Privy Council Appeal No. 13 of 1977

Pao On and others – – – – – – – *Appellants*

v.

Lau Yiu Long and another – – – – – *Respondents*

FROM

THE COURT OF APPEAL OF HONG KONG

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 9TH APRIL 1979

Present at the Hearing:

LORD WILBERFORCE
VISCOUNT DILHORNE
LORD SIMON OF GLAISDALE
LORD SALMON
LORD SCARMAN

[*Delivered by* LORD SCARMAN]

The Litigation

By a judgment dated and entered the 17th February 1976 Mr. Justice Li ordered the defendants, Lau Yiu Long ("Lau") and his younger brother Benjamin, to pay the plaintiffs, Pao On, his wife, and son $5,392,800 with interest as from the 1st May 1974 to the date of judgment. The judge found the money to be due under a written agreement dated the 4th May 1973. It is convenient to refer to this agreement as "the guarantee". It was, in fact, an indemnity.

The defendants appealed. The Court of Appeal, by a majority (Briggs C.J. dissenting), allowed their appeal. The plaintiffs now appeal to Her Majesty in Council.

Two issues are fundamental. Was there consideration for the contract of guarantee? If there was, was the consent of the defendants vitiated by duress? All the judges below regarded the consideration appearing on the face of the document of the 4th May 1973 as a past consideration, which, by itself, could not in law support the defendants' promise to indemnify the plaintiffs against their loss. The trial judge, however, ruled that extrinsic oral evidence was admissible to prove an additional, but not contradictory, consideration, found that the evidence did establish the existence of good additional consideration, and rejected on the facts the defendants' case of duress.

In the Court of Appeal McMullin J. was of the opinion that extrinsic evidence to prove the existence of an additional consideration was in the circumstances of this case inadmissible, and so was for allowing the appeal. He expressed the opinion that such consideration as the extrinsic

evidence, if admitted, would reveal was bad in law because it showed the plaintiffs to have obtained the " guarantee " by dishonest means. " The consideration ", he declared, " might be good in a technical or legalistic sense and yet the bargain based upon it be found voidable ". He also " inclined to the view that the doctrine [of economic duress] is not appropriate to the circumstances of the parties in the present case ".

Leonard J. thought the extrinsic evidence admitted by the trial judge was not contradictory of the written instrument containing the guarantee, and was, therefore, admissible to prove an additional consideration. But he held that to regard as valuable consideration the promise given by the plaintiffs not to break their contract with a third party was in the circumstances of this case " contrary to public policy and contrary to ordinary justice ". Accordingly he also was for allowing the appeal. He was " unconvinced " that there was any evidence of economic duress.

Briggs C.J. agreed that there was no evidence of duress. He held that the extrinsic evidence revealed an additional consideration consistent with that stated in the guarantee. He found the additional consideration in the " whole arrangement " to which the parties came on the 4th May 1973, the date of the guarantee. He was for dismissing the appeal.

There are three significant features in these judgments. First, all four judges are agreed that the consideration expressed in the written guarantee of the 4th May 1973 was a past consideration not, by itself, capable of supporting the defendants' promise of indemnity. This, being a question of construction of a written contract, is a decision upon a point of law. It is the subject of a vigorous challenge mounted for the first time in the appeal to this Board. Secondly, three of the four judges held the extrinsic evidence admissible, expressing the opinion that the additional consideration revealed by it was not inconsistent with the terms of the written guarantee. Two judges, however, held that it would be contrary to public policy to recognise as valid the consideration revealed by the extrinsic evidence. Finally, all the judges negatived on the facts the defendants' case of economic duress.

The Questions for the Board

Three questions call for decision by their Lordships' Board:—

(1) does the guarantee upon its proper construction state a valid consideration for the Laus' promise of indemnity?

(2) does the extrinsic evidence as to the circumstances in which the guarantee was given establish the existence of a valid consideration additional to the consideration, if any, stated in the agreement?

(3) if there be consideration for the promise of indemnity, is the guarantee nevertheless unenforceable, the consent of the Laus having been induced by duress?

Upon the third question there are concurrent findings of fact. It would have to be shown, therefore, that the judges below had misconceived the relevant law before the Board could reverse their unanimous rejection of the defendants' case based on economic duress.

The Facts

In February 1973 the plaintiffs—the Paos—owned the issued share capital of the Tsuen Wan Shing On Estate Company Ltd., a private company incorporated in Hong Kong. The defendants—the Laus—were at that time the majority shareholders in the Fu Chip Investment Company Limited. Fu Chip had been incorporated in January 1973 and " went public " on the 9th February 1973, when permission to deal in its shares was granted by the Far East Stock Exchange. The principal asset of the Shing On company was a 21-storey building under construction—the Wing On building. The Paos were keen to realise the

value of the building by selling the shares of the company. The Laus were keen to extend the property-holding of Fu Chip, an investment company. There were discussions between the Paos and the Laus on or about the 21st February. On Tuesday, 27th February, all was settled and two written agreements were signed.

The first (known as " the main agreement ") was a contract for the sale by the Paos of their shares in the Shing On company to Fu Chip. The parties to the agreement were the Paos as vendors, Fu Chip as purchasers, and the Shing On company, whose total issued share capital was to be transferred to Fu Chip. The price payable by Fu Chip was $10·5m., and was to be met by the allotment to the Paos of 4·2m. ordinary shares of $1 each in Fu Chip. It was provided that the market value of a Fu Chip share for the purpose of the agreement was to be deemed to be $2·50 for each $1 share. Completion was to be on or before the 31st March 1973. It was stipulated that time should " in every respect be the essence of this Agreement ". The parties did, however, agree on the 28th March to defer the date for completion to the 30th April 1973.

These provisions had the effect that no cash was to pass under the agreement. The whole of the price was to be satisfied by the issue of shares. The Paos gave Fu Chip an undertaking as to the way they would deal with the shares to be allotted to them. They undertook, by clause 4(k) of the agreement, that—

> " Each of the Vendors shall retain in his own right in Fu Chip 60% of the shares allotted to him under this Agreement and shall not sell or transfer the same on or before the end of April 1974 ".

In other words, the Paos gave an undertaking to Fu Chip that they would not sell or transfer before the end of April 1974 2·5m. of the 4·2m. shares to be issued to them in satisfaction of the price of $10.5m. The restriction was of great importance to the Laus, as majority shareholders in Fu Chip. As Lau said in evidence, the Paos must support the Fu Chip shares. He feared that heavy selling by the Paos could depress the market, and so the value of his shareholding in Fu Chip. Not unreasonably the Paos wanted a measure of protection before agreeing to the restriction. They wanted from the man, for whose benefit the undertaking was given, a guarantee " against a fall in value of the shares during the year in which they could not sell ". When Mrs. Pao asked Lau " what happened if shares dropped below $2·50 ", Lau offered to sign an agreement to buy back the shares at $2·50 after one year. The trial judge said he was " inclined to believe that the first defendant's account is accurate to the extent that in the course of the discussion the plaintiffs did not object to the first defendant's offer to purchase their retained shares *as a sufficient form of guarantee* " (emphasis supplied). This finding is important because of the stress laid by McMullin and Leonard JJ. on the dishonesty of Mrs. Pao who gave evidence that the parties had orally agreed upon a guarantee. The trial judge found that she was genuinely seeking " a guarantee ". While he rejected her evidence as to the nature of the agreement reached, he did find that the Paos and Lau saw Lau's offer to buy back the shares as a form of guarantee. Indeed, when Lau came to give evidence, he described his offer as " my guarantee ".

Accordingly, the second agreement (" the subsidiary agreement "), signed also on the 27th February 1973, was a contract under which the Paos agreed to sell and Lau agreed to buy on or before the 30th April 1974 at a price of $2·50 a share 2·5m. shares in Fu Chip (being 60% of the total allotment made by Fu Chip in satisfaction of the price to be paid for its acquisition from the Paos of the issued share capital of Shing On). The commercial effect of these two agreements was remarkable. Lau had got very much the better bargain—as he himself recognised.

No cash was required of him or Fu Chip on completion. If Fu Chip shares fell below $2·50 on the 30th April 1974, the Paos would, however, be protected by the obligation upon Lau to buy back 60% of the shares at $2·50 a share. They secured, therefore, their "guarantee" against a fall in the share price. But if the price on that date was higher, the Paos still remained bound to sell back the shares at $2·50. The Paos had elected shares as their price for the issued capital of Shing On because shares could go up in value whereas cash could not, and they expected—as everyone else (including the Laus) did in February 1973—that share values would rise. Yet by the form of guarantee against a fall in the value of the shares which they accepted they deprived themselves, so far as 60% of their holding was concerned, of the very advantage which by taking their price in shares they hoped to gain—and without receiving any other benefit for having to wait a year before they could realise cash on 60% of their price. It is not surprising either that Lau thought he had the better of the bargain or that Mrs. Pao became indignant when she appreciated what she and her family had given away by the subsidiary agreement. She and her husband, therefore, made up their minds that they would not complete the main agreement unless they could substitute a guarantee by way of indemnity for the subsidiary agreement.

On the 25th April 1973 solicitors, describing themselves as acting for Shing On, wrote a letter to the solicitors for Fu Chip asking them

> "to send us on behalf of our clients a guarantee from your clients that the intended allotment of 4·2m. ordinary shares of your clients would be of the value of the sum $10·5m.".

The confusions of the letter are remarkable, but irrelevant. It was well understood that the solicitors who wrote the letter also acted for the Paos, that the solicitors who received it also acted for the Laus and that the guarantee was sought in respect of 60% only of the 4·2m. shares allotted in satisfaction of the purchase price under the main agreement. The reply was a denial of any agreement of guarantee—correct, no doubt, according to the card but not really consistent with Lau's view of the subsidiary agreement as his guarantee of 60% of the price.

The Paos now made clear that they would not complete the main agreement with Fu Chip unless the subsidiary agreement was cancelled and a true guarantee (by way of indemnity) substituted for it. Mr. Pao disappeared on a business trip to Taiwan, while Mrs. Pao remained in Hong Kong, saying there would be no completion until he had returned and considered the position. Mr. Pao returned to Hong Kong on the 29th April and immediately made plain to Lau that, as the judge put it,

> "unless a guarantee and indemnity for the price of the 2·5m. Fu Chip shares was given by the defendants the plaintiffs would not complete the main agreement with the Fu Chip".

This was serious for Lau. Fu Chip had only recently gone public. A public announcement had been made of Fu Chip's acquisition of the Wing On building by its take-over of the share capital of Shing On. If the deal fell through, the public would, Lau thought, lose confidence in Fu Chip shares.

Lau had, therefore, to decide whether to yield to the Paos' demand for the cancellation of the subsidiary agreement and for a guarantee in its place or to stand by the two agreements of the 27th February, and have Fu Chip sue for specific performance of the main agreement. The first course would enable completion to take place on or very soon after the 30th April; the second course would entail the delays of legal action, though Lau was well aware that there was no defence. Lau's problem

is best described in the words of the trial judge. After quoting Lau's evidence that he would lose a lot if Fu Chip failed to take over Shing On, the judge said:—

> "These words reflect the optimism and hope of the first defendant when he yielded to the plaintiffs' demand for a guarantee. At the time the demand was made the first defendant placed the matter in the hands of his solicitors. He had proper legal advice. He knew very well whether he gave the guarantee or not the main agreement between the Fu Chip and the plaintiffs was still valid as a separate document. The Fu Chip could have sued the plaintiffs for specific performance or for damages. Out of the original issued and paid up capital of 12,600,000 shares in the Fu Chip the first defendant owned 6,531,000 shares. In addition he had purchased more since the listing of such shares. His brother, the second defendant, owned 1,500,000 million shares. Between the two of them they owned the controlling interests of the Fu Chip. By then the first defendant had already set himself about in manipulating the price of the Fu Chip shares by buying and selling. If the defendants refused to give the guarantee on the Fu Chip shares, then the Fu Chip shares might drop a few 10 cents in price only if the general condition of the market remained bullish. It would be possible for the first defendant to push the price up again with his manipulation. The Fu Chip, after all, is an investment Company. All its assets consist of landed property. So long as the properties in the Fu Chip have been quoted in their true value the success or failure in the taking over of the Shing On could not have affected the true value of the Fu Chip shares. Whatever set back in the market price of the Fu Chip shares could not have sent them below their true value. Even if it did, the defendants might have suffered a temporary paper loss of profit but would not have suffered a financial ruin. The first defendant did threaten that the Fu Chip would sue the plaintiffs on the main agreement. However, in the end he chose to avoid litigation and yielded to the plaintiffs' demand. The first defendant must have considered the matter thoroughly in the light of the then marketing condition and formed the opinion that the risk in giving the guarantee was more apparent than real. As I have said earlier on, neither party at the time could have foreseen the stock market subsequently slumping in such manner. Had the plaintiffs realised that the prices in general in the stock market would fall to the extent as we now know then they would not even bother to demand for the guarantee. They would be quite satisfied with the subsidiary agreement. Therefore I find as a fact that when the defendants agreed to sign the guarantee neither they nor the plaintiffs envisaged a drastic fall of the market and that the defendants never expected that on the guarantee they might be required to compensate the plaintiffs in terms of millions of dollars. This was an error of judgment in a business deal. The defendants were reluctant to be deprived of a good bargain—the subsidiary agreement. But I find that they were quite prepared to take a calculated risk (which at the time appeared to be very little) in order to pacify the plaintiffs who were adamant. It was in such circumstances that the guarantee was given."

In the light of these findings it is surprising that the trial judge also found that the cancellation of the subsidiary agreement formed no part of the consideration for the giving of the guarantee on the 4th May. The judge found—no doubt, correctly—that the Paos wanted the subsidiary agreement cancelled in any event. But the existence of their desire is perfectly consistent with its cancellation and the substitution for it of a guarantee as part and parcel of a comprehensive settlement accepted

by Lau as the best and most effective way of securing early completion of the main agreement—which was his objective throughout the negotiations of the 4th May.

Their Lordships agree with the Chief Justice's analysis of those negotiations. He said:—

> "However, the cancellation was part of the arrangement for the completion of the main agreement. It was cancelled by mutual agreement as part and parcel of this: it does not stand alone. The consideration for the guarantee was the whole arrangement for the completion of the main agreement of which the cancellation of the subsidiary agreement formed part.
>
> The Judge found that the plaintiffs wanted the subsidiary agreement to be cancelled in any event. But there is no evidence that this was what the defendants wanted. The defendants agreed to the cancellation only as part of the whole arrangement. The cancellation cannot be considered in vacuo".

This analysis is supported by the evidence of Lau himself. When asked whether the subsidiary agreement was cancelled on the basis that a written guarantee would be executed and would be effective, he replied "Yes", saying that he was "forced" to regard the guarantee as a substitute for the subsidiary agreement. He went on to add the significant observation that once he had signed the guarantee he regarded it as binding.

The events of the 4th May can be very shortly stated. Lau's legal advisers produced the first draft of a contract of guarantee. It was revised by both parties, and an option inserted to enable Lau to buy back the shares, if they dropped below $2·50, and he chose to do so. According to Lau, the cancellation of the subsidiary agreement was immediately followed by the signing of the guarantee. The judge made no finding as to the sequence of events, but was satisfied that the guarantee was signed to induce the Paos to complete the main agreement. A somewhat angry discussion then ensued in which Lau was seeking some effective safeguard (*e.g.* retention of the scrip or share certificates) against the Paos defaulting on their obligation (of great importance to Lau) not to sell before the 30th April 1974. The issue was settled by the Paos giving Lau and his brother an indemnity in the event of any breach of their obligation not to sell the shares. The parties then went to the offices of Fu Chip's accountants, where they completed the transaction under the main agreement. There is no suggestion that Lau signed the contract of guarantee under protest. On the contrary, he had present his own legal advisers and, as the trial judge put it, was "quite prepared to take a calculated risk (which at the time appeared to be very little)."

During the period 4th May 1973 to 30th April 1974 share prices slumped. By the 30th April Fu Chip shares had fallen to 36 cents a share. Yet Lau allowed the Paos to continue in the belief that they had their price of $2·50 a share guaranteed by him. Nor has Lau at any time offered to restore the Paos to the "*status quo ante*"—i.e. to their position under the subsidiary agreement. Indeed it is his (remarkable) contention that neither the subsidiary agreement nor the guarantee of the 4th May has legal effect. The Paos, therefore, having accepted a year's restriction on dealing in 60% of the shares allotted to them, were left, according to his case, by the events of the 4th May without any safeguard against a fall in the market, the damaging effects of which they were powerless to forestall or diminish. If the law really compels such a conclusion, one may be forgiven for thinking that the time has come to re-consider it.

The First Question

The first question is whether upon its true construction the written guarantee of the 4th May 1973 states a consideration sufficient in law to support the Laus' promise of indemnity against a fall in value of the Fu Chip shares. The instrument is, so far as relevant, in these terms:—

"Re: Tsuen Wan Shing On Estate Company Limited

"IN CONSIDERATION of your having at our request agreed to sell all of your shares of and in the above mentioned Company whose registered office is situate at 274 Sha Tsui Road Ground Floor Tsuen Wan New Territories in the Colony of Hong Kong for the the consideration of $10.500.000:00 by the allotment of 4.200.000 ordinary shares of $1·00 each in Fu Chip Investment Company Limited whose registered office is situate at No. 33 Wing Lok Street Victoria in the said Colony of Hong Kong and that the market value for the said ordinary shares of the said Fu Chip Investment Company Limited shall be deemed as $2·50 for each of $1·00 share under an Agreement for sale and purchase made between the parties thereto and dated the 27th day of February 1973, we LAU YIU LONG ( ) of No. 152 Tin Hau Temple Road, Flat C1, Summit Court, 14th floor in the Colony of Hong Kong Merchant and BENJAMIN LAU KAM CHING ( ) of No. 31 Ming Yuen Street West, Basement in the said Colony of Hong Kong Merchant the directors of the said Fu Chip Investment Company Limited HEREBY AGREE AND GUARANTEE the closing market value for 2,520,000 shares (being 60% of the said 4,200,000 ordinary shares) of the said Fu Chip Investment Company Limited shall be at $2·50 per share and that the total value of 2,520,000 shares shall be of the sum of HK$6,300,000:00 on the following marketing date immediately after 30th day of April, 1974 AND WE FURTHER AGREE to indemnify and keep you indemnified against any damages, losses and other expenses which you may incur or sustain in the event of the closing market price for the shares of Fu Chip Investment Company Limited according to The Far East Exchange Limited shall fall short of the sum $2·50 during the said following marketing date immediately after the 30th day of April, 1974 PROVIDED ALWAYS that if we were called upon to indemnify you for the discrepancy between the market value and the said total value of HK$6,300,000:00 we shall have the option of buying from you the said 2,520,000 shares of Fu Chip Investment Company Limited at the price of HK$6,300,000:00 . . . ."

Mr. Neill, Q.C., counsel for the appellants before their Lordships' Board but not below, contends that the consideration stated in the agreement is not in reality a past one. It is to be noted that the consideration was not on the 4th May 1973 a matter of history only. The instrument by its reference to the main agreement with Fu Chip incorporates as part of the stated consideration the Paos' three promises to Fu Chip:

to complete the sale of Shing On,

to accept shares as the price for the sale,

and not to sell 60% of the shares so accepted before the 30th April 1974.

Thus, on the 4th May 1973 the performance of the main agreement still lay in the future. Performance of these promises was of great importance to the Laus, and it is undeniable that, as the instrument declares, the promises were made to Fu Chip at the request of the Laus. It is equally clear that the instrument also includes a promise by the Paos to the Laus to fulfil their earlier promises given to Fu Chip.

The Board agrees with Mr. Neill's submission that the consideration expressly stated in the written guarantee is sufficient in law to support the Laus' promise of indemnity. An act done before the giving of a promise to make a payment or to confer some other benefit can sometimes be consideration for the promise. The act must have been done at the promisors' request: the parties must have understood that the act was to be remunerated either by a payment or the conferment of some other benefit: and payment, or the conferment of a benefit, must have been legally enforceable had it been promised in advance. All three features are present in this case. The promise given to Fu Chip under the main agreement not to sell the shares for a year was at Lau's request. The parties understood at the time of the main agreement that the restriction on selling must be compensated for by the benefit of a guarantee against a drop in price: and such a guarantee would be legally enforceable. The agreed cancellation of the subsidiary agreement left, as the parties knew, the Paos unprotected in a respect in which at the time of the main agreement all were agreed they should be protected.

Mr. Neill's submission is based on *Lampleigh v. Braithwait* (1615) Hobart 105. In that case the judges said at p. 106:

> " First, . . . a meer voluntary curtesie will not have a consideration to uphold an assumpsit. But if that curtesie were moved by a suit or request of the party that gives the assumpsit, it will bind, for the promise, though it follows, yet it is not naked, but couples it self with the suit before, and the merits of the party procured by that suit, which is the difference ".

The modern statement of the law is in the judgment of Bowen L.J. in *In Re Cassey's Patents, Stewart v. Casey* [1892] 1 Ch. 104 at pp. 115–116; Bowen L.J. said:

> ". . . Even if it were true, as some scientific students of law believe, that a past service cannot support a future promise, you must look at the document and see if the promise cannot receive a proper effect in some other way. Now, the fact of a past service raises an implication that at the time it was rendered it was to be paid for, and, if it was a service which was to be paid for, when you get in the subsequent document a promise to pay, that promise may be treated either as an admission which evidences or as a positive bargain which fixes the amount of that reasonable remuneration on the faith of which the service was originally rendered. So that here for past services there is ample justification for the promise to give the third share . . .".

Conferring a benefit is, of course, an equivalent to payment: see *Chitty on Contracts*, 24th ed., I, paragraph 154.

Mr. Leggatt, Q.C., for the respondents, does not dispute the existence of the rule but challenges its application to the facts of this case. He submits that it is not a necessary inference or implication from the terms of the written guarantee that any benefit or protection was to be given to the Paos for their acceptance of the restriction on selling their shares. Their Lordships agree that the mere existence or recital of a prior request is not sufficient in itself to convert what is *prima facie* past consideration into sufficient consideration in law to support a promise: as they have indicated, it is only the first of three necessary preconditions. As for the second of those preconditions, whether the act done at the request of the promisor raises an implication of promised remuneration or other return is simply one of the construction of the words of the contract in the circumstances of its making. Once it is recognised, as the Board considers it inevitably must be, that the expressed consideration includes a reference to the Paos' promise not to sell the shares before the 30th April 1974—a promise to be performed in the future, though given in the past—it is not

possible to treat the Laus' promise of indemnity as independent of the Paos' antecedent promise, given at Lau's request, not to sell. The promise of indemnity was given because at the time of the main agreement the parties intended that Lau should confer upon the Paos the benefit of his protection against a fall in price. When the subsidiary agreement was cancelled, all were well aware that the Paos were still to have the benefit of his protection as consideration for the restriction on selling. It matters not whether the indemnity thus given be regarded as the best evidence of the benefit intended to be conferred in return for the promise not to sell, or as the positive bargain which fixes the benefit on the faith of which the promise was given—though where, as here, the subject is a written contract, the better analysis is probably that of the "positive bargain". Their Lordships, therefore, accept the submission that the contract itself states a valid consideration for the promise of indemnity.

This being their Lordships' conclusion, it is unnecessary to consider Mr. Neill's further submission (also raised for the first time before the Board) that the option given the Laus, if called upon to fulfil their indemnity, to buy back the shares at $2·50 a share was itself a sufficient consideration for the promise of indemnity. But their Lordships see great force in the contention. The Laus promised to indemnify the plaintiffs if the market price of Fu Chip shares fell below $2·50. However, in the event of the Laus being called on to implement this promise they were given an option to take up the shares themselves at $2·50. This on the face of it imposes on the plaintiffs in the circumstances envisaged an obligation to transfer the shares to the Laus at the price of $2·50 if called on to do so. The concomitant benefit to the Laus could be a real one—for example, if they thought that the market, after a temporary set-back, would recover to a price above $2·50. The fact that the option is stated in the form of a proviso does not preclude it being a contractual term or one under which consideration moves.

The Second Question

There is no doubt—and it was not challenged—that extrinsic evidence is admissible to prove the real consideration where:

(*a*) no consideration, or a nominal consideration, is expressed in the instrument, or

(*b*) the expressed consideration is in general terms or ambiguously stated, or

(*c*) a substantial consideration is stated, but an additional consideration exists.

The additional consideration must not, however, be inconsistent with the terms of the written instrument. Extrinsic evidence is also admissible to prove the illegality of the consideration. In their Lordships' opinion the law is correctly stated in *Halsbury, Laws of England*, 4th edition, Volume 12, paragraph 1487.

The extrinsic evidence in this case shows that the consideration for the promise of indemnity, while it included the cancellation of the subsidiary agreement, was primarily the promise given by the Paos to the Laus, to perform their contract with Fu Chip, which included the undertaking not to sell 60% of the shares allotted to them before the 30th April 1974. Thus the real consideration for the indemnity was the promise to perform, or the performance of, the Paos' pre-existing contractual obligations to Fu Chip. This promise was perfectly consistent with the consideration stated in the guarantee. Indeed, it reinforces it by imposing upon the Paos an obligation now owed to the Laus to do what, at Lau's request, they had agreed with Fu Chip to do.

Their Lordships do not doubt that a promise to perform, or the performance of, a pre-existing contractual obligation to a third party can

be valid consideration. In *New Zealand Shipping Co. Ltd. v. Satterthwaite Ltd. (The Eurymedon)* [1975] A.C. 154 the rule and the reason for the rule were stated as follows (p. 168):

> " 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: . . . the promisee obtains the benefit of a direct obligation . . . . This proposition is illustrated and supported by *Scotson v. Pegg* (1861) 6 H & N. 295 which their Lordships consider to be good law ".

Unless, therefore, the guarantee was void as having been made for an illegal consideration or voidable on the ground of economic duress, the extrinsic evidence establishes that it was supported by valid consideration.

Mr. Leggatt for the respondents submits that the consideration is illegal as being against public policy. He submits that to secure a party's promise by a threat of repudiation of a pre-existing contractual obligation owed to another can be, and in the circumstances of this case was, an abuse of a dominant bargaining position and so contrary to public policy. This, he submits, is so even though economic duress cannot be proved.

This submission found favour with the majority in the Court of Appeal. Their Lordships, however, consider it misconceived. Reliance was placed on the old " seaman " cases of *Harris v. Watson* (1791) Peake 102 and *Stilk v. Meyrick* (1809) 6 Esp. 129 and 2 Camp. 317. Counsel, also, referred to certain developments in American law, which are to be found described in two leading works, *Corbin on Contracts* and *Williston on Contracts*. The relevant passages are *Corbin*, Vol. I, Chap. 7, and *Williston*, Chap. 47. Their Lordships would make one general observation on what is revealed by these two distinguished American works. Where some judges speak of public policy, others speak of economic duress. No clear line of distinction between the two concepts emerges as settled in the American law.

In the seaman cases there were only two parties—the seaman and the captain (representing the owner). In *Harris v. Watson* the captain during the voyage, for which the plaintiff had contracted to serve as a seaman, promised him five guineas over and above his common wages if he would perform some extra work. Lord Kenyon thought that if the seaman's claim to be paid the five guineas was supported " it would materially affect the navigation of this kingdom ". He feared the prospect of seamen in times of danger insisting " on an extra charge on such a promise ", and non-suited the plaintiff. In *Stilk v. Meyrick* Lord Ellenborough also non-suited the seaman. According to the report in 2 Campbell 317 he said:

> " I think *Harris v. Watson* was rightly decided; but I doubt whether the ground of public policy, upon which Lord Kenyon is stated to have proceeded, be the true principle on which the decision is to be supported. Here, I say, the agreement is void for want of consideration ".

Espinasse, who appeared as junior counsel for the unsuccessful plaintiff in the case, reports the case somewhat differently. He reports (p. 130) Lord Ellenborough as saying that

> ". . . he recognised the principle of the case of *Harris v. Watson* as founded on just and proper policy."

But the report continues—

> " when the defendant [*sic*—but surely the plaintiff is meant?] entered on board the ship, he stipulated to do all the work his situation called upon him to do ".

These cases, explicable as they are upon the basis of an absence of fresh consideration for the captain's promise, are an unsure foundation for a rule of public policy invalidating contracts where, save for the rule, there would be valid consideration.

When one turns to consider cases where a pre-existing duty imposed by law is alleged to be valid consideration for a promise, one finds cases in which public policy has been held to invalidate the consideration. A promise to pay a sheriff in consideration of his performing his legal duty, a promise to pay for discharge from illegal arrest, are to be found in the books as promises which the law will not enforce: see the cases cited in footnote 2, paragraph 326, *Halsbury, Laws of England*, 4th edition, Volume 9. Yet such cases are also explicable upon the ground that a person who promises to perform, or performs, a duty imposed by law provides no consideration. In cases where the discharge of a duty imposed by law has been treated as valid consideration, the courts have usually (but not invariably) found an act over and above, but consistent with, the duty imposed by law: see *Williams v. Williams* [1957] 1 W.L.R. 148. It must be conceded that different judges have adopted differing approaches to such cases: contrast, for example, Denning L.J. at p. 149 *et seq.* with the view of the majority in *Williams'* case.

But, where the pre-existing obligation is a contractual duty owed to a third party, some other ground of public policy must be relied on to invalidate the consideration (if otherwise legal); the respondents submit that the ground can be extortion by the abuse of a dominant bargaining position to threaten the repudiation of a contractual obligation. It is this application of public policy which Mr. Leggatt submits has been developed in the American cases. Beginning with the general rule that " neither the performance of duty nor the promise to render a performance already required by duty is a sufficient consideration " the courts have (according to *Corbin on Contracts* I, paragraph 171) advanced to the view " that the moral and economic elements in any case that involves the rule should be weighed by the court, and that the fact of pre-existing legal duty should not be in itself decisive ".

The American Law Institute in its Restatement of the law of contracts (para. 84D) has declared that performance (or promise of performance) of a contractual duty owed to a third person is sufficient consideration. This view (which accords with the statement of our law in *Satterthwaite's* case *supra*) appears to be generally accepted but only in cases where there is no suggestion of unfair economic pressure exerted to induce the making of what *Corbin* (*op. cit.*) calls " the return promise ".

Their Lordships' knowledge of this developing branch of American law is necessarily limited. In their judgment it would be carrying audacity to the point of foolhardiness for them to attempt to extract from the American case law a principle to provide an answer to the question now under consideration. That question, their Lordships repeat, is whether, in a case where duress is not established, public policy may nevertheless invalidate the consideration if there has been a threat to repudiate a pre-existing contractual obligation or an unfair use of a dominating bargaining position.

Their Lordships' conclusion is that where businessmen are negotiating at arm's length it is unnecessary for the achievement of justice, and unhelpful in the development of the law, to invoke such a rule of public policy. It would also create unacceptable anomaly. It is unnecessary because justice requires that men, who have negotiated at arm's length, be held to their bargains unless it can be shown that their consent was vitiated by fraud, mistake or duress. If a promise is induced by coercion of a man's will, the doctrine of duress suffices to do justice. The party

coerced, if he chooses and acts in time, can avoid the contract. If there is no coercion, there can be no reason for avoiding the contract where there is shown to be a real consideration which is otherwise legal.

Such a rule of public policy as is now being considered would be unhelpful because it would render the law uncertain. It would become a question of fact and degree to determine in each case whether there had been, short of duress, an unfair use of a strong bargaining position.

It would create anomaly because, if public policy invalidates the consideration, the effect is to make the contract void. But unless the facts are such as to support a plea of " *non est factum* ", which is not suggested in this case, duress does no more than confer upon the victim the opportunity, if taken in time, to avoid the contract. It would be strange if conduct less than duress could render a contract void, whereas duress does no more than render a contract voidable. Indeed, it is the Laus' case in this appeal that such an anomaly is the correct result. Their case is that the Paos, having lost by cancellation the safeguard of the subsidiary agreement, are without the safeguard of the guarantee because its consideration is contrary to public policy, and that they are debarred from restoration to their position under the subsidiary agreement because the guarantee is void, not voidable. The logical consequence of Mr. Leggatt's submission is that the safeguard which all were at all times agreed the Paos should have—the safeguard against fall in value of the shares—has been lost by the application of a rule of public policy. The law is not, in their Lordships' judgment, reduced to countenancing such stark injustice: nor is it necessary, when one bears in mind the protection offered otherwise by the law to one who contracts in ignorance of what he is doing or under duress. Accordingly, the submission that the additional consideration established by the extrinsic evidence is invalid on the ground of public policy is rejected.

The Third Question

Duress, whatever form it takes, is a coercion of the will so as to vitiate consent. Their Lordships agree with the observation of Kerr J. in *The " Siboen " and the " Sibotre "* [1976] 1 Lloyd's Rep. 293 at p. 336 that in a contractual situation commercial pressure is not enough. There must be present some factor " which could in law be regarded as a coercion of his will so as to vitiate his consent ": *loc. cit.* This conception is in line with what was said in this Board's decision in *Barton v. Armstrong* [1976] A.C. 104 at p. 121 by Lord Wilberforce and Lord Simon of Glaisdale—observations with which the majority judgment appears to be in agreement. In determining whether there was a coercion of will such that there was no true consent, it is material to inquire whether the person alleged to have been coerced did or did not protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have an alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it. All these matters are, as was recognised in *Maskell v. Horner* [1915] 3 K.B. 106, relevant in determining whether he acted voluntarily or not.

In the present case there is unanimity amongst the judges below that there was no coercion of Lau's will. In the Court of Appeal the trial judge's finding (already quoted) that Lau considered the matter thoroughly, chose to avoid litigation, and formed the opinion that the risk in giving the guarantee was more apparent than real was upheld. In short, there was commercial pressure, but no coercion. Even if this Board was disposed, which it is not, to take a different view, it would not substitute its opinion for that of the judges below on this question of fact.

It is, therefore, unnecessary for the Board to embark upon an inquiry into the question whether English law recognises a category of duress known as "economic duress". But, since the question has been fully argued in this appeal, their Lordships will indicate very briefly the view which they have formed. At common law money paid under economic compulsion could be recovered in an action for money had and received: *Astley v. Reynolds* (1731) 2 Str. 915. The compulsion had to be such that the party was deprived of "his freedom of exercising his will" (at p. 916). It is doubtful, however, whether at common law any duress other than duress to the person sufficed to render a contract voidable: see I *Blackstone's Commentaries* 12th ed. pp. 130–131 and *Skeate v. Beale* (1841) 11 Ad. and E. 983. American law (*Williston, op. cit.*) now recognises that a contract may be avoided on the ground of economic duress. The commercial pressure alleged to constitute such duress must, however, be such that the victim must have entered the contract against his will, must have had no alternative course open to him, and must have been confronted with coercive acts by the party exerting the pressure: *Williston, op. cit.* paragraph 1603. American judges pay great attention to such evidential matters as the effectiveness of the alternative remedy available, the fact or absence of protest, the availability of independent advice, the benefit received, and the speed with which the victim has sought to avoid the contract. Recently two English judges have recognised that commercial pressure may constitute duress the pressure of which can render a contract voidable: Kerr J. in *The Siboen* (*supra*) and Mocatta J. in *North Ocean Shipping Co. Ltd. v. Hyundai Construction Co. Ltd.* [1978] 3 All E.R. 1170. Both stressed that the pressure must be such that the victim's consent to the contract was not a voluntary act on his part. In their Lordships' view, there is nothing contrary to principle in recognising economic duress as a factor which may render a contract voidable, provided always that the basis of such recognition is that it must amount to a coercion of will, which vitiates consent. It must be shown that the payment made or the contract entered into was not a voluntary act.

For these reasons their Lordships will humbly advise Her Majesty that the appeal be allowed and that the judgment of the trial judge be restored with interest up to the date of Her Majesty's Order in Council disposing of this appeal. The respondents must pay the appellants' costs here and below.

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In the Privy Council

PAO ON AND OTHERS

v.

LAU YIU LONG AND ANOTHER

DELIVERED BY LORD SCARMAN

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