English Law of Contract: Consideration

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Introduction

• Consideration is a fundamental prerequisite in English contract law
  – Not present in Norwegian/Scandinavian contract law
  – Nor (other) civil law systems
  – Compare to Principles of European Contract Law (1998), Article 2:101

• Basic rule:
  – A promise will not be enforceable unless it is supported by consideration. Main exception to this rule = promises made under seal.
Definition (1)

- A common definition is in terms of the price of a promise, i.e. what one party must “pay” (not necessarily in financial terms) for promise of other party such that promise becomes legally binding (i.e. gives rise to valid contract).
  - See e.g. *Dunlop v. Selfridge* (1915)

- In other words, for promise (offer) to be legally binding, it must seek something (or some action) in return. Promisee must show that they have “bought” the promise either (i) by doing some act in return for it, or (ii) by promising to do or refrain from doing some act in return for it. A type of bargain principle (*quid pro quo*) is at work here.
  - In case of (i), we talk of **executed consideration**:
    - i.e. consideration consisting of performance of act prior to formation of contract (promise only becomes binding when consideration has actually been executed, i.e. performed). This form of consideration typically arises with **unilateral contracts**.
  - In case of (ii), we talk of **executory consideration**:
    - i.e. consideration consisting of promise, where something is to occur in future, after contract formed. This form of consideration typically arises in **bilateral contracts**.
Definition (2)

• Note:
  – Consideration is traditionally needed not just for a new contract to be formed but also for making effective an agreement to vary or discharge an existing contract;
  – Consideration need not benefit promisor; it can consist simply of some detriment to promisee or some benefit to third party:
    • “A valuable consideration, in the sense of the law, 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.” (Lush J. in Currie v. Misa (1875)
  – Consideration is to be distinguished from motive or reason for contracting.
Basic effect:

- Gives **bargains** a legal privilege over **gifts** (gratutious promises).
Rationale (1)

• Several alternatives suggested over the years …
  1. Consideration plays evidentiary and cautionary function. It corroborates the existence of promise and seriousness of promisor’s intention to be bound.
  2. Consideration embodies ideals of reciprocity, *quid pro quo* and thereby fairness.
  3. Consideration explains appropriate measure of relief when promise is not fulfilled. It is essential for determining level of damages/compensation when due performance of promise fails to occur.
  4. Consideration defines appropriate point at which law ought to step in to regulate social and economic relations in order to encourage useful dealings between persons in situations otherwise characterised by lack of trust and sanctions.
  5. Similar to 4, enforcement of bargain helps maximize social efficiency and welfare.
Rationale (2)

• Patrick S. Atiyah

  
  – Atiyah views consideration basically as the “reason for enforcement of a promise”, the reason being “the justice of the case”.
  
  – For Atiyah, the whole process of interpreting contracts revolves around the notion of fairness in exchange. The adequacy of consideration plays an important role in this regard, e.g.

1. If interpretation of terms of contract is difficult, amount of consideration can be important factor in determining what obligations the parties have assumed;

2. The implied condition in a contract (consideration given), and some rough notion that purchaser is entitled to receive adequate value for money. The court does not expressly ask whether purchaser has received adequate value for money, but it does so implicitly.

3. If consideration is grossly inadequate, this may give rise to strong suspicion of fraud or undue influence – which can justify court setting the contract aside.
Requirements for consideration to be valid

A. Consideration must not be past

- Consideration must be given in return for (must be, to some extent, caused by) promise or act of other party, i.e. there must be fairly direct co-relation between consideration and promise/act. Something only done for reason other than promise will not be valid consideration for promise. This requirement is often summed up by the (slightly misleading) expression “consideration must not be past”. See, e.g. Roscorla v. Thomas (1842); Eastwood v. Kenyon (1840); R. v. Clark (1927).

- Decision in Eastwood v. Kenyon also interesting because it highlights tension between consideration and moral obligations. While husband had moral obligation to honour his promise, he did not have legal obligation (for want of consideration). Decision repudiated doctrine advanced by Lord Mansfield that consideration was closely tied to moral obligations and, in particular, that a pre-existing moral obligation furnishes consideration for one’s susequent promise to pay (a doctrine that essentially dispenses with consideration as a separate requirement).
Requirements for consideration to be valid(2)

• A. Consideration must not be past (cont.)
  – Whether consideration is past is a question of fact. Wording of agreement not necessarily conclusive of issue. See e.g. *Re McArdle* (1951).
  – Two exceptions to past consideration rule:
    1. An act already performed may be valid consideration for subsequent promise if:
       a. Act done at promisor’s request; and
       b. Parties understood at time that the act was to be compensated for; and
       c. The promise would have been legally enforceable had it been made prior to the act.
    – Leading cases: *Lampleigh v. Brathwaite* (1615); *Re Casey’s Patents* (1892); *Pao On v. Lau Yiu Long* (1980).
  2. Negotiable instruments, e.g. cheques.
Requirements for consideration to be valid(3)

- **B. Consideration must move from promisee/claimant**
  - Under traditional view, consideration must be provided by promisee in order for them to be able to enforce promise. Thus, party who has not provided consideration for promise cannot enforce promise; it is only the party who has “paid” for promise who can enforce it. This is a basis of the rule of privity of contract, i.e. contract between A and B for benefit of T cannot be enforced by T (if T did not provide consideration for the promise(s) concerned). See e.g. *Tweddle v. Atkinson* (1861).
  - However, this rule has recently been amended by statute, viz. Contract (Right of Third Parties) Act 1999. The Act enables third parties (TPs) to contract to sue on it if:
    a. Contract expressly provides that TP may do so; or
    b. Contract purports to confer benefit upon TP, and contracting parties intend that this be enforceable.
  - NB: While consideration must move from promisee, it need not move to promisor (see above).
Requirements for consideration to be valid(4)

• **C. Consideration must be legal**
  – Consideration cannot be something or some act which is illegal, immoral or contrary to public morals. See e.g. *Wyatt v. Kreglinger and Fernau* (1933).

• **D. Consideration must be requested**
  – There must be express or implied request by promisor to promisee for consideration. Distinguish from conditional gifts.
Requirements for consideration to be valid(5)

• E. Consideration must be sufficient
  – Consideration must provide some benefit to promisor or some detriment to promisee, but benefit or detriment need not amount to much. Indeed, very nominal consideration can be provided for very valuable promises!
  – Nevertheless, consideration must have some economic or material value even if negligible. Consideration cannot consist solely in sentimental or otherwise emotional value – e.g. following someone’s wishes or promising not to keep boring a person with complaints (see espec. *White v. Bluett* (1853); cf. US case of *Hamer v. Sidway* (1891).
  – In some cases, consideration can be provided by promise not to sue. If A has claim against B, A’s promise not to enforce claim can be valid consideration for promise given by B in return. So if B negligently damages A’s property, A’s promise not to sue B for negligence can be consideration for B’s promise to pay for the damage.
    • Leading case: *Alliance Bank Ltd. v. Broom* (1864).
Requirements for consideration to be valid(6)

• **E. Consideration must be sufficient (cont.)**
  
  – Forbearing to enforce a legal claim will only amount to valid consideration if:
    
    a. Claim is reasonable (as opposed to frivolous or vexatious);
    
    b. Promisee honestly believes claim would be successful;
    
    c. Promisee has not concealed facts from promisor which would affect validity of claim; and
    
    d. Promisee evinces intention to bring proceedings if promise not honoured.
  
  – In terms of (b), it does not matter that claim would actually fail in law; promisee must simply believe honestly in claim’s chances of success.

  – NB: Again, party’s promise not to enforce existing claim will only provide consideration if promise provided in return was actually induced by promise not to enforce claim. See e.g. *Combe v. Combe* (1951).
Requirements for consideration to be valid(7)

• **F. Performance of existing duty**
  
  – Performance or promise of performance of an existing duty will usually not amount to consideration. Rationale: promisee suffers no legal detriment (they can already be sued to enforce original promise) and promisor only obtains that to which they were already entitled. But courts have increasingly introduced exceptions to this rule.
  
  – Three main types of existing duty:

  1. **Public duties**
  
     • Person carrying out duties which they are required to do under general law (i.e. independent of contract), will not provide consideration, unless they do something extra. Main rationale: to discourage persons with public duties from demanding additional contractual payments or other benefits for carrying out those duties.
     
     
     – Leading case in which promisee found to have carried out something additional to their public duty: *Glasbrook Brothers v. Glasmorgan County Council* (1925).
Requirements for consideration to be valid (8)

• F. Performance of existing duty (cont.)

2. Existing contractual duty to promisor

– Traditionally found not to be consideration. See e.g. Stilk v. Myrick (1809); cf. Hartley v. Ponsonby (1857). Basic concern of courts here has been to minimise risk of extortion and duress.

– Now distinction needs to be drawn between (i) contractual duties to supply goods or services and (ii) contractual duties to pay debts.

– Regarding (i) see Williams v. Roffey (1990): if one party’s promise to perform an existing contractual duty to supply goods or services confers an extra practical benefit on the other party, it will be sufficient consideration to make a promise given in return binding – as long as no duress is involved and the parties are involved in genuine renegotiations of the contract.
Requirements for consideration to be valid (9)

• F. Performance of existing duty (cont.)
  2. Existing contractual duty to promisor (cont.)
    – In sum, if:
      i. A enters into contract with B to supply goods or services to B in return for payment by B, and
      ii. Prior to A’s completion of his/her obligations B has reason to doubt that A will be able to complete those obligations, and
      iii. B thereupon promises A extra money in return for A’s promise to complete on time, and
      iv. As a result of B’s new promise, B gains in practice a benefit or obviates a disbenefit, and
      v. B’s new promise is not a result of duress or fraud on A’s part, then
      vi. The benefit to B is capable of being consideration for B’s promise (per Glidewell LJ).
    – Most academic commentators praise result, claiming that it accords with commercial reality. But is decision entirely satisfactory?
Requirements for consideration to be valid(10)

• F. Performance of existing duty (cont.)

2. Existing contractual duty to promisor (cont.)
   – In NZ, courts have gone further than Roffey and held that contractual variations, once relied upon, do not need consideration at all: see e.g. NZ Ct. of Appeal decision in Antons Trawling Co. Ltd. v. Smith (2003).
   – Cf. Duties to pay debts – where some person owes another person money, a promise by the latter to accept a smaller repayment will only be binding if the debtor provides some extra element as consideration. Leading decision is Pinnel’s Case (1602), in which Lord Coke famously held:

      • “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 judge, that by no possibility a lesser sum can be satisfaction to the plaintiff for a greater sum.”

   – This is termed the rule in Pinnel’s Case. An example of application of this rule is Foakes v. Beer (1884).
Requirements for consideration to be valid (11)

• F. Performance of existing duty (cont.)
  2. Existing contractual duty to promisor (cont.)
    – A rationale for rule in *Pinnel’s Case* is to protect creditor from pressure from debtor who attempts to force creditor to take less or nothing at all. Yet rule is criticised as not sufficiently refined to distinguish and allow fair and reasonable transactions where part payment is truly desired by creditor. And how do we reconcile rule in *Pinnel’s Case* with *Roffey*?
    – More recent application of rule in Pinnel’s Case is *Re Selectmove Ltd* (1995) per CA, which held that it was bound by precedent to apply the rule (the rule not having been overturned by higher court or legislation). Cf. *Collier v. P & M J Wright (Holdings) Ltd* (2008) – one judge in Court of Appeal prepared to use promissory estoppel (see next lecture) to override effect of *Pinnel’s Case*, but authority is weak.
Requirements for consideration to be valid(12)

- F. Performance of existing duty (cont.)
  2. Existing contractual duty to promisor (cont.)
    - In *Pinnel’s Case*, however, the court made clear that a change to debtor’s obligation (other than reduction of amount owing) could provide consideration for promise by the creditor to accept lesser amount. Thus, early repayment of percentage of original amount owed, could be consideration for creditor’s promise to accept repayment as full settlement of debt. Same could apply if repayment made by third party (see *Hirachand Punamchan v. Temple* (1911) or in different currency or by way of providing material item (rather than money).
    - Rule in *Pinnel’s Case* will also not apply if there is genuine dispute about how much is owed or if any money at all is owed (*Cooper v. Parker* (1885)). It also does not apply to unliquidated claims or composition agreements.
Requirements for consideration to be valid (13)

- F. Performance of existing duty (cont.)
  3. Existing contractual duty to third party
     - Situation: A promises C that A will perform contractual obligation already owed to B; the performance of that obligation can = good consideration for promise made by C to A. Early (though ambiguous) decision on point is *Shadwell v. Shadwell* (1860). Later (and clear) decision on point is *New Zealand Shipping Co. v. A.M. Satterthwaite & Co. (The Eurymedon)* (1975). In *Pao On v. Lau Yiu Long* (1980), Privy Council held that mere promise to perform contractual duty to TP = consideration.