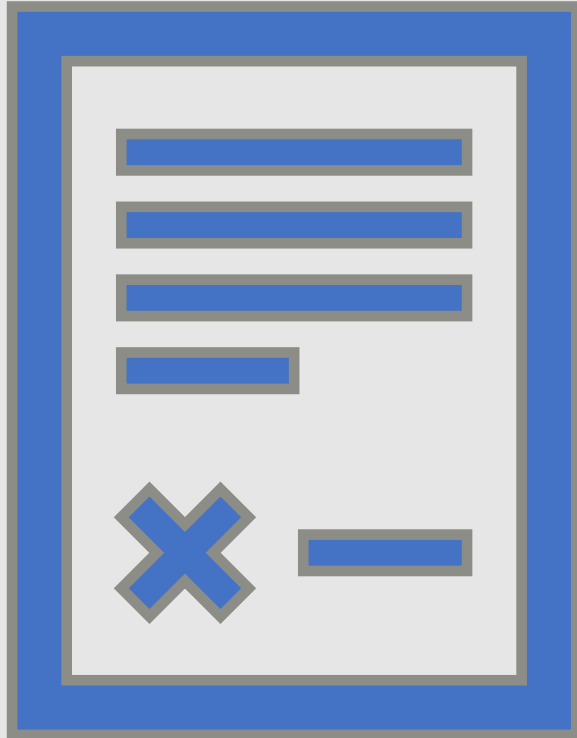


THE LAW OF CONTRACT



HKU | LAW

Lecture 4: Intention to Create Legal Relations, Consideration

Benjamin M. Chen

23 September 2024

Plan for Today

- Intention to Create Legal Relations
- Consideration





INTENTION TO CREATE LEGAL RELATIONS

Contract Formation

- (1) Offer made by one party
- (2) Offer accepted by the other party
- (3) The parties intended to create a legal relation
- (4) The terms of the contract are sufficiently certain and capable of being enforced
- (5) There is consideration on both sides

Legal Enforceability

Even where there is offer and acceptance, there is no contract where the parties did not intend their promises or agreement to be legally enforceable.

The test is, as in most of contract law, an objective one:

“in all these cases the court does not try to discover the intention by looking into the minds of the parties. It looks at the situation in which they were placed and asked itself: would reasonable people regard this agreement as intended to be binding?”

Merritt v. Merritt [1970] 1 WLR 1211 (Denning M.R.)

Legal Enforceability

Two points bear emphasis:

- First, the parties may not have thought about the matter at the outset. Intention to create legal relations is imputed based on the nature of the relationship and context.
- Second, intention to create legal relations should not be confused for willingness to sue. Put differently, do not conflate enforceability and enforcement.

Legal Enforceability

Albert v. Motor Insurers Bureau [1971] 3 WLR 291(Cross L.J.):

“Suppose that when one of Mr. Quirk’s fellow workers got in touch with him and asked whether he could travel in his car to Tilbury and back next day, an ‘officious bystander’ had asked ‘Will you be paying anything for your transport?’ the prospective passenger would have answered at once ‘Of course I will pay’. If the officious bystander had gone on to ask Mr. Quirk whether, if he was not paid, he would sue the man in county court, Mr. Quirk might well have answered...‘Not bloody likely’. But the fact that if default was made Mr. Quirk would not have started legal proceedings but would have resorted to extrajudicial remedies does not mean that an action could not in theory have been brought to recover payment for the carriage. If one imagines such proceedings being brought, a plea on the part of the passenger that he never meant to enter into a contract would have received short shrift...”

See also Esso Petroleum Ltd v. Commissioners of Custom and Excise [1976] 1 WLR 1 (Simon L.J.)

Domestic Agreements

- Domestic agreements between spouses living “in amity” are presumed to be legally unenforceable. *Balfour v. Balfour* [1919] 2 KB 571
- Abstracting from the intention of the parties, policy reasons for this presumption are twofold
 - to avoid judicial intrusion into intimate relationships
 - to avoid overburdening the courts
- But the presumption is negated and may even be reversed in cases where the spouses are separated or about to separate. *Merritt v. Merritt* [1970] 1 WLR 1211
- The same reasoning applies to other familial relationships.
 - *Jones v. Padavatton* [1969] 1 WLR 328 (agreement by mother to finance daughter’s legal studies in England).

Social Agreements

- As with domestic agreements, social agreements are presumed to be legally unenforceable. Examples cited by Atkin L.J. in *Balfour v. Balfour*:
 - agreement to take a walk together
 - offer and acceptance of hospitality
- But this presumption is also rebuttable.
 - *Simpkins v. Pays* [1955] 1 WLR 975 (agreement between housemates to jointly enter a competition and split the winnings legally enforceable)

Commercial Agreements

- Commercial agreements are strongly presumed to be legally enforceable.
 - *Edwards v. Skyways Ltd* [1964] 1 WLR 349 (“ex gratia” payment to a retrenched airline pilot legally enforceable)
- This presumption may be rebutted by express stipulation of the parties.
 - *Rose and Frank Co. v. JR Crompton and Bros Ltd* [1925] AC 445 (no intention to create legal relations where agreement states that “it is not entered into . . . as a formal and legal agreement, and shall not be subject to legal jurisdiction in the Law Courts either of the United States or England...”)
- The presumption may also be rebutted by the context in which the alleged promise was made.
 - *Blue v. Ashley* [2017] EWHC 1928 (Comm) (no intention to create legal relations where promise to pay an investment banker an exorbitant bonus was made by a shareholder in a bar in an “obviously jocular” tone, where the purpose of the meeting was not to discuss compensation, where the promise made no commercial sense, and where none of the witnesses thought the offer was serious)



CONSIDERATION

Contract Formation

- (1) Offer made by one party
- (2) Offer accepted by the other party
- (3) The parties intended to create a legal relation
- (4) The terms of the contract are sufficiently certain and capable of being enforced
- (5) There is consideration on both sides

Reciprocal Transaction

“ULPIAN, Sabinus, book 42: When people know that runaway slaves are being hidden somewhere, they often point them out to their owners where they are hidden; this act does not make them thieves. They often even receive a fee for this act and point out [runaways] on that condition; this payment is also not considered illegal. Therefore, the recipient, because he receives [money] for a reason that is not immoral, does not fear a *condictio*. But what if nothing was paid [in advance], but there was an agreement about a reward, that is, that a fixed sum would be paid if he pointed out the runaway and he was then caught? Can he bring an action? This agreement is not a bare one such as requires the ruling that no action arises from agreement [alone]; **it has a bit of reciprocal transaction in it**. Hence, a civil-law action can arise, that is, *praescriptis verbis*, except if someone might say that the action for fraud lies in this case as well, where a kind of fraud is alleged”.

The Digest of Justinian
(translated by Alan Watson)

Reciprocal Transaction

“It is the essence of consideration, that...it is given and accepted as the motive or inducement of the promise. Conversely, the promise must be made and accepted as the...motive or inducement for furnishing the consideration. The root of the whole matter is the relation of reciprocal conventional inducement, each for the other, between consideration and promise”.

Oliver Wendell Holmes, *The Common Law* (1881)

The Requirement of Consideration

- A promisee must plead and prove that he or she
 - has given up something of value
 - has conferred something of value on the promisorin exchange for the promise he or she is trying to enforce.
- Otherwise, the promise is a *nudum pactum* unenforceable at common law.
- Note that a promise unsupported by consideration may nevertheless be enforceable if
 - it is contained in a valid deed
 - or promissory estoppel applies*

*More on this next lecture

In General

Consideration

- 1) may consist either in some right, interest, profit, or benefit accruing to the one party, or some forbearance, detriment, loss, or responsibility, given, suffered, or undertaken by the other”. *Currie v. Misa* (1875) LR 10 Ex 153 (Lush J)
- 2) means “something which is of value in the eye of the law”. *Thomas v. Thomas* [1842] 2 QB 851, 859
- 3) must be given at the request of the promisor in return for the promise.

Note that the law does not inquire into the adequacy of consideration, only its sufficiency.

In General

- Consideration can consist of a benefit to the promisor or a detriment to the promisee
 - *Bainbridge v. Firmstone* (1838) 8 A & E 743 (plaintiffs gave sufficient consideration for defendant's promise to return boilers in the same condition by parting with possession)
- The benefit or detriment does not actually have to be actual, only legal. The test is in this sense value neutral.
 - *Hamer v. Sidway*, 124 N.Y. 538 (1891) (nephew who abstained from drinking, smoking, and gambling until he was 21 gave sufficient consideration for uncle's promise of \$5,000)
- The consideration must move from the promisee (but not necessarily to the promisor). This is related to the notion of privity in contract.
 - *Tweddle v. Atkinson* [1861] EWHC QB J57 (plaintiff had not supplied consideration for deceased father in law's promise of £200 because the written agreement was made between the latter and plaintiff's father)

In General

Chan Man Tin v. Cheng Leeky

[2008] 3 HKLRD 593, Court of First Instance



Facts

- Defendant counterclaimed against plaintiff arguing that they had entered into an oral agreement for her to replace the plaintiff's former girlfriend. Under the agreement, "in consideration of the plain loyalty and chastity" of the defendant, the plaintiff promised to provide the defendant with accommodation, material support and to "cohabit...and live happily together".
- Defendant contended that when plaintiff emigrated to the United States, he failed to pay her the same separation fee which the latter's former girlfriend had received and ceased to provide any financial support.
- Plaintiff denied any such agreement and argued that it was, in any event, unsupported by consideration.

In General

Chan Man Tin v. Cheng Leeky

[2008] 3 HKLRD 593, Court of First Instance



Held

- There was no consideration supplied by the defendant.
- “It is difficult to understand precisely what is meant by the pleaded consideration ‘plain loyalty and chastity’ of the defendant. But assuming this amounts to her remaining in cohabitation with Mr. Chan, providing no sexual favours to any other person, this has been held to be *contra bonos mores* and unenforceable”.
- “The primary difficulty about [‘cohabit...and live happily together’] amounting to good consideration is that in its form as pleaded the commitment or promise comes from Mr. Chan. But that offends the basic premise that for a promise to be enforceable the consideration in respect of it must move from the promisee”.

In General

Chappell & Co Ltd v. The Nestlé Co Ltd

[1960] AC 87, House of Lords

Facts

- Plaintiffs were owners of the copyright in a song titled “Rockin’ Shoes”.
- Defendants were purveyors of chocolate who offered to sell gramophone records containing the song to anyone who sent in a postal order for 1s 6d together with three wrappers from their 6d milk chocolate bars.
- These wrappers were discarded by Nestlé on receipt.



In General

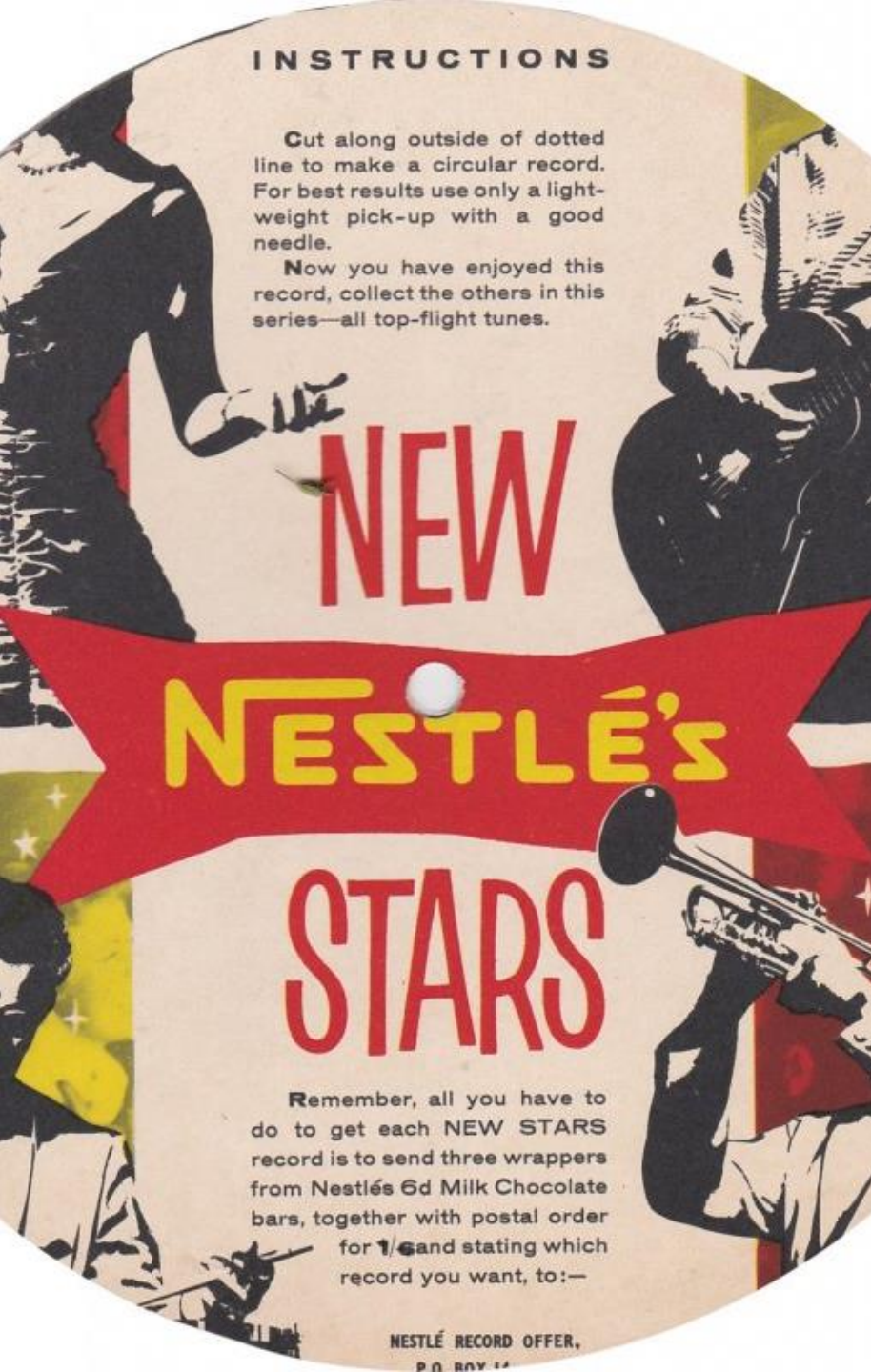
Chappell & Co Ltd v. The Nestlé Co Ltd

[1960] AC 87, House of Lords

Facts

- Section 8 of the Copyright Act 1956 permitted such records to be made for retail provided the copyright owner was given prior notice and paid a royalty of 6¼% of the “ordinary retail price”.
- Defendants notified plaintiffs that the “ordinary retail price” of the records would not exceed 1s 6d.
- Plaintiffs sued for copyright infringement, arguing that Section 8 was inapplicable because the “ordinary retail price” asserted by defendants did not take into account the three wrappers from the chocolate bars.





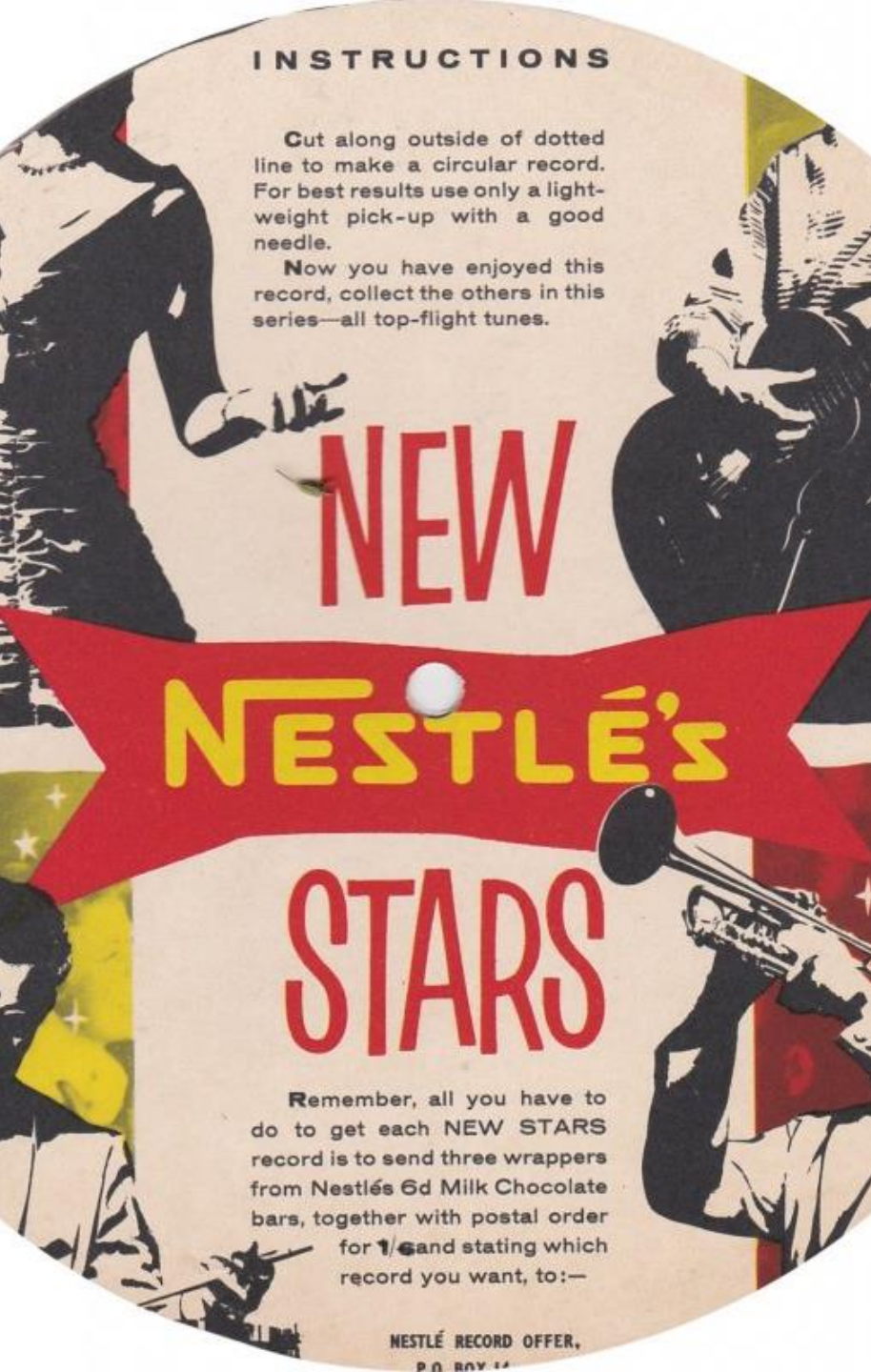
In General

Chappell & Co Ltd v. The Nestlé Co Ltd

[1960] AC 87, House of Lords

Held

- The three wrappers were not a condition to entering into the bargain but were part of the consideration for the bargain itself.
- Reid L.J.: “It seems to me clear that the main intention of the offer was to induce people interested in this kind of music to buy (or perhaps get others to buy) chocolate which otherwise would not have been bought...It seems to me quite unrealistic to divorce the buying of the chocolate from the supplying of the records”.



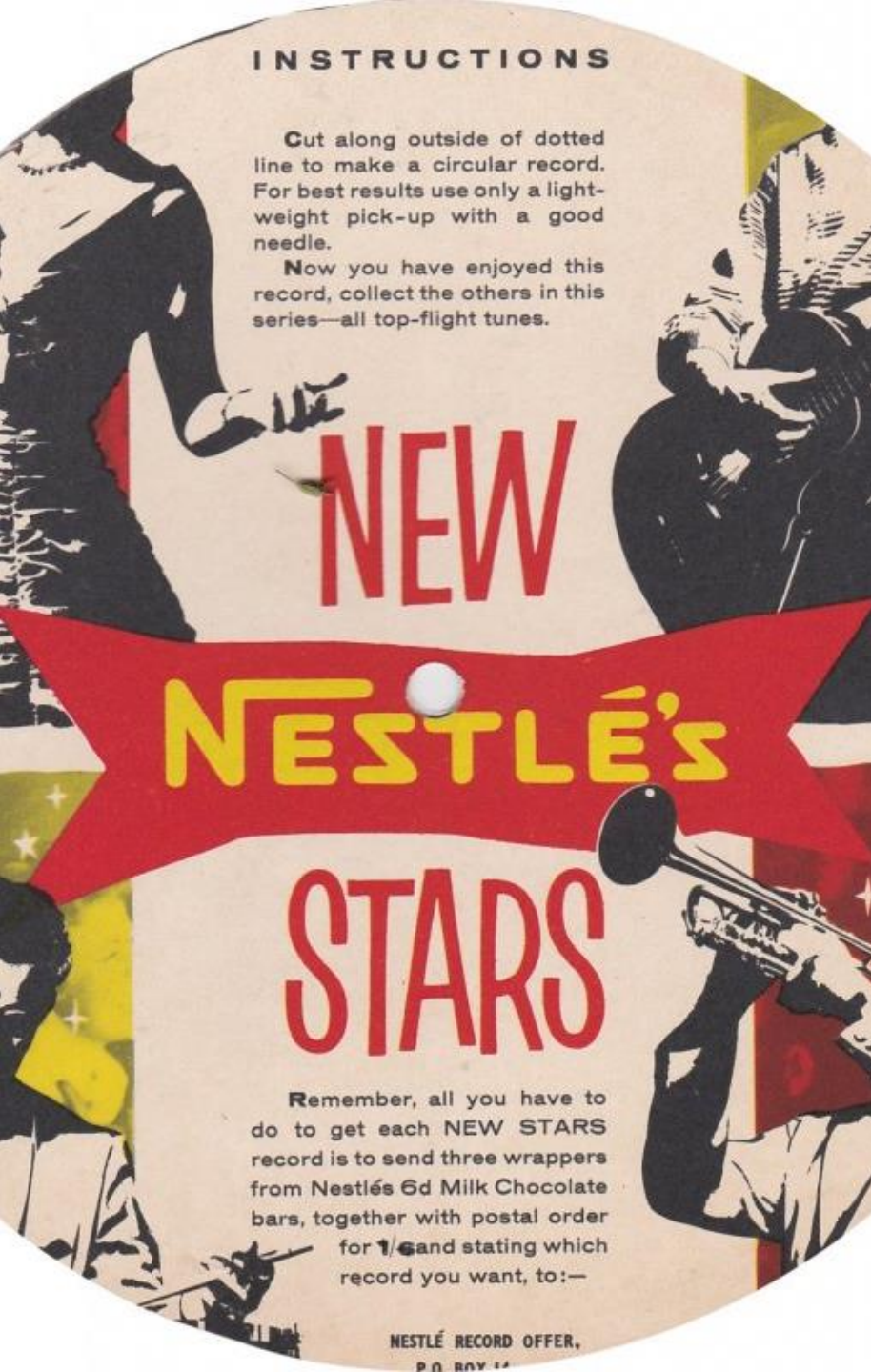
In General

Chappell & Co Ltd v. The Nestlé Co Ltd

[1960] AC 87, House of Lords

Held

- Somervell L.J.: “It is said that when received the wrappers are of no value to Nestlés. This I would have thought irrelevant. A contracting party can stipulate for what consideration he chooses. A pepper-corn does not cease to be good consideration if it is established that the promisee does not like pepper and will throw away the corn. As the whole object of selling the records, if it was a sale, was to increase the sales of chocolate, it seems to me wrong not to treat the stipulated evidence of such sales as part of the consideration”.



In General

Chappell & Co Ltd v. The Nestlé Co Ltd

[1960] AC 87, House of Lords

Held

- Simmonds L.J. (dissenting):
 - The wrappers were of no value in and of themselves but were evidence of a successful marketing campaign. The person sending the wrappers may not have bought the chocolate bars himself or herself. Moreover, the purchase of chocolate bars is not necessarily part of the same transaction as the purchase of the record.
 - The sending of a wrappers were a condition, not consideration. “What can be easier than for a manufacturer to limit his sales to those members of the public who fulfil the qualification of being this or doing that?”

Settlement of Bad or Invalid Claims

A parties who gives up a good legal claim in exchange for payment—or the promise of it—supplies good consideration. What if the legal claim is a bad or invalid one?

- Generally speaking, the promisee's relinquishment of a bad or invalid claim is good consideration. *Cook v. Wright* (1861) 1 B & S 559
- But not if the promisee knows his or her own claim to have no basis. *Wade v. Simeon* [1846] 2 CB 548

Past Consideration

Given that the idea underlying consideration is mutual inducement, the traditional position is that

- past consideration is not good consideration
 - *Re McArdle* [1951] Ch 669 (despite recital, no consideration given by promisee who completed alterations and improvements to house co-owned by promisors before promise to pay her was made)
 - Cf. *Lampleigh v. Braithwaite* (1615) Hob 105 (although promisee had secured a royal pardon for the promisor before promise to pay was made, there was good consideration because the former acted upon a request by the latter)

Existing Duties

Given that the idea underlying consideration is mutual inducement, the traditional position is that

- the discharge of an existing duty to the promisor is not good consideration
- in particular, part-payment of a debt is not good consideration for full discharge of the debt
 - *Foakes v. Beer* (1884) 9 App Cas 605 (even if creditor had agreed to forgo interest on judgment debt by accepting instalment payments, debtor had not supplied any consideration for the promise)
 - *Pinnel's Case* [1602] 5 Co Rep 117a: “payment of a lesser sum on the day in satisfaction of a greater, cannot be any satisfaction for the whole, because it appears to the Judges that by no possibility, a lesser sum can be a satisfaction to the plaintiff for a greater sum: but the gift of a horse, hawk, or robe, etc. in satisfaction is good”

Existing Duties

An existing duty might fall into one of three categories

- public duty or duty imposed by law
 - *Collins v. Godefroy* (1831) 1 B & Ad 950 (attorney subpoenaed to give evidence at trial did not supply good consideration for promised fee of one guinea a day)
 - Cf. *Glasbrook Brothers Ltd v. Glamorgan County Council* [1925] AC 270 (county council gave good consideration for colliery owners' promise to pay £2,200 for billeting police officers in their facility because the garrison was, in the reasonable and good faith judgment of the authorities, a "superfluity" and not "necessary for the protection of life and property".)

Existing Duties

An existing duty might fall into one of three categories

- contractual duty owed to promisor
 - *Stilk v. Myrick* (1809) 2 Camp 318 (as reported by Campbell, sailors did not provide consideration for the promised bonus after two members of the crew deserted as they were already under a contractual obligation to do their utmost to bring the ship home safely)
 - Cf. *Chong Cheng Lin Courtney v. Cathay Pacific Airways Ltd* [2011] 1 HKLRD 10 (plaintiff's continuance in her employment at defendant company furnished consideration for the retiree travel benefit scheme which was contended to be a variation of the original contract)
- contractual duty owed to a third party
 - *Shadwell v. Shadwell* (1860) 9 CB(NS) 159 (nephew who had entered into a marriage contract with his fiancée provided good consideration for uncle's promise of an annuity by performing the contract)
 - *The Eurymedon* [1975] AC 154 (stevedores who were contractually obliged to unload goods from a carrier's vessel provided good consideration for shipper's promise not to sue for damage after one year limitation period)

Past Consideration and Existing Duties

Pao On v. Lau Yiu Long

[1980] AC 614, Privy Council



Facts

- Plaintiffs owned all shares in the Tsuen Wan Shing On company whose principal asset was the Wing On Building. Defendants were majority shareholders in a public-listed company called Fu Chip Investment which desired to acquire Shing On.
- On 27 February 1973, the parties agreed on a price of \$10.5 million to be paid by allotment of \$4.2 million newly issued \$1 shares in Fu Chip at a deemed value of \$2.50 each. At defendants' request, the plaintiffs also covenanted not to sell or transfer 60% of the shares allotted to them on or before 30th April 1974.
- This covenant exposed plaintiffs to the risk of a drop in Fu Chip's share price. The parties thus entered into a subsidiary agreement under which the defendants agreed to buy back the shares at \$2.50 per share on or before the end of April 1974.

Past Consideration and Existing Duties

Pao On v. Lau Yiu Long

[1980] AC 614, Privy Council



Facts

- However, this agreement allowed the defendants to gain from an increase in the share price of Fu Chip. When plaintiffs discovered this, they informed defendants they would not perform the main agreement unless the subsidiary agreement was cancelled and replaced by a guarantee which would become operative only if the share price of Fu Chip fell below \$2.50.
- Defendants were anxious to complete the sale so as not to undermine confidence in the newly listed company and the guarantee was duly executed on 4 May 1973.
- Plaintiffs sought to enforce the guarantee against the defendants when the market price of Fu Chip share slumped. The defendants asserted *inter alia* lack of consideration and duress.

Past Consideration and Existing Duties

Pao On v. Lau Yiu Long

[1980] AC 614, Privy Council



Held

- The consideration recited in the guarantee, i.e. plaintiffs' promises to Fu Chip to complete the sale of Shing On, to accept shares as the price of the sale, and not to sell 60% of these shares before 30th April 1974, was good.
- Scarman L.J.: "An act done before the giving of a promise to make a payment or to confer some other benefit can sometimes be consideration for a promise. The act must have been done at the promisor's request: the parties must have understood that the act was to be remunerated either by a payment or the conferment of some other benefit; and payment, or the conferment of a benefit, must have been legally enforceable had it been promised in advance".

Past Consideration and Existing Duties

Pao On v. Lau Yiu Long

[1980] AC 614, Privy Council



Held

- Scarman L.J.: “[T]he consideration for the promise of indemnity, while it included the cancellation of the subsidiary agreement, was primarily the promise given by the Paos to the Laus, to perform their contract with Fu Chip, which included the undertaking not to sell 60% of the shares allotted to them before the 30th April 1974. Thus the real consideration for the indemnity was the promise to perform, or the performance of, the Paos’ pre-existing contractual obligations to Fu Chip. This promise was perfectly consistent with the consideration stated in the guarantee. Indeed, it reinforces it by imposing upon the Paos an obligation now owed to the Laus to do what, at Lau’s request, they had agreed with Fu Chip to do”.

Assignments and Readings

- Next Lecture
 - Date: 30 September 2024
 - Topic: Estoppel
 - Readings: McKendrick, pages 213 to 245