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SOUTH AUSTRALIA

THIRTY-SEVENTH REPORT

of the

LAW REFORM COMMITTEE

of

SOUTH AUSTRALIA

to

THE ATTORNEY-GENERAL

RELATING TO THE DOCTRINES OF FRUSTRATION AND ILLEGALITY IN THE LAW OF CONTRACT

1977

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The Law Reform Committee of South Australia was established by Proclamation which appeared in the *South Australian Government Gazette* of 19th September, 1968. The Members are:

THE HONOURABLE MR. JUSTICE ZELLING, C.B.E., *Chairman.*

THE HONOURABLE MR. JUSTICE JACOBS, *Deputy Chairman.*

THE HONOURABLE MR. JUSTICE KING, *Deputy Chairman.*

B. R. COX, Q.C., S.G.

D. W. BOLLEN, Q.C.

J. F. KEELER.

K. T. GRIFFIN.

The Secretary of the Committee is Miss J. L. Hill, c/o Supreme Court, Adelaide, South Australia 5000.

THIRTY-SEVENTH REPORT OF THE LAW REFORM COMMITTEE OF SOUTH AUSTRALIA RELATING TO THE DOCTRINES OF FRUSTRATION AND ILLEGALITY IN THE LAW OF CONTRACT

To:

The Honourable Peter Duncan, M.P.,
Attorney-General of South Australia.

Sir,

One of your predecessors referred to us the consideration of the reform of the law relating to the doctrines of frustration and illegality in the law of contract. We have now considered these matters and report to you as follows.

It is convenient to divide the consideration of the two matters in this report into separate parts for although the doctrines of frustration and illegality have this in common, that under the present law, in cases where the doctrine applies, the loss lies where it falls, the historical derivation and also the cases to which the doctrine applies differ in each case and it is therefore convenient to treat them separately in this report and any legislation giving effect to this report would in our opinion be better if contained in two separate Acts.

We deal first with the doctrine of frustration. The common law in relation to the doctrine of frustration stems from the theory of absolute obligation set out in *Anson on Contract, 23rd Edition, pages* 453-454 as follows:—

> "Before 1863 it was a general rule of the law of contract that a man was absolutely bound to perform any obligation which he had undertaken, and could not claim to be excused by the mere fact that performance had subsequently become impossible; for 'where there is a positive contract to do a thing, not in itself unlawful, the contractor must perform it or pay damages for not doing it, although in consequence of unforeseen accidents, the performance of his contract has become unexpectedly burthensome or even impossible: *Taylor* v. *Caldwell* (1863), 3 *B* & *S*. 826, per Blackburn, J., at p. 833. So in *Paradine* v. *Jane* in 1647: (1647), Aleyn 26—
>
> > Paradine sued Jane for rent due upon a lease. Jane pleaded 'that a certain German Prince, by name Prince Rupert, an alien born, enemy to the king and kingdom, had invaded the realm with an hostile army of men; and with the same force did enter upon the defendant's possession, and him expelled, and held out of possession . . . whereby he could not take the profits'. This plea was in substance a plea that the rent was not due because the lessee had been deprived, by events beyond his control, of the profits from which the rent should have come.
>
> The Court held that this was no excuse (at p. 27):
>
> > When the party by his own contract creates a duty or charge upon himself, he is bound to make it good, if he may, notwithstanding any accident by inevitable necessity because he might have provided against it by his contract. And therefore

> if the lessee covenant to repair a house, though it be burnt by lightning, or thrown down by enemies, yet he ought to repair it.
>
> This passage has often been cited, and, indeed, has been followed in more recent times, for it is still true to say that, where a man specifically undertakes an absolute obligation, he cannot claim to be absolved from liability by the fact that his failure to perform the obligation is due to the occurrence of an event over which he has no control. For example, the charterer of a ship will undertake in a contract of charter-party that the cargo shall be unloaded within a certain number of days, and, in default, that he will pay a certain sum of money to the ship-owner by way of 'demurrage'. If, therefore, a dock strike occurs, affecting the labour engaged by the shipowner or the charterer, this event does not necessarily release the latter from liability. He makes 'an absolute contract to have the cargo unloaded within a specified time. In such a case the merchant takes the risk' (*Budgett & Co.* v. *Binnington & Co.* [1891] 1 *Q.B.* 35, per Lopes, L. J. at p. 41. See also *Thiis* v. *Byers* (1876), 1 *Q.B.D.* 244). On the other hand, the parties may, if they choose, provide expressly in their contract against such risks, and every charter-party contains a formidable list of such exceptions, known as 'excepted risks' (see, for example, *Reardon Smith Line Ltd.* v. *Ministry of Agriculture, Fisheries and Food,* [1963] A.C. 691)."

We inherited this along with the rest of the general law of contract in 1836 and the doctrine applies in all its rigour in South Australia today: see for example the judgments of Barton J. and Isaacs J. in *Hirsch* v. *The Zinc Corporation Ltd.* 24 *C.L.R.* 34 *at* 53 *and* 57 respectively.

The criterion of absolute liability laid down in *Paradine* v. *Jane* (*supra*) does not seem to have excluded defences of Act of God or of illegality—see *Simpson*: *A History of the Common Law of Contract Volume* 1 *pages* 31-33 *and* 107-112.

The first exception to mitigate the rigour of the common law was that introduced by the Court of Queen's Bench in 1863 in *Taylor* v. *Caldwell* to which reference has already been made. In that case the contract was one for the hire of a music hall and gardens for the purpose of entertainment. Before the day of performance the music hall was destroyed by fire. The Court held that there was an implied condition that the parties should be excused where before the breach, performance had become impossible from the perishing of the thing without the default of the contractor. This doctrine was extended, particularly in the case of charter-parties, where frustration of the contract was due to excessive delays, perils of the seas or the effects of war.

The most celebrated instances of the application of the doctrine are the so-called "Coronation cases" which arose out of the postponement of the coronation of King Edward VII due to his sudden illness. It was held that where the sole object or the foundation of the contract became incapable of performance due to supervening impossibility the doctrine of frustration applied: see *Krell* v. *Henry* [1903] 2 *K.B.* 740; aliter if some, even though a truncated mode, of performance was possible: see *Herne Bay Steam Boat Co.* v. *Hutton* [1903] 2 *K.B.* 683.

Despite criticism *Krell* v. *Henry* appears to have been followed. It has been applied in four New Zealand cases and distinguished in two

others. In this country it has been considered in *Coffey* v. *Clinton* (1924) 24 *S.R. N.S.W.* 168 and *Cooper* v. *Neilson* [1918] *V.L.R.* 583; [1919] *V.L.R.* 66. A long discussion of it occurs in Latham C. J.'s judgment in *Scanlan's case* 67 *C.L.R.* 169 *at pages* 188-194. The former Chief Justice does not say that *Krell* v. *Henry* does not apply here; only that its exact *ratio decidendi* is hard to ascertain. The Australian edition of *Creshire & Fifoot pages* 685-700 passim treats the case as being law here.

It may be noted that the excessive delay cases seem to be restricted to cases arising out of charter-parties, and delay in other forms of contracts does not seem to be sufficient to attract the operation of the doctrine: see the speeches in the House of Lords in *Davis Contractors Limited* v. *Fareham Urban District Council* [1956] *A.C.* 696. Delay, however, when taken together with the exercise of the use of statutory powers arising out of the use of such powers, seems to stand on a different footing: see *Metropolitan Water Board* v. *Dick Kerr & Co. Ltd.* [1918] *A.C.* 119.

So too the performance of a contract may become legally impossible either because of a change in the law or because of a change in the operation of the law by reason of new and supervening facts. However if a party voluntarily undertakes an absolute and unconditional obligation he cannot complain merely because events turn out to his disadvantage: see *Mayne* v. *Lyons* 15 *C.L.R.* 671, nor can he complain if the contract is so drawn as to avoid the operation of the doctrine of frustration: see *Claude Neon Limited* v. *Hardie* 1970 *Q.R.* 93. The law appears to be still in a state of flux in some areas: see 1972 *Annual Survey of Commonwealth Law* 434-435 *and cases there cited.*

The leading exposition of the doctrine of frustration by the High Court of Australia is in *Scanlan's New Neon Ltd.* v. *Tooheys Limited* 67 *C.L.R.* 169 particularly in the judgment of Latham, C. J. The former Chief Justice at page 186 of his judgment lists nine different theories of the doctrine of frustration and then deals with three of them as set out in an article by *McNair*: *Frustration of Contract by War in* 56 *L.Q.R.* 173. The predominant English theory these days without doubt is that propounded by Lord Radcliffe in the *Davis Contractors case,* to which we have already referred, in his speech at pages 728-729 where His Lordship says:—

> "So perhaps it would be simpler to say at the outset that frustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. *Non haec in foedera veni.* It was not this that I promised to do."

Sir John Latham however criticises both this test and the other two proposed tests vigorously and there is substance in all of his criticisms. He did not however finally propound any test of his own because he said that on any of the tests the plaintiffs failed in the two appeals then before the Court. Basically his view appears to be that one ascertains what was the substance of the contract both from the terms of the contract and from the surrounding circumstances of which the parties were aware and then asks oneself the question whether that substantial contract needs for its foundation the assumption of the existence of a particular state of things. If the contract becomes impossible of performance by reason of the non-existence of the state of

things assumed by both contracting parties as the foundation of the contract then the doctrine of frustration applies: see his judgment at pages 192-193. His criticism of the "reasonable man" test at pages 195-196 of his judgment is particularly cogent. He sums up his position at pages 199-200 as follows:—

> "I have sought in vain for some definite criterion which would make it possible to identify events of the kind mentioned. Men take all kinds of risks when they make contracts. A business man chooses his risks and takes them. He may be said to buy a chance of making a profit, rather than to secure a certainty of not making a loss. A court appears to me to be in a poor position to determine, as a matter of law and apart from the terms of the contract, whether a particular risk is to be deemed to have been taken in a particular case."

The result of the doctrine, whatever its juridical basis, is however not in doubt. The loss lies where it falls and it can produce grave injustice to a party who has either paid money or done work for which he has received no answering benefit or recompense. Such a solution, as Scottish law lords have pointed out time and time again, would be unthinkable under any civil law system including that of Scotland, and its injustice is so palpable that shortly after the worst excesses of the doctrine had been over-ruled by the House of Lords in *Fibrosa Spolka Akcyina* v. *Fairbairn Lawson Coombe Barbour Ltd.* [1934] *A.C.* 32, the English Parliament intervened, following the seventh interim report of the Law Reform Committee, to amend the law on this point by passing the Law Reform (Frustrated Contracts) Act, 1943, 6 & 7 Geo. VI c.40.

It is not however certain that the amelioration given by the *Fibrosa Spolka case* applies in Australia because *Chandler* v. *Webster* which declared the previous law and which was over-ruled in Fibrosa Spolka was expressly applied by the High Court in the *Continental Rubber case* 27 *C.L.R.* 194 and the High Court has ruled that where any principle of law has been expressly laid down by the High Court, it is not for State Courts to assume that a later decision of the House of Lords or Privy Council alters or affects a previous pronouncement of the High Court of Australia on the law and it is for the High Court to say whether the law is to be altered.

The English legislation in its turn has raised its own problems one of which is that referred to in *Cheshire & Fifoot's Law of Contract* Australian Edition page 702 where it is said:

> "It is submitted that legislation is necessary to rectify this unsatisfactory situation, but for such legislation to produce substantially satisfactory results it must deal not only with the situation arising where a contract has been frustrated but also with the unsatisfactory situations that can arise, where, under the law as it stands, the Courts are powerless to hold that the contract has been frustrated."

and the authors refer with approval to the criticisms of Latham C. J. in Scanlan's case at pages 187-188 to which we have already referred.

Legislation in relation to frustrated contracts has also been enacted in Victoria by the Frustrated Contracts Act 6539 of 1959; in New Zealand by the Frustrated Contracts Act No. 20 of 1944; and in British Columbia by the Frustrated Contracts Act 1974 Chapter 37. We have considered all these statutes in our recommendations to you.

We recommend that the law as to frustration in relation to contracts be amended and the only question then remaining is the form that the amendment should take.

The Victorian and New Zealand Acts follow the pattern of the English Act with some minor amendments. The British Columbia Act, following a very detailed report of the Law Reform Commission of British Columbia in 1971, departs substantially from the English model.

On the assumption that you will prefer the uniformity afforded by the English, Victorian and New Zealand Acts, it is perhaps convenient if we take the English Act subsection by subsection and then deal with criticisms and amendments to it.

Section 1 (1) of the English Act of 1943 reads:—

> "Where a contract governed by English law has become impossible of performance or been otherwise frustrated, and the parties thereto have for that reason been discharged from the further performance of the contract, the following provisions of this section shall, subject to the provisions of section two of this Act, have effect in relation thereto."

A grammatical change is necessary to bring out the force of this subsection. In the third line it is suggested that the text should read after "thereto" "might for that reason have been discharged &c."

The first criticism that can be made of this subsection is the words "governed by English law". As has been pointed out by numerous commentators, this means, or should mean, that if the proper law of the contract is other than English law then an English Court is precluded from giving effect to the provisions of the Law Reform (Frustrated Contracts) Act. The reason for the particular limitation in wording is no doubt due to the fact to which we have already adverted, namely that Scotland already had a much better law on the point and it was intended to restrict the operation of the new Act to contracts the proper law of which was the law of England. However it seems to us that it would be much better to do as Victorian and British Columbia have done and omit all reference to "governed by English law". If the contract is justiciable in South Australia, then the South Australian Courts should have power, in the case of frustration of the contract, to apply South Australian law. This is particularly important because a great deal of recent consumer legislation in South Australia has made South Australian law applicable to goods and services supplied in South Australia and to acts done partly in South Australian for the protection of the consumer, and the proper law of the contract is not the determinant of the jurisdiction of South Australian Courts under these Statutes but rather whether the consumer is in South Australia or whether any act or supply in relation to which the consumer needs protection, takes place wholly or partly in South Australia. We recommend that the determinants of jurisdiction for the purpose of the legislation recommended in this report should be the same as those which now obtain in relation to consumer legislation in this State. One member thinks that this recommendation goes too far, and would prefer to use the Victorian wording, subject to a proviso similar to that recommended on page 14 of the report with respect to the proposed clause (Section 2 (3)) on contracting out.

The second is the words "has become impossible of performance". This, as an article in 93 *L.J.N, page* 326 points out, means that on a

strict construction the Act does not apply to contracts originally impossible of performance. We suggest that both cases should be covered in our legislation.

On a point of drafting the Victorian Act says:—

> "Where a contract becomes impossible of performance or is otherwise frustrated or where a contract is avoided by the operation of Section 12 of the Goods Act 1958" &c.

Section 12 of their Goods Act 1958 is the same as Section 7 of the South Australian Sale of Goods Act, 1895, and we think that the additional Victorian provision should be adopted here, but we think there should be an additional reference to our Section 6 and to the projected Section 7a which is dealt with at page 16 of this report.

As we said earlier, frustration is not defined anywhere in the English Act or indeed in any of the other Acts to which we have referred. The absence of a definition means that the parties wishing to use the new laws are thrown back on the definition of frustration as it existed prior to the enactment of the new Act and the new Act does not alter the law as to frustration but only the remedies consequent upon the operation of frustration. We do not feel able to define all the causes of frustration, which are manifold. The judgment of Latham C. J. in the *New Neon Case* to which we have referred shows the defects in all the existing theories relating to frustration. We do however draw attention to one matter which is referred to by Williams in an article in 7 *M.L.R. at page* 68 and that is that the English Act does not explicity deal with the case where the failure of consideration is partial and not total. He thinks that the Act does intend to deal with this question but does not deal with it explicitly. He recommends that what is implicit in the English Act should be made explicit. We agree because there are many cases of frustration where the payer may have received some benefit under the contract but not the benefit which he covenanted to receive or which it was in the expectation of both parties of the contract that he would receive.

Section 1 subsection (2) reads:—

> "All sums paid or payable to any party in pursuance of the contract before the time when the parties were so discharged (in this Act referred to as 'the time of discharge') shall, in the case of sums so paid, be recoverable from him as money received by him for the use of the party by whom the sums were paid, and, in the case of sums so payable, cease to be so payable: Provided that, if the party to whom the sums were so paid or payable incurred expenses before the time of discharge in, or for the purpose of, the performance of the contract, the court may, if it considers it just to do so having regard to all the circumstances of the case, allow him to retain or, as the case may be, recover the whole or any part of the sums so paid or payable, not being an amount in excess of the expenses so incurred."

As a matter of drafting we would delete from the English Section 1 (2) the words from "before" in line two of the subsection to " 'discharge')" in line three and the word "before the time of discharge" in lines nine and ten. A consequential amendment would then be made in Section 1 (3) (see our report page 11 by deleting "before the time of discharge" in line five of that subsection.

We would also add a further paragraph to the proviso to Section 1 (2):—

"Provided further that the preceding paragraph shall not apply in cases governed by Sections 6, 7 or the proposed 7a of the Sale of Goods Act."

For the proposed Section 7a see page 16 of this report.

The first criticism which may be made on this subsection is a criticism which appears in 93 *L.J.N. at page* 315, namely that the section deals only with sums of money. It does not deal with a return of goods delivered in which the property has not passed, which goods are still in being and this ought to be specifically provided for. There is however a much more basic criticism of Section 1 subsection (2) of this Act which affects the whole working of the Act and it is contained in *Goff and Jones*: *Law of Restitution at pages* 331-334 and reads as follows:—

"The proviso to this subsection is the most controversial part of the Act. It provides that the loss of expenditure incurred by a party before the time of discharge 'in, or for the purpose of, the performance of the contract' shall not necessarily fall on him. If the other party has paid or has contracted to pay money in advance before the time of discharge, the court has power to allow the party who has incurred the expenditure to retain or recover the whole or part of the sums so paid or payable, not, however, exceeding the amount of such expenditure. This provision follows the recommendation of the Law Revision Committee, which was based on the assumption that in stipulating for prepayment the payee intends to protect himself against loss under the contract. That assumption is open to criticism. It by no means follows that, where a prepayment is stipulated for, the parties intend that the payer shall stand the risk of expenditure lost by the payee because of the frustration of the contract. The object of the advance may be to put the payee in funds to continue the contract, or to protect him from loss flowing from the payer's breach or insolvency. Moreover, it is arguable that, under the proviso, a party who has made an advance payment before the time of discharge which he was not bound to make, to that extent stands the risk of the other party's lost expenditure. Such a conclusion cannot have been intended by the Law Revision Committee, but its effect may in practice be alleviated or negatived by the exercise of judicial discretion."

"Expenses" in the proviso include a reasonable sum for overhead expenses and for work or services personally performed. They must have been incurred before the time of discharge, and it is to be presumed that expenses must mean net expenses. Moreover, the expenses must have been incurred in, or for the purpose of, the performance of the contract. Such a test would, of course, exclude expenditure incurred in mere speculation on future contracts, but would include expenditure incurred before the contract is entered into on the reasonable assumption that it will be made. The following hypothetical cases may be contrasted:

A erects a stand for a procession and sells tickets for seats on the stand. The procession is cancelled, and the contracts to supply seats are frustrated. The ticket holders would be entitled to recover their money; but A should not be entitled to invoke the proviso in respect of expenditure incurred in the erection of the stand.

A and B enter into serious negotiations which, in the light of past experience, A assumes will very likely result in a contract. In anticipation of such contract, A incurs expenditure for the

purpose of its performance. The contract is duly made, but is subsequently frustrated. A should be able to recover his expenses.

The party incurring the expenditure has no *right* to retain or recover any sum paid or payable by the other party before the time of discharge; he can only invite the court to exercise its discretion to enable him to do so.

In commercial law, it is undesirable that these questions should rest on the uncertain exercise of judicial discretion. Moreover, the proviso to the subsection perpetuates in a different form the old vice of *Chandler* v. *Webster* [1904] 1 K.B. 493, namely, that the incidence of loss depends on the accident of payment in advance.

There are two other solutions which might have been adopted. One is that, whereas benefits received by either party in pursuance of the contract should be restored or paid for, the loss of expenditure otherwise incurred under the contract should lie where it falls. This is the solution generally adopted in the United States. The other solution is that, in addition to restitution of benefits received, the two parties should bear equally the expenditure otherwise incurred by both under the contract. This solution regards the contract as a joint adventure which has failed without fault. The choice is not easy, but we suggest that the former of the two solutions should have been adopted by Parliament as being more in accordance with business ethics and commercial expectations.

The simplicity and clarity of the following provisions of the *Restatement of Contracts* contrast favourably with the cumbrous discretionary provisions of the 1943 Act.

468. Rights of Restitution.

(1) Except where a contract clearly provides otherwise, a party thereto who has rendered part performance for which there is no defined return performance fixed by the contract, and who is discharged from the duty of further performance by impossibility of rendering it, can get judgment for the value of the part performance rendered, unless it can be and is returned to him in specie within a reasonable time.

(2) Except where a contract clearly provides otherwise, a party thereto who has rendered performance for which the other party is excused by impossibility from rendering the agreed exchange, can get judgment for the value of what he has rendered, less the value of what he has received, unless what he has rendered can be and is returned by him in specie within a reasonable time.

(3) The value of performance within the meaning of subsections (1, 2) is the benefit derived from the performance in advancing the object of the contract, not exceeding, however, a rateable portion of the contract price."

The British Columbia report has taken note of this criticism and recommended the adoption of a restitutionary solution and therefore British Columbia has drawn its Act differently. Section 5 (1) of their Act reads:—

"Subject to section 6, every party to a contract to which this Act applies is entitled to restitution from the other party or parties to the contract for benefits created by his performance or part performance of the contract."

The remainder of Section 5 and Sections 6-8 deal with the working out of this general principle.

We think that the solution adopted by British Columbia is the better way of dealing with the matter. On the other hand it is a matter of policy for the Government to consider whether or not in order to promote uniformity it prefers to have an Act which is in *pari materia* with those in England, Victoria and New Zealand. If it does not then the British Columbia Act Sections 5-8 should be followed as a pattern for drafting. Because of the value of uniformity the Committee recommends the solution adopted in England, Victoria and New Zealand. Assuming that this recommendation is adopted, we refer to three other criticisms of the English Section 1(2). The first is that it only deals with events "before the time of discharge" as does Section 1 (3) whereas there may be performance after frustration by a party who is innocent of the frustration. As is pointed out in several of the articles, it may well be that a party will do acts or incur expenses after what the law regards as the time of discharge either because he does not know of the events which constitute frustration or because he does know of them but does not know of their legal quality. In the first of the two instances he may well be able to recover his loss as money payable under a mistake of fact. In the second he certainly would not because the mistake is a mistake of law and yet the line is a fine one, and, as the cases show where a case has progressed through several appeals from the trial Judge to the Court of Appeal and to the House of Lords, different Courts have frequently taken different views of the legal quality of the act in question as inducing or not inducing frustration and of the time at which such frustration took effect. Clearly, in our opinion, Sections 1 (2) and 1 (3) should not be restricted to monies paid or valuable benefits obtained before the time of discharge.

Similarly the word "expenses" in Section 1 (2) and Section 1 (3) (*a*) may or may not include other forms of losses and "all sums paid or payable to any party" are not words apt to catch payments made to stakeholders or to agents on behalf of a party and that portion of the drafting should be clarified accordingly. Further we think that having regard to the provisions of the English Section 1 (4) set out hereunder the preceding subsection should be expressed to be subject to the provisions of subsection (4).

In relation to the drafting of this subsection if the English precedent is to be followed we draw your attention to a comment in *F. H. Lawson: Remedies of English Law page* 179 where the writer speaking of the drafting of the last words of the subsection says:—

> "The passage may be made more intelligible if one extracts and rearranges the essential words as follows:—'All sums paid shall be recoverable and all sums payable shall cease to be payable'."

Section 1 subsection (3) reads:—

> "Where any party to the contract has, by reason of anything done by any other party thereto in, or for the purpose of, the performance of the contract, obtained a valuable benefit (other than a payment of money to which the last foregoing subsection applies) before the time of discharge, there shall be recoverable from him by the said other party such sum (if any), not exceeding the value of the said benefit to the party obtaining it, as the court considers just, having regard to all the circumstances of the case and, in particular—

(*a*) the amount of any expenses incurred before the time of discharge by the benefited party in, or for the purpose of, the performance of the contract, including any sums paid or payable by him to any other party in pursuance of the contract and retained or recoverable by that party under the last foregoing subsection, and

(*b*) the effect, in relation to the said benefit, of the circumstances giving rise to the frustration of the contract."

We would add that "valuable benefit" in the third line could with advantage be defined so as to include a case in which the apprehended benefit has been destroyed or diminished by an event which frustrates the contract.

Apart from the comments which we have already made under the last subsection which apply equally to this subsection there is a further question which is raised by articles in 7 *M.L.R.* at page 68 and 14 *Australian Lawyer* at page 11 and which has been the subject of a specific decision of the Supreme Court of Newfoundland: *Parsons Brothers Limited* v. *Shea* (1965) 53 *D.L.R.* 2*d*. 86 and it is this:—It was thought in the article in the Modern Law Review to which we have referred but denied by the Supreme Court of Newfoundland, that this subsection altered the rule in *Appleby* v. *Myers* (1867) *L.R.* 2 *C.P.* 651. That rule says that where a party enters into an entire contract and performs that contract in part but fails to complete it then except where the failure to complete is the result of a breach of contract by the other party the party who has performed in part can recover nothing. Furlong C. J. of the Supreme Court of Newfoundland held that the rule survived the Frustrated Contracts Act 1956 of Newfoundland, which although we have not seen it, we gather from comments in Canadian publications is in similar terms to the English Act and we draw your attention to the comments and to this decision. In our opinion it should be made clear in drafting our Act that the rule in *Appleby* v. *Myers* does not survive Section 1 subsection (3) and that the Court can apply the Frustrated Contracts Act in circumstances covered by the rule in *Appleby* v. *Myers*.

Section 1 subsection (4) reads as follows:—

"In estimating, for the purposes of the foregoing provisions of this section, the amount of any expenses incurred by any party to the contract, the court may, without prejudice to the generality of the said provisions, include such sum as appears to be reasonable in respect of overhead expenses and in respect of any work or services performed personally by the said party."

This subsection appears in the same form in the New Zealand and Victorian Acts. The only matter to which we would draw attention in the drafting is the word "personally". In most cases today work or services are performed by some servant or other member of an organisation and this must necessarily be so in the case of a party to a contract which is a body corporate and the word "personally" does not seem to add anything to the subsection and could in fact on a strict construction detract from the allowances which ought properly to be made under subsection (4).

Section 1 subsection (5) reads:—

"In considering whether any sum ought to be recovered or retained under the foregoing provisions of this section by any party to the contract, the court shall not take into account any

sums which have, by reason of the circumstances giving rise to the frustration of the contract, become payable to that party under any contract of insurance unless there was an obligation to insure imposed by an express term of the frustrated contract or by or under any enactment."

This subsection is found in identical wording in the Victorian and New Zealand Acts. It follows the old concept that if a party insures any risk for his own benefit, any monies that he recovers under the contract of insurance are *res inter alios acta* as far as any claim is concerned by or against any third party. As the object of this statute is to do substantial justice between the parties we find it hard to see why if in fact a man has not sustained loss because he has prudently insured against it that should not be a factor to be taken into account in deciding how much ought to be allowed to him in relation to a contract as to which he must have had some fears that the contract might be frustrated or he would not have taken out the insurance. Of course if the concept of restitution advocated by Goff and Jones and made the basis of the British Columbia Act is the method adopted, then this subsection would not appear in the Act and the matter would be of no importance.

Section 1 subsection (6) reads:—

"Where any person has assumed obligations under the contract in consideration of the conferring of a benefit by any other party to the contract upon any other person, whether a party to the contract or not, the court may, if in all the circumstances of the case it considers it just to do so, treat for the purposes of subsection (3) of this section any benefit so conferred as a benefit obtained by the person who has assumed the obligations as aforesaid."

The New Zealand Act is in identical terms. The Victorian Act on the other hand commences with the words "where any party" instead of "where any person" and this would seem to us to be better drafting. The Victorian drafting avoids the criticism of the English subsection contained in the article in 60 *L.Q.R.* 160 *at page* 168.

Subsection 2 subsection (1) reads:—

"This Act shall apply to contracts, whether made before or after the commencement of this Act, as respects which the time of discharge is on or after the first day of July, nineteen hundred and forty-three, but not to contracts as respects which the time of discharge is before the said date."

The Victorian and New Zealand Acts have the same subsection *mutatis mutandis*. We have no comment to offer.

Section 2 subsection (2) reads:—

"This Act shall apply to contracts to which the Crown is a party in like manner as to contracts between subjects."

The Victorian and New Zealand Acts are in similar terms but we think that the subsection as expressed is too narrow. Most contracts entered into these days for the benefit of Governments are entered into not by the Crown but by some agency or instrumentality of government which quite frequently is a separate corporation or by a minister who has separate corporate status and the Crown is not technically a party to such a contract. It would in our opinion be better if the time honoured provision were inserted in its place. "This Act shall bind the Crown". If that be inserted the instrumentalities

which claim the privileges of the Crown can only have the same rights as the Crown would have had and no point can be taken that their contracts are outside the purview of the statute.

Section 2 subsection (3) reads:—

> "Where any contract to which this Act applies contains any provision which, upon the true construction of the contract, is intended to have effect in the event of circumstances arising which operate, or would but for the said provision operate, to frustrate the contract, or is intended to have effect whether such circumstances arise or not, the court shall give effect to the said provision and shall only give effect to the foregoing section of this Act to such extent, if any, as appears to the court to be consistent with the said provision."

However, because of the impact of our consumer legislation as a specific code in the cases to which it applies, we recommend the insertion of a subclause reading:—

> "Nothing in this subsection shall permit the parties to any agreement which falls within the provisions of the Consumer Credit Act 1972 or the Consumer Transactions Act 1972 to contract out of the provisions of this Act."

The New Zealand Act is in identical terms. The Victorian Act uses the words "or would but for the said provision operate to frustrate or avoid the contract." This would appear to be better drafting and we recommend its use in place of the English and New Zealand wording.

We draw your attention to a possible deficiency in Section 2 (3) in that it may not be expressed in terms sufficiently wide to prevent wholesale contracting out in other types of agreement by writing into a contract words such as "The Frustrated Contracts Act 1976 of the Parliament of South Australia shall not apply to this contract."

Section 2 subsection (4) reads as follows:—

> "Where it appears to the court that a part of any contract to which this Act applies can properly be severed from the remainder of the contract, being a part wholly performed before the time of discharge, or so performed except for the payment in respect of that part of the contract of sums which are or can be ascertained under the contract, the court shall treat that part of the contract as if it were a separate contract and had not been frustrated and shall treat the foregoing section of this Act as only applicable to the remainder of that contract."

The Victorian and New Zealand equivalent subsections are in identical form. We would if this section were to be adopted amend the words "can properly" in the second line of the subsection to read "may reasonably".

Section 4 of the British Columbia Act on the same point reads as follows:—

> "Act applicable to part of contract.—Where a part of any contract to which this Act applies is
>
> (*a*) wholly performed before the parties are discharged; or
>
> (*b*) wholly performed except for the payment in respect of that part of the contract of sums that are or can be ascertained under the contract,

and that part may be severed from the remainder of the contract, that part shall, for the purposes of this Act, be treated as a separate contract that has not been frustrated or avoided, and this Act, excepting this section, is applicable only to the remainder of the contract."

We think that this makes for clearer drafting than the equivalent English, Victorian and New Zealand subsection and we recommend its adoption with one amendment, namely that the word "justly" be inserted between "may" and "be severed" in the eighth line of the proposed section.

Section 2 subsection (5) reads:—

"This Act shall not apply—

(*a*) to any charter-party, except a time charter-party or a charter-party by way of demise, or to any cantract (other than a charter-party) for the carriage of goods by sea; or

(*b*) to any contract of insurance, save as is provided by subsection (5) of the foregoing section; or

(*c*) to any contract to which section seven of the Sale of Goods Act, 1893 (which avoids contracts for the sale of specific goods which perish before the risk has passed to the buyer) applies, or to any other contract for the sale, or for the sale and delivery, of specific goods, where the contract is frustrated by reason of the fact that the goods have perished."

British Columbia dealt very carefully with the exemption relating to a charter-party and concluded that on the balance of convenience it was better to have uniform legislation on the question. In any case we understand from other sources that it is possible that the Commonwealth Parliament will legislate on the subject and indeed some parts of this area of the law are already covered by the Commonwealth Sea Carriage of Goods Act 1924. For all these reasons we think that the exemption should stand as in the English, Victorian and New Zealand Acts.

As far as the insurance exemption is concerned, life insurance is of course already a matter for Commonwealth law. As far as accident and other forms of risk insurance is concerned, the exception is based on the rule that the premium is payable at the commencement of the risk and covers the whole period of the risk from then on. We think it better to have uniform legislation on the subject. There seems to be no particular reason for deciding either way. Glanville Williams in his book on *The Frustrated Contracts Act* at page 80 says that it is "difficult to see why contracts of insurance are excluded". On the other hand Professor Gutteridge in an article in 61 *L.Q.R. at page* 99 says:—

"As regards the rule that no part of an insurance premium is recoverable when once the risk has attached, there are no grounds for regarding this as inequitable. The insurer has no claim to an increase of premium in case the risk should have become enhanced during the currency of the policy and the assured cannot have it both ways."

These are the two competing views and we think it better to have the Act uniform with the English, Victoria and New Zealand Acts because the two views seem to be evenly balanced.

As far as the exemption in relation to sale of specific goods is concerned, we recommend that, as in Victoria, this subsection be deleted. The New South Wales Law Reform Commission in a careful study of this question say at page 259 that their Section 12 of the Sale of Goods Act (our Section 7) should be replaced by two new Sections reading as follows:—

> "12. (1) Where, after the making of a contract for the sale of goods but before delivery, the goods wholly perish, or the contract is otherwise frustrated, in either case without any fault on the part of the seller, the seller is not liable for damages for non-delivery.
>
> (2) Where, after the making of a contract for the sale of goods and while the risk is with the seller, the goods wholly perish, or the contract is otherwise frustrated, in either case without any fault on the part of the buyer, the buyer is not liable for the price of the goods.
>
> 12A. (1) Where, after the making of a contract for the sale of goods and while the risk is with the seller, the whole or a material part of the goods so deteriorates in quality as to be substantially changed in character, or part of the goods perish, in either case without any fault on the part of the seller or of the buyer, the buyer may at his option either treat the contract as discharged by frustration or accept the goods.
>
> (2) If pursuant to subsection (1), the buyer treats the contract as discharged by frustration, the seller is not liable for damages for non-delivery and the buyer is not liable for the price of the goods.
>
> (3) If pursuant to subsection (1) the buyer accepts the goods, he shall be entitled to a reasonable allowance from the price for the deficiency in quantity or deterioration in quality of the goods, but without any further right against the seller."

As they point out their new Section 12A seeks to cover the situation where part only of the goods perish or where the goods or a material part of them are not destroyed but have so deteriorated in quality as to be substantially changed in character and they refer to *Sainsbury Limited* v. *Street* [1972] 1 *W.L.R.* 834 and *Asfar* v. *Blundell* [1891] 1 *Q.B.* 123. The recommended New South Wales section is based on Sections 7 and 8 of the United States Uniform Sales Act and Section 2-613 of the United States Uniform Commercial Code. Although this is not strictly within our terms of reference we would think that the New South Wales recommendation was a good one and should be given effect to by an amendment to our Sale of Goods Act 1895 by inserting a new Section to stand as 7a.

In any event we recommend that the Victorian drafting be followed in deleting Section 2 subsection (5) subparagraph (c) from the equivalent Act in this State. The subsection is also criticised in the article in 60 *L.Q.R. at pages* 172-173 and in the article in 93 *L.J. at page* 326.

We recommend also two matters which are not in the English Act at all but which are in the Victorian Act and another which is in neither Act but ought to be covered. The first is a definition clause which stands as Section 2 of the Victorian Act which reads as follows:—

> "In this Act unless inconsistent with the context or subject matter—

'Court', in relation to any matter, means the court or arbitrator by or before whom the matter falls to be determined.

'Time of discharge', in relation to any contract, means the time at which the contract becomes impossible of performance or is otherwise frustrated or at which it is avoided by the operation of section twelve of the Goods Act 1958."

Section 12 of the Victorian Goods Act 1958 is in identical terms with Section 7 of our Sale of Goods Act 1895. However because of our recommendation of the adoption of a new Section 7a of the Sale of Goods Act (the New South Wales Section 12A) reference should be made to this in the definition of "time of discharge".

The second is also in the Victorian Act and deals with limitation of actions. It is their Section 5 which reads as follows:—

"All actions and proceedings to recover moneys under this Act shall be deemed to be founded on simple contract and subject to the provisions of Part II of the *Limitation of Actions Act* 1958 the cause of action shall be deemed to have first accrued at the time of discharge."

The relevant section of our Limitation of Actions Act 1936 as amended is Section 35 subsection (*a*). We would add the words "goods or" before "moneys" in the first line.

The third recommendation which we make is that a Section should be inserted to make it clear that the doctrine of frustration applies to leases and tenancies, and also to agreements creating an interest in land of which a Court will decree specific performance. The applicability of the Victorian Act to these cases was queried by Hudson J. of the Supreme Court of Victoria in *Lobb* v. *Vasey Housing Auxiliary* (*War Widows Guild*) 1963 V.R. 239. We think that His Honour's query in respect to all these matters was well grounded and that the matter should be put beyond doubt by a declaratory section in this Act stating that the Act does apply to frustration in relation to leases and tenancies and also to any agreement creating an interest in land of which the Court would decree specific performance. On frustration in relation to leases we would also refer to the judgment of Williams J. in *Minister of State* v. *Dalziel* 68 *C.L.R.* 261 *at* 302.

We have in this report made it plain that we prefer the remedy in the British Columbia Act which follows the recommendation of Goff and Jones, by way of restitution and that the remedy should not be restricted to the mechanical reform by way of return of monies paid or expenses incurred. We should add that the whole matter of pecuniary restitution on breach of contract has recently been the subject of a working paper number 65 of the Law Commission of England and you may think it proper to refer this wider subject to the Law Reform Committee for more general consideration than it has been possible to give to this small fragment of the subject in this paper.

As we have not subjected the British Columbia Act to the same analysis as the English, Victorian and New Zealand Acts on the assumption that our recommendation set out above will be adopted and that you will prefer to have uniformity of legislation where possible, we attach a copy of the British Columbia Act as an appendix to this Report. If this turns out to be ill-founded and you desire us to examine the British Columbia Act and its underlying concepts in depth, we shall be pleased to do so.

We turn now to the consideration of the question of illegal contracts. An illegal contract is a contract made in contravention of a legal prohibition which is imposed either by statute (and by the word statute we include all forms of delegated legislation made under the authority of a statute) or by the common law. The illegality may consist either in the making of the contract; in its performance; in the consideration for the contract; or in the purpose or object of entering into the contract. Contracts for an illegal purpose cover a very wide sphere in terms of moral reprehensibility from an agreement to commit murder on the one hand to an agreement which contravenes some minor provision of a regulation to which a criminal sanction has been attached. The classification of illegal contracts has become more difficult in recent years in that there is now a tendency to divide illegal contracts into illegal contracts and void contracts. We have dealt with both types of contract as illegal contracts in this paper because in our opinion relief is required in both classes of case but the two are gradually separating in terms of case law and in the textbooks and we shall deal with this separation later in the paper. As *Chitty on Contracts* 21st edition Volume 1 page 466 says:—

> "Whenever the contract which a party seeks to enforce, be it express or implied, is expressly or by implication forbidden by the common or statute law, no Court, either of law or equity, will lend its assistance to giving it effect."

This defence of illegality has come down from the mediaeval times: see *Simpson loc. cit. pages* 507-510.

Courts take notice of illegality, whether the illegality is pleaded or not. If the illegality is plain either on the face of the contract or on the face of the pleadings or from the evidence then notwithstanding that neither party wishes the point of illegality to be taken or the case to be decided on that point it is the duty of the Court to take the point and to refuse to give relief to the parties to an illegal contract. The last statement is subject to certain exceptions which we shall set out in detail in this paper but the general rule is still as it has always been at common law; *ex turpi causa non oritur actio.* The result of this policy in the hands of the Courts is that, as in the case of frustrated contracts, the loss lies where it falls.

The following contracts are illegal at common law:—

1. A contract to commit a crime, to commit a tort or to commit a fraud on a third party.

   This is based on the wide maxim that no one can benefit from his own wrong. The same rules apply in the case of insurance contracts if the assured feloniously commits suicide unless of course he is insane when he takes his own life. Samples of all these contracts can be found in *Cheshire & Fifoot—Law of Contract Australian Edition pages* 432-433 and *Chitty on Contracts (supra) pages* 477-480.

2. Contracts which are in intention sexually immoral or tend to promote future sexual immorality. This rule is not confined to cases of intention or motive only but applies also if the agreement is such that it will tend to promote sexual immorality: see *Ramsay* v. *Trustees Executors & Agency Company Limited* 77 *C.L.R.* 321 in the judgment of Latham C.J. at pages 326-327 and *Church Property Trustees Diocese of Newcastle* v. *Ebbeck* 104 *C.L.R.* 394 in the judgment of Windeyer J. at pages 415-416.

3. Contracts to the prejudice of public safety or of good relations with friendly states. This includes contracts with an alien enemy in time of war and contracts inimical to the public welfare of a friendly foreign country. It is not sufficient where the contract is to be performed here that the performance of the contract may be a breach of a foreign law binding on the defendant: see *Kleinwort v. Ungarische Baumwolle Industrie Akt.* (1939) 2 *K.B.* 673 and *British Nylon Spinners* v. *Imperial Chemical Industries* 1955 *Ch.* 37. This last is a distinction which is extremely difficult to draw in practice. In Kleinwort's case the Hungarian Government had it made illegal for Hungarian subjects to pay money outside Hungary without the consent of the Hungarian National Bank. The Hungarian Government clearly thought that such payments were inimical to the public welfare of Hungary. Similarly in the British Nylon Spinners case Upjohn J. (as he then was) disregarded the anti-trust laws of the United States. Anyone who has ever discussed anti-trust laws with United States lawyers knows well that Americans have very strong views on anti-trust laws and regard any breach of them as inimical to the interests of the United States. Accordingly it is, as it seems to us, really a question of whether the Australian Court will categorize the action as being inimical to the public welfare of Australia rather than inimical to the public welfare of the other country.

4. Contracts affecting the course of justice. Any contract or agreement which has a tendency however slight to affect the administration of justice is illegal: such as contracts to stifle a prosecution, contracts not to appear and give evidence at a trial and contracts forebearing to prosecute. This type of contract is only illegal if the prosecution is for a public offence but not where there are both criminal and civil remedies for the same act and it is the civil remedy which is being compounded. Any contracts however which deal with any aspect of the perversion of justice, any contract or agreement which makes the carrying out of the duties of a court of justice more difficult or which indemnifies persons against the consequences of such an act is within the purview of the prohibition; thus for example a contract with one's bail to indemnify them against loss is within the purview of the prohibition: see *Herman v. Jeuchner* 15 *Q.B.D.* 561.

5. Contracts which savour of maintenance or champerty. Maintenance has almost ceased to be of legal relevance since the decision of the House of Lords in *Neville* v. *London Express Newspapers Limited* [1919] *A.C.* 368, but nevertheless the defence of maintenance has been raised in recent cases in Australia though not successfully within the last decade. Champerty on the other hand remains both an offence at common law and under the statute declaring the common law and also produces illegality in contract tainted with champerty. A champertous agreement is one whereby a party who is not interested in the proceedings agrees to carry on the suit of a party who is so interested, at the expense of the champertee, in consideration of his receiving a share of the proceeds of the litigation: see *Jones* v. *Bouffier* 12 *C.L.R.* 579 and *Re Trepca Mines Limited* (*No.* 2) 1963 *Ch.* 199.

6. Contracts which produce or have a tendency to produce corruption in public life. The usual instance in this is a contract for

the buying, selling or procuring of public offices. Certain contracts relating to such sales are also illegal by the statutes 5 Edward VI c.16 and 49 Geo. III c.126 which are still in force in South Australia.

7. Contracts to defraud the revenue: see *Alexander* v. *Rayson* [1936] I *K.B.* 169.

8. Contracts giving a right to a pretenced title which is illegal at common law and is also illegal under the Statute 32 Henry VIII c.9 which is in force in South Australia.

9. Contracts entered into for the purpose of evading a public statute: see *Napier* v. *The National Business Agency* [1951] 2 *All E.R.* 264; *Prole* v. *Wiggins* (1836) 3 *Scott* 601, and *Wilkinson* v. *Barclay* (1946) 62 *T.L.R.* 581.

10. If the usury laws are still in force in South Australia as to which see V.D.L. Act11 Geo. IV No. 6 and N.S.W. Act 5 Wm. IV c.10 (they were repealed in England in 1854 after the reception of English law here in 1836 and have never been repealed in this State), then certain types of contract tainted with usury were and are illegal either by the common law or by the common law as modified by pre-1836 imperial statutes (see *Simpson loc. cit. pages* 510-518).

11. Contracts illegal as contravening the Lord's Day Acts which are still in force in South Australia namely the Statutes 27 Henry VI c.5, 1 Charles I c.1; 3 Charles I c.2; 29 Charles II c.7; 2 George III c.15 and 3&4 Will. IV c.31, some of which statutes are said to be declaratory of the common law and some of which have widened the common law position.

There are three other types of contract which are technically spoken of as illegal contracts but which in terms of modern textbook writing are now regarded as more correctly classified as void contracts rather than illegal contracts following a dictum of Denning L.J. (as he then was in *Bennett* v. *Bennett* [1952] 1 *K.B.* 249 *at page* 260 where his Lordship said of such contracts:—

> "They are not 'illegal' in the sense that a contract to do a prohibited or immoral act is illegal. They are not 'unenforceable' in the sense that a contract within the Statute of Frauds is unenforceable for want of writing. These convenants lie somewhere in between. They are invalid and unenforceable. The law does not punish them. It simply takes no notice of them. They are void, not illegal."

The three types of contract which are now frequently characterized as void rather than illegal are: contracts to oust the jurisdiction of the Courts, contracts tending to prejudice the status of marriage or, apart from the Adoption Acts, to give up the control and bringing up of children and contracts in restraint of trade. Certainly a difference has arisen in respect to the consequences of these last three types of contract. As is said in *Halsbury Laws of England* 4th Edition Volume 9 page 297 paragraph 429:—

> "Certain contracts are rendered void (but not illegal) either by statute or by the common law as offending public policies. Such contracts resemble illegal contracts in that they are unenforceable,, but they differ from illegal contracts in relation to severance, their effect on related transactions and, perhaps, the effect of transfers of property or payment of money."

The third type of contracts which certainly are illegal are contracts declared illegal expressly or by implication by statute (as distinct from statutes declaring contracts to be void as in the case of some contracts by way of gaming and wagering).

It is obvious that if the stringent consequences which follow from illegality in relation to contracts were carried out in their entirety, very great injustice would be produced. Accordingly the law has over the years provided a number of exceptions to the rule that contracts which are illegal or void are completely unenforceable in the Courts. The exceptions are as follows:—

1. The law does not presume a crime. It presumes the opposite, namely that a crime has not or will not be committed. Accordingly if a contract is executory and there are two ways of carrying it out and no part of the illegal purpose has been performed the Court will presume in the absence of evidence to the contrary that the contract will be carried out legally and not illegally.
2. The statute may be construed as merely imposing a penalty and not as striking down a contract falling within its terms. Courts are particularly careful in this regard in the case of implied prohibitions by statute: see the remarks of Sangster J. in *Chappel* v. *Pett* (1971) 1 *S.A.S.R.* 189 *at* 197. The cases on this subject are not easy to follow and it is not necessary in this report to set them out in detail. They will be found in *Halsbury* 4*th Edition Volume* 9 *title "Contract" pages* 290 *and* 291 *paragraphs* 423 *and* 424.

These first two points may perhaps be better characterized as points of construction rather than as true exceptions but they are stated here for purposes of completeness.

3. If the parties are not in *pari delicto* then the party who is less guilty is allowed to enforce his claim but the party who is more guilty is not. This is particularly so where the object of the statute prohibiting the contract is to protect one class of persons against the acts of another: see the judgment of Lord Mansfield C. J. in *Browning* v. *Morris* (1778) 2 *Cowp*, 790; 98 *E.R.* 1364 and the judgment of Napier C.J. in *S.A. Cold Stores Ltd.* v. *Electricity Trust of South Australia* 1965 S.A.S.R. 360 *at* 368. So too where public policy is considered as advanced by allowing the more excusable of the two parties to sue for relief against the transaction relief is given: see the judgment of Knight-Bruce L.J. in *Reynell* v. *Sprye* (1852) 1 *DeG. M. & G.* 660 *at* 679. It is difficult in many of these cases to decide which is the "innocent party" and how far such innocent party participated in the illegal performance: see a note on this point and on the case of *Ashmore Benson Pease & Co. Limited* v. *A. V. Dawson Limited* [1973] 1 *W.L.R.* 828 in 1973 *Cambridge Law Journal at pages* 199-203.

   Another exception to the *par delictum* rule is that a trustee in bankruptcy can recover monies paid, even though the bankrupt was in *pari delicto*, where the payment is an offence against the bankruptcy laws or the money is paid in fraud of creditors or the payment is made after the commencement of the bankruptcy.
4. If the plaintiff does not have to prove the illegality as part of his cause of action he can recover: see *Singh* v. *Ali* [1960]

A.C. 167. A more difficult decision in this area is *Bowmakers Limited* v. *Barnett Instruments Limited* [1945] *K.B.* 65 *which* was distinguished by the High Court of Australia in *Thomas Brown & Sons Limited* v. *Deen* 108 *C.L.R.* 391. The correctness of the decision in the Bowmakers case was doubted by Gresson J. (as he then was) in *Watson v. Miles* 1953 N.Z.L.R. 958 *at pages* 967-969 but it has never been overruled. See also an article by Coote in 35 *M.L.R.* 38.

5. The doctrine of *locus poenitentiae.*

   Either party to an illegal contract may rescind the contract whilst it remains executory and may recover from the other party any money which he may have paid to him even though to do so he may have to prove the illegality as part of his case but if the illegal purpose has been wholly or substantially effected or frustrated then the law does not allow any *locus poenitentiae.*

6. In some cases of transfer of ownership of goods or land or of limited interests in property the law will give its aid to recovery but not in others. The law on this subject is in a very confused state and in fact in the case of limited interests in land the latest edition of Halsbury simply says bluntly that "there is no decisive authority". The cases are discussed in *Volume* 9 *of the 4th Edition of Halsbury at paragraphs* 433, 434 *and* 435. If the property in the asset has already passed the illegality will not prevent the passing being effective: see the judgment of Jacobs J. in *Amid Pty. Ltd.* v. *Beck & Jonas Pty. Ltd. and others* (1974) 11 *S.A.S.R.* 16.

7. Where the illegal part of the contract is severable from that part of the contract which is not tainted by illegality, the Courts will sever and enforce the part of the contract which is not illegal provided that they are not thereby writing a completely new contract for the parties. Further the contract shorn of the offending parts must retain the characteristics of a valid contract so that if severance will remove the whole or the main considerations given by one or both parties the contract becomes unenforceable. It is clear that in these circumstances severance is not in practice a very useful remedy in most cases. This question of severance is discussed in an article by Teh in 4 *University of Tasmania Law Review at pages* 249-257.

8. A separate promise for lawful performance is enforceable, i.e. one party as a condition of entering into a contract may exact a promise from the other agreeing to keep the performance of the contract free from the taint of any illegality: see *Strongman* (1945) *Limited* v. *Sincock* [1955] 2 *Q.B.* 525.

9. In recent cases a further refinement has been imposed that in the case of breach of statutory requirement it has to be shown that there is a sufficient nexus between the statutory requirements and the contract itself: see *Curragh Investments Limited* v. *Cook* [1974] 3 *All E.R.* 658.

There are three types of agreement which are strictly speaking void and not illegal but which require to be dealt with in this paper and in the proposed statute.

1. Agreements ousting or tending to oust the jurisdiction of the Court: see *Czarnikow* v. *Roth Schmidt & Co.* (1922) 2 *K.B.* 478 and *Hyman* v. *Hyman* 1929 *A.C.* 601.

2. Agreements deleterious to family relationships. An agreement by a wife not to seek maintenance in the future is void: see *Hyman* v. *Hyman* (*supra*) and *Felton* v. *Mullighan* 124 *C.L.R.* 367. An agreement in general restraint of marriage is void: see *Baker* v. *White* (1690) 2 *Vern.* 215 Marriage brokage contracts are void: *Hermann* v. *Charlesworth* [1905] 2 *K.B.* 123. Agreements for the future separation of husband and wife are void: *Brodie* v. *Brodie* 1917 P. 271. Agreements between husband and wife purporting to restrict the right to apply to a Court for financial provision for children are void: *Northrop* v. *Northrop* 1968 P. 74.
3. Contracts in restraint of trade are probably only void and not illegal at common law: see *Bennett* v. *Bennett* [1952] 1 *K.B.* 249 *at* 262 and the judgment of Lord Parker of Waddington delivering the advice of the Privy Council in *Attorney-General of the Commonwealth* v. *Adelaide Steamship Co. Ltd.* 1913 *A.C.* 781 *at* 794 *and again at* 797. On restraint of trade generally see the judgment of the Privy Council in *Amoco Australia Pty. Ltd.* v. *Rocca Bros. Motor Engineering Co. Pty. Ltd.* (1975) 49 *A.L.J.R.* 57. Many types of contracts in restraint of trade are today illegal by statute both under State law and under Commonwealth law.

As has already been pointed out in this report the rules relating to void contracts differ in the treatment of severance, related transactions and transfers of property, from those relating to illegal contracts. The nature and extent of the differences and the cases in which the differences will apply are uncertain and ought to be the subject of definitive rules.

When one adds to the enumeration of illegal and void contracts at common law and all the exemptions which have been fashioned by the Courts over the centuries, the facts that some contracts are illegal at their inception, some are illegal by reference to or by incorporation of other statutes, some are only illegal by statutory implication, some contracts fail by reason of supervening illegality either at common law or by statute and, as has already been pointed out, the group of contracts which are today regarded as void rather than illegal have different consequences in law from those that are strictly illegal, it is obvious that the common law rules need some statutory assistance. We recommend that this be given. The only country in which such regulation has so far been essayed is New Zealand and we therefore turn to a discussion of the New Zealand Statute on the matter.

The New Zealand Act is based upon a report of the Contracts and Commercial Law Reform Committee of New Zealand presented to the Minister of Justice of that country October, 1969. The report, and also the New Zealand Act. No. 129 of 1970 which was passed in pursuance of the report, have been subjected to very considerable criticism by M. P. Furmston in an article in 5 *N.Z.U.L.R.* 151. Higgins and Fletcher on the other hand in their book on *The Law of Partnership in Australia and New Zealand 3rd Edition* (1975) page 42 say of the 1970 New Zealand Act:—

> "The Act is a bold piece of legislation but one suspects that it merely gives legislative force to what less timorous members of the common law judiciary have been doing for some time."

The fact is that the New Zealand report and Act were the first in this area of the law. Once a new reform has been essayed by one Law Reform Committee and by one Parliament, it is easy to show how it

could have been done differently but it does not necessarily follow that the different method so advocated would necessarily be better. For ourselves we think that the New Zealand Act merits consideration and that there are suggestions which could be made which would assist in its operation in this State.

We therefore proceed to deal, as we did in the case of frustration, with the New Zealand Act section by section. After the enacting words and Section 1—the short title, Section 2 reads as follows:—

"*Interpretation*—In this Act, unless the context otherwise requires,—

'Act' means any Act of the General Assembly; and includes any Act of the Parliament of England, or of the Parliament of Great Britain, or of the Parliament of the United Kingdom, which is in force in New Zealand:

'Court' means the Supreme Court or a Magistrate's Court that has jurisdiction under section 9 of this Act:

'Enactment' means any provision of any Act, regulations, rules, bylaws, Order in Council, or Proclamation; and includes any provision of any notice, consent, approval, or direction which is given by any person pursuant to a power conferred by any Act or regulations;

'Property' means land, money, goods, things in action, goodwill, and every valuable thing, whether real or personal, and whether situated in New Zealand or elsewhere; and includes obligations, easements, and every description of estate, interest, and profit, present or future, vested or contingent, arising out of or incident to property."

This Section requires adaptation for South Australian use but it is not necessary for us to comment upon it further.

Section 3 reads as follows:—

" '*Illegal contract' defined*—Subject to section 5 of this Act, for the purposes of this Act the term 'illegal contract' means any contract that is illegal at law or in equity, whether the illegality arises from the creation or performance of the contract; and includes a contract which contains an illegal provision, whether that provision is severable or not."

We would suggest the following alterations to the definition. We think the word "formation is the proper word to be used in relation to a contract rather than the word "creation". The definition does not include a contract which is illegal because the parties to it intend to use the contract to effect an illegal purpose. We are not sure whether the words "or performance" are apt to cover two different types of illegality:—(a) performance which is prohibited *per se* by the common law or by statute and (*b*) performance which contains an element of illegal conduct sufficient to taint the contract. We think that it would be better to set out the various ways in which illegality may affect a contract in several subprovisions to cover these points. In addition, as we have said, usage and possibly also the law, provides that certain contracts are in truth void rather than illegal and there should be a further subclause to say that "illegal contract" for this purpose includes a contract which is void as being in restraint of trade, in derogation or ouster of the jurisdiction of the Courts or which operates so as to take away or derogate from the interdependent rights and liabilities of husband and wife or parent and child.

Section 4:—

"*Act to bind the Crown*—This Act shall bind the Crown." We agree that the legislation should bind the Crown.

Section 5 reads as follows:—

"*Breach of enactment*—A Contract lawfully entered into shall not become illegal or unenforceable by any party by reason of the fact that its performance is in breach of any enactment, unless the enactment expressly so provides or its object clearly so requires."

This would appear to be merely declaratory of the present law and probably does no harm except that the law is still developing in this context, as we pointed out earlier in this report when referring to the case of *Curragh Investments Limited* v. *Cook* (1974) 3 All *E.R.* 658 which requires a nexus between the contract and the contravention of the statute: It may be impossible to say which part of the contract has in fact been performed illegally even though some illegal performance must have occurred somewhere. Here the common law does not allow the defence of illegality to prevail: see *St. John Shipping Corporation* v. *Joseph Rank Ltd.* [1956] 3 *All E.R.* 683

If an amendment is to be made then we suggest that the second and third lines be redrafted to read:

"shall not be deemed to be illegal or unenforceable by any party by reason of the fact that its performance is or has been in breach".

Section 6 reads as follows:—

"*Illegal contracts to be of no effect*—(1) Notwithstanding any rule of law or equity to the contrary, but subject to the provisions of this Act and of any other enactment, every illegal contract shall be of no effect and no person shall become entitled to any property under a disposition made by or pursuant to any such contract:

Provided that nothing in this section shall invalidate,

(*a*) Any disposition of property by a party to an illegal contract for valuable consideration; or

(*b*) Any disposition of property made by or through a person who became entitled to the property under a disposition to which paragraph (*a*) of this proviso applies—

if the person to whom the disposition was made was not a party to the illegal contract and had not at the time of the disposition notice that the property was the subject of, or the whole or part of the consideration for, an illegal contract and otherwise acts in good faith.

(2) In this section the term 'disposition' has the meaning assigned to that term by section 2 of the Insolvency Act 1967."

Here we part company with the New Zealand draftsman. As we have already pointed out the common law has already provided a number of ways in which relief may be granted to persons whose contracts would otherwise be caught by illegality either at common law or by statute in a contract and it would seem unfortunate to force contracts with very varying kinds of illegality into a strait jacket. Secondly the words "subject to . . . any other enactment" are words which very substantially decrease the value of the section in practice: see *R. D. Bull Limited* v. *Broadlands Rentals Ltd.* [1975] 1 *N.Z.L.R.* 304. We would therefore suggest that instead of the present Section 6 there should

be in our Act a section stating that the remedies in this Act are in addition to any remedy already given by the common law or by any other statute in relation to illegal contracts.

It may well be that it is Government policy that contracts in violation of some Acts shall not be entitled to any more than the common law protection if indeed to any protection and if that is so then that Act, present or future, should be exempted from the effect of our proposed legislation. The Committee discussed whether there ought to be provision made in the Act for exemption by proclamation. Although this method would be useful to correct inadvertent mistakes in later legislation and to reflect policy changes easily and quickly the Committee agreed that it was desirable that exemption be a matter for the Legislature and not for the Executive. If it is desired that any contracts made illegal by statute should be outside the provisions of the legislation recommended by us, the statute should say so in express terms.

Section 7 reads as follows:—

"*Court may grant relief*—(1) Notwithstanding the provisions of section 6 of this Act, but subject to the express provisions of any other enactment, the Court may in the course of any proceedings or on application made for the purpose, grant to—

(*a*) Any party to an illegal contract; or

(*b*) Any party to a contract who is disqualified from enforcing it by reason of the commission of an illegal act in the course of its performance; or

(*c*) Any person claiming through or under any such party—

such relief by way of restitution, compensation, variation of the contract, validation of the contract in whole or part or for any particular purpose, or otherwise howsoever as the Court in its discretion thinks just.

(2) An application under subsection (1) of this section may be made by—

(*a*) Any person to whom the Court may grant relief pursuant to subsection (1) of this section; or

(*b*) Any other person where it is material for that person to know whether relief will be granted under that subsection.

(3) In considering whether to grant relief under subsection (1) of this section the Court shall have regard to—

(*a*) The conduct of the parties; and

(*b*) In the case of a breach of an enactment, the object of the enactment and the gravity of the penalty expressly provided for any breach thereof; and

(*c*) Such other matters as it thinks proper;

but shall not grant relief if it considers that to do so would not be in the public interest.

(4) The Court may make an order under subsection (1) of this section notwithstanding that the person granted relief entered into the contract or committed an unlawful act or unlawfully omitted to do an act with knowledge of the facts or law giving rise to the illegality, but the Court shall take such knowledge into account in exercising its discretion under that subsection.

(5) The Court may by any order made under subsection (1) of this section vest any property that was the subject of, or the whole or part of the consideration for, an illegal contract in any party to the proceedings or may direct any such party to transfer or assign any such property to any other party to the proceedings.

(6) Any order made under subsection (1) of this section, or any provision of any such order, may be made upon and subject to such terms and conditions as the Court thinks fit.

(7) Subject to the express provisions of any other enactment, no Court shall, in respect of any illegal contract, grant relief to any person otherwise than in accordance with the provisions of this Act."

Again for the same reason as we discussed under Section 6 we would leave out the words "but subject to the express provisions of any other enactment." We have provided for modification by proclamation of the application of this legislation to any other Act and any later Act which expressly says that this legislation shall not apply will *pro tanto* amend the law in any case. It follows from our earlier comments that subsection (7) should be deleted and that the Court should have in addition its normal powers which have come by the common law and by the exposition of statutory rights over the years.

Section 8 reads as follows:—

"*Restraint of trade*—(1) Where any provision of any contract constitutes an unreasonable restraint of trade, the Court may—

(*a*) Delete the provision and give effect to the contract as so amended; or

(*b*) So modify the provision that at the time the contract was entered into the provision as modified would have been reasonable, and give effect to the contract as so modified; or

(*c*) Where the deletion or modification of the provision would so alter the bargain between the parties that it would be unreasonable to allow the contract to stand, decline to enforce the contract.

(2) The Court may modify a provision under paragraph (*b*) of subsection (1) of this section, notwithstanding that the modification cannot be effected by the deletion of words from the provision."

This would appear in general to follow the law as it stands at present although it may give a slightly wider power of severance than at present exists, particularly having regard to subsection (2). We would prefer to have the provisions set out in New Zealand section 7 (1) (*c*) inserted again here instead of their subsection (2). As far as subsection (1) is concerned we would recommend an amendment to put it beyond doubt that a Court may do all or any of the matters in (*a*) (*b*) and (*c*) and that these clauses are not mutually exclusive. Again however the Parliament may wish to provide that this section is not to apply in so-called "monopoly" situations or similar situations which Parliament wishes to prohibit so far as it can in any event. It may be necessary also to provide that nothing in this legislation applies to the operation of any law of the Commonwealth on the subject, so as to prevent any conflict arising under section 109 of the Commonwealth Constitution.

Section 9 of the New Zealand Act deals with the jurisdiction of their Magistrates' Courts. We need not set it out here. No doubt there will

be some provision in our Act conferring jurisdiction on Local Courts up to the extent of their ordinary jurisdiction.

Section 10 reads as follows:—

> "*Application of Act*—This Act shall apply to contracts whether made before or after the commencement of this Act: Provided that nothing in section 6 of this Act shall apply to contracts made before the commencement of this Act."

We agree with the first sentence of it down to the colon, but think that it would be better if this situation were dealt with in a general amendment placed in the Acts Interpretation Act rather than in a specific amendment in this proposed Act.

Section 11 of the New Zealand Act is a collection of saving clauses. Insofar as it deals with restraint of trade we have aleady commented on it; insofar as it deals with contracts purporting to oust the jurisdiction of the Court that has been dealt with elsewhere in this report; actions for breach of promise of marriage have been abolished in this State and the only subsection of their section 11 which we think of any importance is subsection (3) which reads as follows:—

> "(3) Nothing in this Act shall affect the rights of the parties under any judgment given in any Court before the commencement of this Act, or under any judgment given on appeal from any such judgment, whether the appeal is commenced before or after the commencement of this Act."

We think that a similar subsection should appear in our Act.

We desire to express our appreciation to Mrs. Wendy Eyre the research assistant to the Solicitor-General and to Miss Meek of the office of the Commissioner for Prices and Consumer Affairs for their respective research work in relation to the matters discussed in this paper.

We have the honour to be

HOWARD ZELLING
S. J. JACOBS
L. J. KING
B. R. COX
D. W. BOLLEN
J. F. KEELER
K. T. GRIFFIN

The Law Reform Committee of South Australia.

30th August, 1976.

BRITISH COLUMBIA

FRUSTRATED CONTRACTS ACT

S.B.C. 1974, *c.* 37

(See Compilation ¶ 10-000 *et seq.*)

[¶ 42-596]

Sec. 1. Application—(1) Subject to subsection (2), this Act applies to every contract

(*a*) from which the parties thereto are discharged by reason of the application of the doctrine of frustration; or

(*b*) that is avoided under section 13 of the *Sale of Goods Act.*

[¶ 42-597]

(2) [*Exception*]—This Act does not apply

(*a*) to a charterparty or a contract for the carriage of goods by sea, except a time charterparty or a charterparty by demise; or

(*b*) to a contract of insurance; or

(*c*) to contracts entered into before the date of coming into force of this Act.

[¶ 42-598]

Sec. 2. [Extent of application]—This Act applies to a contract referred to in section 1 (1) only to the extent that, upon the true construction of that contract, it contains no provision for the consequences of frustration or avoidance.

[¶ 42-599]

Sec. 3. Crown bound—The Crown and its agencies are bound by this Act.

[¶ 42-600]

Sec. 4. Act applicable to part of contract—Where a part of any contract to which this Act applies is

(*a*) wholly performed before the parties are discharged; or

(*b*) wholly performed except for the payment in respect of that part of the contract of sums that are or can be ascertained under the contract.

and that part may be severed from the remainder of the contract, that part shall, for the purposes of this Act, be treated as a separate contract that has not been frustated or avoided, and this Act, excepting this section, is applicable only to the remainder of the contract.

[¶ 42-601]

Sec. 5. Adjustment of rights and liabilities—(1) Subject to section 6 every party to a contract to which this Act applies is entitled to restitution from the other party or parties to the contract for benefits created by his performance or part performance of the contract.

[¶ 42-602]

(2) [*Relief from obligations*]—Every party to a contract to which this Act applies is relieved from fulfilling obligations under the contract that were required to be performed prior to the frustration or avoidance but were not performed, except insofar as some other party to the

contract has become entitled to damages for consequential loss as a result of the failure to fulfil those obligations.

[¶ 42-603]

(3) [*Apportionment of loss*]—Where the circumstances giving rise to the frustration or avoidance cause a total or partial loss in value of a benefit to a party required to make restitution under subsection (1), that loss shall be apportioned equally between the party required to make restitution and the party to whom such restitution is required to be made.

[¶ 42-604]

(4) [*Benefit defined*]—In this section, a "benefit" means something done in the fulfilment of contractural obligations whether or not the person for whose benefit it was done received the benefit.

[¶ 42-605]

Sec. 6. Exception—(1) A person who has performed or partly performed a contractural obligation is not entitled to restitution under section 5 in respect of a loss in value, caused by the circumstances giving rise to the frustration or avoidance of a benefit within the meaning of section 5, if there is

(*a*) a course of dealing between the parties to the contract; or

(*b*) a custom or a common understanding in the trade, business, or profession of the party so performing; or

(*c*) an implied term of the contract,

to the effect that the party so performing should bear the risk of such loss in value.

[¶ 42-606]

(2) [*Insurance evidences assumption of risk*]—The fact that the party performing such an obligation has in respect of previous similar contracts between the parties effected insurance against the kind of event that caused the loss in value is evidence of a course of dealing under subsection (1).

[¶ 42-607]

(3) [*Evidence of common understanding*]—The fact that persons in the same trade, business, or profession as the party performing such obligations, on entering into similar contracts, generally effect insurance against the kind of event that caused the loss in value is evidence of a custom or common understanding under subsection (1).

[¶ 42-608]

Sec. 7. Calculation of restitution—Where restitution is claimed for the performance or part performance of an obligation under the contract other than an obligation to pay money.

(*a*) insofar as the claim is based on expenditures incurred in performing the contract, the amount recoverable shall include only reasonable expenditures and

(*b*) if performance consisted of or included delivery of property that could be and is returned to the performer within a reasonable time after the frustration or avoidance, the amount of the claim shall be reduced by the value of the property returned.

[¶ 42-609]

Sec. 8. [Basis of calculation]—In determining the amount to which a party is entitled by way of restitution or apportionment under section 5, no account shall be taken of

(*a*) loss of profits; or

(*b*) insurance money that becomes payable

by reason of the circumstances that give rise to the frustration or avoidance, but account shall be taken of any benefits which remain in the hands of the party claiming restitution.

[¶ 42-610]

Sec. 9. Limitations—(1) No action or proceeding under this Act shall be commenced after the period determined under subsection (2) of this section.

[¶ 42-611]

(2) [*Claim deemed breach of contract*]—For the purposes of subsection (1), a claim under this Act shall be deemed to be a claim for a breach of the contract arising at the time of frustration or avoidance, and the limitation period applicable to that contract applies.

[¶ 42-612—42-680] Reserved

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