

INCAPACITY

Extract from JC Smith, *Smith & Thomas: A Casebook on Contract*, Eleventh Edition, 2000, Chapter 17.

The general rule of English law is that any person is competent to bind himself to any contract he chooses to make, provided that it is not illegal or void for reasons of public policy. (See below, Chapter 19.) At common law there are exceptions to this rule in the case of corporations, minors, married women, mentally incompetent and intoxicated persons. The exceptions are now greatly reduced in scope. A series of statutes from 1870 to 1949 abolished the married woman's disabilities and she now enjoys full contractual capacity. The present state of the other exceptions requires a little further explanation.

(a) CORPORATIONS

A corporation created by Royal Charter has always had the same contractual capacity as an ordinary person but a company incorporated under the Companies Act could, until recently, only make such contracts as were within the scope of the objects set out in its memorandum of association. Anything beyond that was *ultra vires* and void.

In the leading case of *Ashbury Railway Carriage and Iron Co. Ltd v. Riche* (1875) L.R. 7 H.L. 653 the objects set out in the company's memorandum were "to make and sell, or lend on hire, railway carriages and waggons, and all kinds of railway plant, fittings, machinery and rolling stock; to carry on the business of mechanical engineers and general contractors; to purchase, lease, work and sell mines, minerals, land and buildings; to purchase and sell as merchants, timber, coal, metals, or other materials, and to buy any such materials on commission or as agents." The directors purchased a concession for making a railway in Belgium and purported to contract with Riche that he should have the construction of the line. Riche's action for breach of the alleged contract failed since the House of Lords held that the construction of a railway, as distinct from rolling stock, was *ultra vires* the company and that therefore the contract was void. Even if every shareholder of the company had expressed his approval of the act, it would have made no difference, for it was an act which the company had no power, in law, to do. Important changes were made by section 108 of the Companies Act 1989, substituting a new section 35 of the Companies Act 1985. Under that new section it remains the duty of the directors to observe any limitations on their powers flowing from the company's memorandum (section 35(3)) and a member of a company may bring proceedings to restrain the doing of an act in excess of those powers (section 35(2)); but, by section 35(1):

"The validity of an act done by a company shall not be called into question on the ground of lack of capacity by reason of anything in the company's memorandum."

So, by applying the modern law to the *Ashbury* case, the directors committed a breach of duty by making the contract and might have been restrained by action by a member; but once the contract was made its validity could not be questioned provided that the making of the contract was "an act done by the company." It might be objected that it was not such an act because the directors had no power to make the contract. This objection is met by section 35A(1):

"In favour of a person dealing with a company in good faith, the power of the board of directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitation under the company's constitution."

A person is presumed to have acted in good faith unless the contrary is proved and is not to be regarded as acting in bad faith merely because he knows the act is beyond the directors' powers. An *ultra vires* act by the directors may now be ratified, but only by special resolution which does not affect any liability incurred by the directors or any other person—any such relief must be agreed to separately by special resolution.

Formerly a corporation's contracts were invalid unless made under the corporate seal but, since the Corporate Bodies' Contracts Act 1960, a corporation may make contracts in the same manner as a natural person—that is the contract may be made orally unless a special rule requires a written contract—as in contracts for the sale or disposition of an interest in land—or evidence in writing—as in the case of a guarantee within section 4 of the Statute of Frauds 1677.

(b) MINORS

At common law persons under the age of 21 were designated “infants” and had only a limited capacity to contract. From January 1, 1970, the Family Law Reform Act 1969 reduced the age of majority to 18 and authorised the term “minor” as an alternative to “infant.” “Minor” is now the preferred term. The capacity of a minor to contract is still regulated by the common law, modified by the Minors’ Contracts Act 1987 which repealed a troublesome statute, the Infants Relief Act 1874.

The general principle is that a contract made by a minor with an adult is binding on the adult but not on the minor. If, after attaining his majority, he ratifies it by an act confirming the promise he made when a minor, he is bound. There need be no consideration for the act of ratification. A contract by a minor is not void and any money or property transferred by him under the contract can be recovered only if there has been a total failure of consideration. There are three exceptional cases where a minor is to some extent bound.

Necessaries. A minor is bound to pay for necessities supplied to him under a contract. The Sale of Goods Act 1979 s.3, re-enacting the Act of 1893, provides:

“... where necessities are sold and delivered to an infant (or minor) ... he must pay a reasonable price therefor.

‘Necessaries’ in this section means goods suitable to the condition of life of such infant (or minor) ... and to his actual requirements at the time of sale and delivery.”

“Necessaries” are those things without which a person cannot reasonably exist and include food, clothing, lodging, education or training in a trade and essential services. The “condition of life” of the minor means his social status and his wealth. What is regarded as necessary for the minor residing in a stately home may be unnecessary for the resident of a council flat. Whatever the minor’s status, the goods must be suitable to his actual requirements—if he already has enough fancy waistcoats, more cannot be necessary: *Nash v. Inman* [1908] 2 KB 1, CA.

The nature of the minor’s liability for necessary goods is uncertain. The fact that the Sale of Goods Act makes him liable only for goods “sold and delivered” and to pay, not any agreed price, but a reasonable price, suggests quasi-contractual liability—he must pay, not because he has contracted to do so, but because the law requires him to recompense the seller for a benefit conferred and accepted. Some dicta support this view but others treat the minor’s liability as contractual. In *Roberts v Gray* [1913] KB 520, CA, a minor was held liable for his failure to perform a contract for a tour with the plaintiff, a noted billiards player. It was a contract for the instruction of the minor. The contract was wholly executory and but it was held that the contract was binding on him from its formation. It may be thought that there is a distinction between necessary goods and necessary services but this is difficult to justify logically or historically. Perhaps the contract in *Roberts v. Gray* belongs more properly to the category of beneficial contracts of service, below.

A contract is not binding on a minor merely because it is proved to be for the minor’s benefit; but a contract which would otherwise be binding as a contract for necessities is not so if it contains harsh and onerous terms: *Fawcett v. Smethurst* (1914) 84 LK 473, (Atkin J).

Beneficial contracts of service. It is for the minor’s benefit that he should be able to obtain employment which would be difficult if he could not make a binding contract. The law allows him to do so, provided that the contract, taken as a whole, is manifestly for his benefit. So where a young railway porter agreed to join an insurance scheme and to forgo any claims he might have under the Employers’ Liability Act, he had forfeited his rights under the Act, the contract as a whole being for his benefit: *Clements v London & North Western Railway* [1894] 2 QB 482, CA. Contracts enabling a minor to pursue a career as a professional boxer and as an author have been held binding as being for their benefit.

Acquisition of property with obligations. When a minor acquires “a subject of a permanent nature ... with certain obligations attached to it”—such as a leasehold, or shares in a company—he is bound by the obligations as long as he retains the subject. He must pay the rent or calls on the shares: *London & North Western Railway v M’Michael* (1850) 5 Ex 114. The contract is voidable by the minor—he may repudiate it any time during his minority or within a reasonable time thereafter. It is uncertain whether avoidance here means rescission *ab initio* or avoidance of only future obligations; but, whether it is retrospective or not, it seems that the minor cannot recover money which he has already paid unless there has been a total failure of consideration: *Steinberg v. Scala Ltd* [1923] 2 Ch 452, CA.

Restitution by a minor. Where a minor has obtained property under a contract which is not enforceable against him, the adult party who can neither sue for the price nor get the property back may suffer an injustice. Even where the minor has lied about his age, no action in deceit will lie because this would, in effect, enable the contract to be enforced against him; and for the same reason it is improbable that the minor would be estopped from asserting his true age. The Minors' Contracts Act 1987, s3, now affords a limited measure of redress. Where a contract made after the commencement of the Act is unenforceable against a defendant because he was a minor when it was made:

“... the court may, if it is just and equitable to do so, require the defendant to transfer to the plaintiff any property acquired by the defendant under the contract or any property representing it.”

This may assist the plaintiff where the property is identifiable but where the plaintiff has loaned the money it will usually not be. The plaintiff will then be able to recover in equity only if he is able to prove that he loaned the money for the express purpose of enabling the minor to buy necessities and that he in fact did so: *Lewis v Alleyne* (1888) 4 TLR 560.

The 1987 Act, s2, provides “Nothing in this section shall be taken to prejudice any other remedy available to the plaintiff.” The plaintiff might rely on the equitable doctrine which required a fraudulent minor to return property which he had obtained by deception and which was still identifiable in his possession: *R. Leslie Ltd v. Shiell* [1914] 3 KB 607, CA; but it is not clear that there would be any advantage in doing so, since the remedy under section 2 appears to overlap the equitable remedy and does not require proof of fraud.

Guarantee of a minor's contract. Section 3 of the 1987 Act provides that a guarantee of a minor's contract is not unenforceable against the guarantor merely because the contract made by the minor is unenforceable against him on the ground that he is a minor. The section does not apply if the contract made by the minor is unenforceable against him for some other reason, for example misrepresentation or duress by the adult party. In such a case the guarantor would not be bound.

(c) MENTAL INCOMPETENTS

The ancient rule of the common law was that a lunatic could not set up his own insanity (though his heir might) so as to avoid an obligation which he had undertaken. But by 1847 Pollock C.B. was able to say, in delivering the judgment of the Court of Exchequer Chamber in *Moulton v. Camroux*, 2 Ex 487, that “the rule had in modern times been relaxed, and unsoundness of mind would now be a good defence to an action upon a contract, if it could be shown that the defendant was not of the capacity to contract ‘and the plaintiff knew it.’” Cf. *Imperial Loan Co. v. Stone* [1892] 1 QB 599, CA. Section 3 of the Sale of Goods Act 1979 makes the same provision for persons who are incompetent to contract by reason of mental incapacity as for minors (see above).

A lunatic so found by inquisition was held to be incapable of making a valid *inter vivos* disposition of property (although he could make a valid will) since this would be inconsistent with the position of the Crown under the Lunacy Acts: *Re Walker* [1905] 1 Ch 160. Presumably the position of a lunatic so found with respect to contracts not effecting *inter vivos* dispositions of his property was the same as that of a lunatic not so found; that is, he would be bound unless he could show that he was not in fact of capacity to contract and that the plaintiff knew it. The Lunacy Acts have been repealed, but an order under the Mental Health Act 1983, may have the same effect as a finding of lunacy.

(d) INTOXICATED PERSONS

The authorities are scanty; but in *Gore v. Gibson* (1845) 13 M & W 621; 153 ER 260, it was held that a contract made by a person so intoxicated as not to know the consequences of his act is not binding on him if his condition is known to the other party. It appears, however, that such a contract is not void but merely voidable, for it was held in *Matthews v. Baxter* (1873) LR 8 Ex 132 that if the drunken party, upon coming to his senses, ratifies the contract, he is bound by it.

Section 3 of the Sale of Goods Act 1979 makes the same provision for persons who are incompetent to contract by reason of “drunkenness” as for minors and the mentally incompetent. No doubt, the same rule would be applied to persons intoxicated by drugs other than alcoholic drink, either by a broad interpretation of “drunkenness,” or at common law.