

ILLEGALITY

INTRODUCTION

WARNING: Illegality is the most confusing area within the law of contract, primarily because it lacks structure. For example, the ILEx Coursebook states that “Authors have always had trouble in classifying the separate heads of illegality” (at 11.1), and, on the effects of illegality, that “The law on this area is completely unsatisfactory and full of contradictions” (at 11.5).

1. CONTRACTS RENDERED ILLEGAL BY STATUTE OR THE COMMON LAW

A contract may be expressly forbidden by a statutory provision. (See below for examples)

Certain contracts are regarded as illegal at common law on the ground that they would be harmful to society and therefore contrary to public policy. Such contracts are as follows:

(1) *CONTRACTS TO COMMIT A CRIME OR CIVIL WRONG*

If a contract has as its object the deliberate commission of a crime, then it is illegal and the courts will not enforce it.

If the contract is to deliberately commit a civil wrong it is illegal and unenforceable. However, if the parties are ignorant of the fact that by the contract they are committing a civil wrong, then it is not illegal. If one of the parties to the contract knows that the contract is illegal, then only the innocent party is entitled to rely on the contract (*Clay v Yates* [1856] 1 H&N 73).

(2) *CONTRACTS TENDING TO LEAD TO CORRUPTION IN PUBLIC LIFE*

A contract for the acquisition of a title of honour or for the sale of public office will be illegal (*Parkinson v College of Ambulance* [1925] 2 KB 1).

(3) *CONTRACTS PROMOTING SEXUAL IMMORALITY*

A contract which directly or indirectly promotes sexual immorality is illegal. For example, the hire of a carriage to a known prostitute so that she could ply her trade more effectively was considered illegal unless the hirer was ignorant of the intended use in *Pearce v Brooks* [1866] LR 1 Ex 213.

(4) *CONTRACTS PREJUDICIAL TO THE ADMINISTRATION OF JUSTICE*

A contract tending to affect the administration of justice is illegal and void. For example, an agreement not to appear at the public examination of a bankrupt nor to oppose his discharge.

(5) *CONTRACTS PREJUDICIAL TO PUBLIC SAFETY*

Under the Trading with the Enemy Act 1939, it is an offence to trade or attempt to trade with the enemy. Such contracts are therefore illegal.

Where a contract has as its object the doing of an act which is illegal by the law of a friendly foreign country, it is illegal and void (*Foster v Driscoll* [1929] KB 470).

(6) *OTHER CONTRACTS*

There are many other examples of contracts which would offend public policy such as unduly restricting personal liberty (*Horwood v Millar's Timber* [1917] 1 KB 305) and contracts to defraud the Inland Revenue (*Miller v Karlinski* (1945) 62 TLR 85).

(7) *UNLAWFUL MANNER OF PERFORMANCE*

A contract may be lawful in its formation but performed by the parties in an illegal manner. Such a contract will become unlawful. Two contrasting cases are *Anderson v Daniel* [1924] 1 KB 138 and *Archbalds (Freitage) Ltd v Spanglett Ltd* [1961] 1 All ER 417.

The test for determining the legality or illegality of a contract that would otherwise be lawful but for the fact that its performance involved a breach of a statute was laid down in *St John's Shipping Corp v Rank Ltd* [1957] 3 All ER 683, ie did the statute intend to penalise only conduct or did it intend also to prohibit the contract itself?

2. CONTRACTS RENDERED VOID ON GROUNDS OF PUBLIC POLICY

Certain contracts are expressly declared to be void by statute. For example, wagering contracts are rendered void by the Gaming Act 1845.

Certain contracts are void at common law on the grounds of public policy:

(1) *CONTRACTS WHICH OUST THE JURISDICTION OF THE COURTS*

Any contract which attempts to deprive the courts of a jurisdiction which they otherwise would have is void. For example, the House of Lords decided in *Hyman v Hyman* [1929] AC 601, that a wife could not validly contract with her husband not to apply for maintenance on a divorce, and that a contract of that kind did not prevent her from applying.

(2) *CONTRACTS PREJUDICIAL TO THE STATUS OF MARRIAGE*

A contract which attempts to restrain or prevent a party from marrying is void and against public policy (*Lowe v Peers* (1768) 4 Burr 2225).

Marriage brokerage contracts (agreements to procure the marriage between two parties) are against public policy and void (*Hermann v Charlesworth* [1905] 2 KB 123). What is the status of contracts between marriage bureaux and their clients?

(3) *CONTRACTS IN RESTRAINT OF TRADE*

All covenants in restraint of trade are prima facie void and unenforceable at common law. They only become enforceable if they are shown to be reasonable as between the parties and to be in the public interest (*Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co* [1894]).

Many employment contracts contain clauses restricting employees' activities during the course of employment and after its termination. Restraint clauses also appear in commercial dealings between businesses such as where the purchaser of a business wishes to protect its goodwill.

See separate Handout.

3. THE CONSEQUENCES OF THE VARIOUS FORMS OF ILLEGALITY

GH Treitel, *The Law of Contract* (9th edition, 1995) has classified the effects of illegality into two parts: (1) Enforcement, and (2) Restitution.

(1) ENFORCEMENT

The court will never “enforce” an illegal contract in the sense of ordering a party actually to do something that is unlawful or contrary to public policy. However, in certain circumstances a party may be able to claim damages on the contract. The law on this question is complex and not very satisfactory.

(A) POSITION OF GUILTY PARTY

An illegal contract cannot be enforced by a guilty party. Thus a person who hires a hall to deliver blasphemous lectures cannot sue for possession (*Cowan v Milburn* (1867)); a landlord who lets premises with guilty intent cannot sue for rent (*Alexander v Rayson* (1936)); and the owner of a brougham knowingly let to a prostitute for the purpose of her profession cannot sue for hire (*Pearce v Brooks* (1866)).

The severity of the rule that a guilty party cannot enforce an illegal contract is mitigated in two ways:

- (i) The rule only prevents a guilty party from enforcing *the contract*: it does not prevent him from recovering damages in tort where the other party's conduct constitutes, not merely a breach of the illegal contract, but also an independent tort. See: *Saunders v Edwards* [1987] 1 WLR 1116.
- (ii) There is some latitude in determining who is a “guilty” party where the illegality lies in the method of performance. For the present purposes, a party is not guilty because he performs a contract in an unlawful manner. See: *St John Shipping Corp v Rank Ltd* [1957] 1 QB 267.

Where the intention that one party should do an unlawful (or immoral) act exists at the time of contracting, even the other party may be unable to sue on the contract. See: *Ashmore & Co v Dawson Ltd* [1973] 1 WLR 828.

(B) POSITION OF INNOCENT PARTY

For the present purpose, a person may be “innocent” because he is mistaken, or ignorant, about either the law or the facts.

- (i) Ignorance or mistake of law does not, in general, give a party the right to enforce a contract which is affected by illegality.
- (ii) A party may be innocent in the sense of being unaware of, or mistaken about, the facts which give rise to the illegality. The right of such a party to enforce the contract has been upheld in some cases but denied in others; even where it has been denied, other remedies may be available to the innocent party.

Cases upholding the innocent party's claim include *Bloxsome v Williams* (1824) 3 B&C 232 and *Archbalds (Freightage) Ltd v Spanglett Ltd* [1961] 1 QB 374.

Cases rejecting the innocent party's claim include the leading case of *Re Mahmoud and Ispahani* [1921] 2 KB 716.

- (iii) The innocent party may have three other remedies. First, the innocent party may be able to recover damages for breach of “collateral warranty” (See *Strongman v Sincock* [1955]). Secondly, the innocent party may be able to recover damages for misrepresentation (See *Shelley v Paddock* [1980]). Thirdly,

innocence may be material in an action for the recovery of money paid or property transferred under an illegal contract.

(2) RESTITUTION

A person who cannot enforce an illegal contract may instead claim restitution in respect of money paid, property transferred or services rendered by him under the contract.

The general rule is that money paid or property transferred under an illegal contract cannot be recovered back (for example, see *Parkinson v College of Ambulance* (1925)).

In practice however, the general rule is subject to many exceptions:

(A) CLASS-PROTECTING STATUTES

If a contract is made illegal by a statute passed for the protection of a class of persons, a member of that class can recover back money paid or property transferred by him under the contract. Some statutes expressly provide that a member of a protected class shall be entitled to recover back money paid or property transferred under an illegal contract.

For example, under s125 of the Rent Act 1977, the payment of a premium in consideration of being granted a tenancy is illegal and an offence, and is expressly stated to be recoverable by the paying party, that is, the tenant.

(B) OPPRESSION

A person can recover back money paid or property transferred under an illegal contract if he was forced by the other party to enter into the contract. "Oppression" is here used in a somewhat broad sense. See:

Atkinson v Denby (1862) H&N 934.

(C) MISREPRESENTATION

A person can recover back money paid or property transferred under an illegal contract if he entered into the contract as a result of the other party's fraudulent misrepresentation that the contract was lawful. See:

Hughes v Liverpool Victoria Legal Friendly Society [1916] 2 KB 482.

(D) MISTAKE

Mistake of fact can be a ground for recovery of money or property even where it does not give the mistaken party the right to enforce the contract. For example see:

Oom v Bruce (1810) 12 East 225.

Note: Some writers state that where a party is induced into an illegal contract by some oppressive conduct, fraud or mistake, then it is clear that the parties are not in *pari delicto* (equally wrong) and in such circumstances the courts will allow restitution.

(E) REPUDIATION OF ILLEGAL PURPOSE

A person may be able to reclaim money paid or property transferred under an illegal contract if he repudiates the illegal purpose in time. Two conditions must be satisfied to bring the rule into operation:

(i) *Repudiation in time*

A party who repudiates before anything has been done to perform the illegal purpose can recover back his money or property, while one who repudiates after the illegal purpose has been fully carried out cannot recover. Two cases may be contrasted on this point:

Taylor v Bowers (1876) 1 QBD 291
Kearley v Thomson (1890) 24 QBD 742.

(ii) *Voluntary repudiation*

Repudiation must be voluntary: it must not be forced on the party claiming recovery by the intervention of the police, or of a third person, or by the other party's breach of contract as in:

Bigos v Bousted [1951] 1 All ER 92.

(F) NO RELIANCE ON ILLEGAL TRANSACTION

A person may be able to recover money or property which has been transferred under an illegal contract, if he can establish his right to title to it without relying on the contract or on its illegality. For example, see:

Bowmakers Ltd v Barnet Instruments Ltd [1945] 2 All ER 579
Tinsley v Milligan [1993] 3 WLR 126.

4. THE RULES OF SEVERANCE

Severance involves the court in removing the objectionable parts of a contract whilst enforcing the remainder. This power may be exercised in the case of void contracts and, possibly, illegal contracts. This power is seldom used by the courts as it is tantamount to condoning unlawful activities, although contracts in restraint of trade provide a marked exception to this policy.

Severance of a clause will only be allowed if the clause forms a subsidiary rather than a substantial part of the contract, otherwise the contract becomes totally unenforceable. See:

Bennett v Bennett [1952] 1 All ER 1088
Goodinson v Goodinson [1954] 2 All ER 255.

Alternatively, it may be possible to sever specific parts of a clause by employing the "blue pencil" test. This test provides that the objectionable part of a clause will only be severed if it leaves the remainder in a grammatically correct and understandable form. The courts are not allowed to redraft clauses. See:

Mason v Provident Clothing [1913] AC 724
Goldsoll v Goldman [1915] 1 Ch 292.

The only pre-condition is that the clause itself must be divisible in nature; that is, the clause must not be a single covenant but in effect a combination of several distinct covenants. Otherwise, severance will not be allowed as it will change the nature of the contract. See:

Attwood v Lamont [1920] 3 KB 571.