — p 107 lines 40-41; p 108 lines 10-11; p 120 lines 26-30

28. The present case, therefore, is one where improper pressure was unfairly brought to bear on the promisor. To the extent that the Appellants were falsely asserting that they had not got what they bargained for and knew at the time that they were putting forward a false assertion, they were, in the words of McMullin J., acting "dishonestly". Further, the Appellants' attitude was "we will continue in breach of our contract unless you give us this guarantee". This, said Leonard J., was "dishonest". The Appellants no doubt — p 162 lines 45-6; p 176 lines 38-40

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were trying to subject the Respondents to what Corbin (Paragraph 184) calls "a hold up game". As the Trial Judge found:-

p 108 lines 28-42

> "The 1st plaintiff's decision to go to Taiwan was made probably in order to play for time and to enable the 2nd Plaintiff to start a new bargain. No reason was given for the necessity of this Taiwan trip. It is more inexplicable why he should leave at a time when it was essential for him to remain in Hong Kong to complete the main agreement with the Fu Chip. He knew by that time an announcment of the acquisition by the Fu Chip of the Shing On shares had been made to the public. He knew also that the defendants were anxious to see to /it/ that the Fu Chip completing /sic/ the transaction. He knew that the longer the Defendants had to wait the better bargaining power he would have in his hand. In short he knew he had the upper hand over the defendants who would have to agree even if he wanted something more than the original bargain viz: the subsidiary agreement. In my opinion his threat of refusing to complete was, for the plaintiffs, a good starting point for a new bargain and his temporary absence a very shrewd move".

29. The Respondents submit that McMullin and Leonard JJ. were right in holding that this is one example of a case where the Courts will not regard as good consideration the performance of an existing duty, albeit owing to a third party. To hold otherwise by drawing a distinction between two-party and three-party cases would, on the facts of the present case, be highly artificial, wrong in principle and unjust in result. This is particularly so where there is, as here, a close relationship between the identity of the third party and the identity of the persons from whom the promise was exacted. As Leonard J. said:-

p 177 lines 18-20

> "I consider that to regard this consideration as good would be contrary to public policy particularly in Hong Kong where there is a close relationship between the identity of individuals and the identity of the companies in which they have a controlling

30. Briggs C.J. took a different view. He

applied Scotson v Pegg (1861) 6 H. & N. 295. The case, however, does not purport to lay down an absolute rule applicable to all three-party cases, such as a case where the promise was exacted by means of an unlawful threat to break a contract. It is one thing to promise to pay, in the absence of a deliberate andunlawful threat to break a contract, a sum of money in order to "induce another" to perform that which he has already contracted with a third person to do; it is quite another thing to be the victim of a "hold up game". The Respondents submit that, in the light of Satterthwaite's case /1975/ A.C. 168, Scotson v Pegg (supra) is only authority for the proposition that performance by X of the pre-existing obligation owed to Y could be good consideration to support a contract with Z. As Leonard J. put it:-

> "For my part I would enter the door clearly left open in Satterthwaite's case /1975/ A.C. 168 and refuse to regard as good the additional consideration let in by the extrinsic evidence."

Economic Duress

31. Even if the consideration were held to be good, it is submitted that the guarantee would not be enforceable by reason of economic duress.

32. The Respondents submit that this is not merely a case of two parties driving a hard bargain using legitimate means of doing so. The threat to break a contract or to remain in breach of a contract was an unlawful one and amounted to the tort of intimidation: Rookes v Barnard /1964/ A.C. 1129, Stratford JJ & Sons Ltd v Lindley 1965 A.C. 269 and D & C Builders v Rees /1966/ 2 Q.B. 617 at page 625. The Respondents were therefore victims of an unlawful act or threat.

33. It is submitted that Briggs C.J. drew the wrong inference from the established facts when he held that the threat to break the contract did not operate on the mind of the Defendants and that therefore there was no duress in the sense in which that word is used in this branch of the law. The facts as established clearly show that the Respondents gave the guarantee because the Appellants were refusing to complete the Main Agreement and were exacting from them the

p 149 lines 10-17

guarantee in circumstances which put the Respondents under unfair pressure. Barton v Armstrong [1976] A.C. 104 P.C. made it clear that in cases of duress it would be sufficient for the party seeking the relief of equity to show that the threats were a reason for entering into the contract even though he might well have entered into the contract if no threats had been uttered. In the present case the Respondents gave the guarantee solely because of the Appellants' threat to repudiate the Main Agreement.

34. It is true that on the facts as found by the Trial Judge the Respondents would not have been put into financial ruin if they had resisted the Appellants' unlawful demands. But it is submitted that the doctrine of economic duress can be invoked even if the person put under improper pressure would not have suffered financial ruin if he had refused to give in to the unlawful demands.

35. American law has recognised that the increase of economic interdependence can result in certain types of business behaviour causing grave injury to commercial interests, and, accordingly, has broadened the doctrine of duress and undue influence to cover economic duress or "business compulsion". In Williston on Contracts at paragraph 1617, it is said:

> "While there is disagreement among the Courts as to what degree of coercion is necessary to a finding of economic duress, there is general agreement as to its basic elements:
>
> (1) The party alleging economic duress must show that he has been the victim of a wrongful or unlawful act or threat, and
>
> (2) Such act or threat must be one which deprives the victim of his unfettered will.
>
> As a direct result of these elements, the party threatened must be compelled to make a disproportionate exchange of values or to give up something for nothing. If the payment or exchange is made with the hope of obtaining a gain, there is not duress;

it must be made solely for the purpose of protecting the victim's business or property interest. Finally, the party threatened must have no adequate legal remedy."

This doctrine does not entitle a party to avoid an agreement merely upon the grounds of "driving a hard bargain", but does entitle him to allege business compulsion where the financial difficulty of which the other party takes advantage has been, at least in part, caused by that party. The authorities also recognise that, even if there is a remedy in the Courts, it may be inadequate if it cannot be invoked sufficiently quickly to protect the threatened interest.

The Subsidiary Issues

36. There are three subsidiary issues:-

(1) Whether the cancellation of the subsidiary agreement was a consideration for the guarantee;

(2) Whether the indemnity given by the Appellants was a consideration for the guarantee;

(3) If the guarantee should be held to be invalid, whether the subsidiary agreement which had been cancelled would revive.

37. On the first of these three issues, the Trial Judge held that the Appellants wanted the subsidiary agreement to be cancelled in any event. It was therefore not a consideration for the guarantee. Furthermore the subsidiary agreement was cancelled by a mutual discharge of obligations thereunder. Both McMullin J. and Leonard J. held in favour of the Respondents on this point.

p 117 lines 30-34
p 118 lines 17-18
p 120 lines 16-18

38. As regards the second of the aforesaid issues, the Trial Judge found as a fact that the indemnity was given after disposal of all the other matters and given for a reason entirely separate, namely, because of lack of trust on the part of the Respondents. The Respondents wished the Appellants to accept scrips for the shares in question in the form of one certificate. This the Appellants refused to do. The Respondents then suggested that the

p 107 lines 40-47
p 108 lines 43-48
p 109 lines 1-12

scrips for the shares which the Appellants had undertaken not to sell should remain with the Secretaries. This again the Appellants refused and it was because of this that the indemnity was given. The Trial Judge and the Court of Appeal unanimously held that the indemnity was not a consideration for the guarantee.

39. As regards the third of the aforesaid issues, the Respondents submit that, since the Appellants would in any event have agreed to the cancellation of the subsidiary agreement and since the subsidiary agreement was discharged by reason of a bilateral release of obligations thereunder, the invalidity or otherwise of the guarantee would not resurrect the cancelled agreement. McMullin and Leonard JJ., following the Trial Judge, held that there was no revival. Briggs C.J. dissented.

40. The Respondents therefore submit that this appeal should be dismissed with costs for the following among other

R E A S O N S

(1) BECAUSE the decision of McMullin J. in allowing the Respondents' appeal on the ground the extrinsic evidence is not admissible was correct;

(2) BECAUSE the decision of the majority of the Court of Appeal (McMullin J. and Leonard J.) to the effect that the performance of an existing obligation owed to a third party by the Appellants was in the circumstances of this case not a good consideration was correct;

(3) BECAUSE, even if extrinsic evidence is admissible and performance of a pre-existing obligation owed to a third party constituted good consideration on the facts of this case, the guarantee is vitiated or otherwise rendered unenforceable in equity by reason of economic duress;

(4) BECAUSE there was no other valid consideration for the guarantee.

Andrew Leggatt QC

Christopher Swift

No. 13 of 1977

IN THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL

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