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Keywords

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Contracts Effected With a Bank on the Basis of Coercion or Pressure: Grounds for Judicial Intervention

Or

Contracts Entered Into with a Bank on the Basis of Coercion or Pressure: Grounds for Judicial Intervention

DR. CHARLES Y.C. CHEW*

Abstract

This article critically examines duress as a doctrine relied upon by guarantors or sureties to set aside contracts of guarantees (the most common types of bank security) they have given with inadequate understanding or informed consent. The article discusses duress as “a form of coercion or pressure” which can impair any contractual assent resulting in a guarantee being vitiated. In general terms though, the defence of duress is concerned mainly with the issue of whether the guarantor was placed under unacceptable pressure, or under an illegitimate threat. Common law and equitable concepts in respect of duress apply equally to both guarantees and contracts generally. Nevertheless, since guarantees frequently involve persons who have close relationships to each other, there is probably a greater risk of duress being associated with guarantees than with other kinds of commercial contracts.

Introduction

Contracts of guarantee are being signed in situations where the guarantors have little or no information or are misinformed about important aspects of the transaction such as the borrower's loan or the financial soundness of the business they are supporting. Such guarantees are therefore given with an inadequate understanding of crucial aspects of the transaction, which in general terms would relate to the financial viability of the business secured and the nature and extent of the liability.¹

Contracts of guarantee secure the repayment of the borrower's debts and that dissatisfaction with the borrower's account is probably the reason for the creditor's insistence that such a contract be given. This article deals with a critical analysis of the application of coercion (threat) or pressure, generally referred to as duress to guarantees, resulting in its contribution to the disparity of information between the creditor and the guarantor leading to the guarantee being set aside.

Common law and equity both accept the principle that a party ought not to be held to a contract unless he or she is a free agent, but the contribution made by common law in this domain is confined to the avoidance of contract produced by duress, a term which has a limited meaning. More specifically then, duress occurs

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¹ Trade Practices Commission Discussion Paper: *Guarantors: Problems and Perspectives*, way back in 1992 pointed out that liabilities on guarantees were the main cause of 46% of bankruptcies in Australia in 1990-1991 (when statistics were available) although this figure did not distinguish between liabilities of consumer or commercial guarantees: p.3.

when contractual assent is procured by “illegitimate pressure” brought to bear by one party over the other.²

Different Types of Duress

Different types of duress have been identified, based on the nature of the pressure exerted. They are: duress to the person, duress to goods and economic duress. Where one of these forms of duress is established, it will render the transaction voidable at the option of the victim such as the guarantor and expose the person exerting the pressure to a claim for damages.³

Duress to the person, referred to sometimes as “legal duress”, is seen as actual violence or threats of violence to the person (calculated to bring about fear of bodily harm, loss of life, or loss of physical freedom)⁴ can vitiate the contract. Duress to the person which can include duress to a member of the contractual party’s family⁵ to induce that person to enter into a guarantee can also vitiate the contract,⁶

It has been pointed out that circumstances that would traditionally constitute duress may also be seen as constituting actual undue influence. On this basis, duress

² J Patterson, A Robertson, A Duke, *Principles of Contract Law*, (Australia: Thomson Reuters (Professional) Australia Limited, 2012) p. 694. This proposition is certainly supported in recently cases such as *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 per McHugh JA at 4-6.

³ S Davenport, D Parker, *Business and Law in Australia*, (Australia: Thomson Reuters (Professional) Australia Limited, 2012), pp. 157-8.

⁴ *McLarnon v McLarnon* (1968) 112 Sol J 419; *Cumming v Ince* (1847) 11 Q.B. 112, 120; E.R. 418, 421.

⁵ *Public Service Employees Credit Union Co-op Ltd v Champion* (1984) 75 F.L.R. 131; *Mutual Finance Ltd v John Wetton & Sons Ltd* [1937] 2 K.B. 389.

⁶ *Public Service Employees Credit Union Co-op Ltd v Champion* (2984) 75 F.L.R. 131.

may therefore, for all intents and purposes, have become subsumed by the equitable doctrine of undue influence.⁷

If duress is to be acknowledged as having a continued relevance, it may be as a result of its application in the decision of the Privy Council in *Barton v Armstrong*.⁸ In this case, the basic proposition in the area of duress, in terms of threatened violence, and its general significance can be seen in the judgment of Jacobs JA in *Barton v Armstrong*⁹ later approved on appeal before the Privy Council:¹⁰

“the duress or intimidation must consist in threats of violence calculated to cause fear of loss of life or of bodily harm...or of unlawful imprisonment...to one party or his or her husband or wife or child”.

Duress to goods occurs where contractual assent is procured by actual or threatened seizure, detention, damage or destruction of the contractual party's goods.¹¹ Such duress is also capable of being a ground for setting aside the guarantee.¹² In *Hawker Pacific v Helicopter Charter Pty Ltd*, for example, the court found that an implied threat not to release a helicopter unless an agreement for additional payment was obtained from the plaintiff constituted duress on the basis that there was here an unlawful pressure to withhold goods.¹³ In cases of this kind, it was considered that the plaintiff had no real alternative but to submit to the defendant's demands, and

⁷ L Willmott, S Christiansen, D Butler, B Dixon, *Contract Law* (Australia: Oxford University Press, 2009) p.551.

⁸ [1976] A.C. 104.

⁹ [1976] A.C. 104 at 106.

¹⁰ [1976] A.C.104 at 107.

¹¹ *Skeate v Beale* (1841) 11 Ad & E 983; 113 E.R. 688; *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 N.S.W.L.R. 298; J O'Donovan and J Phillips, (Sydney: *The Modern Contract of Guarantee*, 3rd ed LBC Information Services, 1996), p. 168.

¹² *Vantage Navigation Cpn v Suhail & Saud Bahwan Building Materials (The Alev)* [1989] 1 Lloyd's Rep. 138.

¹³ *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 N.S.W.L.R. 298 at 306.

consequently, the element of compulsion or coercion had been made out. In *The Siboen and the Sibotre*¹⁴ Kerr J gave the following example of the operation of this category of duress:¹⁵

“If I should be compelled to sign a lease or some other contract for a nominal but legally sufficient consideration under an imminent threat of having my house burnt down or a valuable picture slashed...I do not think that the law should uphold the agreement”.

The application of the doctrine of duress, however, is not restricted or limited to duress to the person and duress of goods. Duress is based on a broad general principle, encompassing what is at times termed the doctrine of economic duress.

Economic duress is concerned with contractual assent being procured by actual or threatened conduct which is deleterious to the contracting party's economic interest.¹⁶ Economic duress has important ramifications for contracts of guarantee which are typically entered into in a commercial context. It is the most “difficult” type of duress to understand, due to the fact that commercial or economic pressure of a kind is present in most commercial transactions.¹⁷ A loan contract can be vitiated on the basis of economic duress where the guarantor is induced to enter into the contract by illegitimate pressure in the form of unlawful threats.¹⁸ It is not accurate to characterise economic duress as just driving a hard bargain. This is because it involves an exercise of power in a manner which is not authorised by the existing

¹⁴ [1976] 1 Lloyd's Rep 293.

¹⁵ [1976] 1 Lloyd's Rep 293 at 302.

¹⁶ L Willmott, S Christiansen, D Butler, B Dixon, *Contract Law*, (Australia: Oxford University Press, 2009) pp. 561-565. See SA Smith, “Contracting Under Pressure: A Theory of Duress” [1997] 56 *Cambridge Law Journal* 343 at 346.

¹⁷ A McClelland, “The Doctrine of Economic Duress” (2002) 76 (3) *Law Institute Journal* 69 at 69.

¹⁸ See, for example, *Westpac Banking Corporation v Cockerill* (1998) 152 A.L.R. 67.

contractual arrangements or the general law, in such a way, that the guarantor is left with no alternative but to submit to the illegitimate pressure of the lender.¹⁹

It should be noted that economic duress is not restricted to cases where the lender, such as the bank, is in breach of contract or some other legal wrong. It can occur where the lender resorts to enforce its legal rights so as to obtain concessions which were not envisaged in the original agreement entered into by the parties.²⁰

There is also economic duress where the lender intends to withdraw a loan facility which is not in default. This is done so as to force the guarantor to provide further security.²¹ Economic duress is also present where there is a threat to terminate a fixed interest loan with the intention of forcing the borrower to agree to an increase in interest rate. Yet there is no economic duress where there is a bona fide threat to enforce security, which turns out to be not enforceable for want of consideration.²²

Duress in Guarantee Contracts

The principle of duress was originally based on the fact that the will of the victim was overborne so as to invalidate any contractual consent.²³ The more contemporary view is not so much the lack of consent on the part of the victim that is at issue, but “the

¹⁹ The effect of the pressure is compulsion or the absence of choice. See *Universal Tankship Inc of Moravia v International Transport Workers' Federation* [1983] 1 A.C. 366; *Westpac Banking Corp v Cockerill* (1998) 152 A.L.R..67.

²⁰ *Crescendo Management Pty Ltd v Westpac Banking Corp* (1988) 19 N.S.W.L.R. 40.

²¹ Compare *Wardley Australia Ltd v McPharlin* (1984) 3 BPR 9500

²² *McKay v National Australia Bank Ltd* (unreported, Sup Ct, CA, Victoria, 8 April 1998).

²³ *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd* [1979] Q.B. 705 at 717 and 719; *Pao On v Lau Yiu Long* [1980] A.C. 614 at 635.

victim's intentional submission arising from the realisation that there is no other practical choice open to him".²⁴ The two elements of duress are the procuring of a benefit by compulsion or pressure and the illegitimacy of such pressure²⁵ although it is not necessary to establish that the pressure was the sole or main reason that the contract was entered into, but merely that it was one of the reasons.²⁶ McHugh J in *Crescendo Management Pty Ltd v Westpac Banking Corporation* expressed the view that "pressure will be illegitimate if it consists of unlawful threats or amounts to unconscionable conduct".²⁷ Notwithstanding this reference to "unconscionable conduct", there remains a distinction between duress and unconscionable conduct.²⁸ There has been no decisive resolution of the matter, and for present purposes, one must assume that the two doctrines remain separate.

Crescendo, as mentioned above, marks a crucial point in the development of the doctrine of duress. Before this case was decided, the development of the doctrine was hampered by the traditional requirement that a claim for duress could only be made out if the pressure exerted resulted in the victim's will being overborne so much so that he or she is said to be incapable of acting as a free and independent party.²⁹ If this were literally true the contract entered into would be void. The generally accepted view, however, is that a contract such as a guarantee which is obtained by duress is not void (except perhaps in very extreme cases) but voidable at the discretion of the party subject to the duress. On this basis, the will of the victim may be impaired,

²⁴ *Universal Tankships Inc of Moravia v International Transport Workers Federation* [1983] 1 A.C. 366 at 400.

²⁵ *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 at 46.

²⁶ *Barton v Armstrong* [1976] A.C. 104 at 121 per Lord Wilberforce and Lord Simon.

²⁷ (1988) 19 N.S.W.L.R. 40 at 46.

²⁸ J Patterson, A Robertson, A Duke, *Principles of Contract Law*, (Australia: Thomson Reuters (Professional) Australia Limited, 2012) p. 694.

²⁹ See also *Pao On v Lau Yiu Long* [1980] A.C. 614 at 635; *Westpac Banking Corp v Cockerill* (1998) 152 A.L.R..67.

inhibited or deflected, but it is not destroyed or negated. The victim does indeed assent to the other party's terms but the assent is given because there is no other practical choice open.³⁰

The “overbearing of the will” requirement was rejected in *Crescendo*³¹ where McHugh JA set the appropriate test to be applied:³²

“The proper approach in my opinion is to ask whether any applied pressure induced the victim to enter into the contract and then ask whether that pressure went beyond what the law is prepared to countenance as legitimate”.

So what is important in proving economic duress is not the overbearing of the victim's will but the legitimacy of the pressure used.³³ Illegitimate pressure is where, for example, it consists of unlawful threats³⁴ or amounts of unconscionable conduct.³⁵ Nevertheless, the categories are not closed and “even overwhelming pressure, not amounting to unconscionable or unlawful conduct, however, will not necessarily constitute economic duress”.³⁶

³⁰ (1988) 19 N.S.W.L.R. 40 at 46 (McHugh J). See also, *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366 at 400; *Equiticorp Finance Ltd v Bank of New Zealand* (1993) 32 N.S.W.L.R. 50 at 149-50.

³¹ (1988) 19 N.S.W.L.R. 40 at 45 (McHugh J).

³² (1988) 19 N.S.W. L.R. 40 at 46 (McHugh J).

³³ In line with the rejection of the overborne will theory, the law of duress now focuses on the illegitimacy of the pressure or threats present as opposed to the destruction of the victim's will. See *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 at 45-46. See also *Dimskal Shipping Co S A v International Transport Workers' Federation* [1992] 2 A.C.152 at 166.

³⁴ For example, as when there is a threat to prosecute where the charge is known to be false.

³⁵ Thus rejecting the view that the effect of duress must be such as to “overbear the will”.

³⁶ *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 at 46.

In *Crescendo*, the bank withheld money unless certain documents were signed.³⁷ However, based on the facts, duress was not shown as there was a lack of causation and it was held that the mortgage was executed before the pressure was applied.³⁸

Even though duress was not found to exist in *Crescendo*, the test developed from it was applied in *Karam v ANZ Banking Group Limited & Ors*.³⁹ Here the bank was attempting to procure the signatures of the plaintiffs on certain security documentation.⁴⁰ The bank advised the plaintiffs that, unless they signed the transaction, it would immediately sell their properties and close their already struggling business. For pressure to be illegitimate, it must consist of unlawful threats or unconscionable conduct.⁴¹ The court here found that the pressure exerted by the bank on the Karams to sign the documentation was illegitimate. It was derived from the stronger party, the bank, exploiting the financial vulnerability of the Karams in their desperate financial circumstances, by the threat of cutting off funding, thereby collapsing their business and forcing a sell-off of the bank's securities.

The distinction between what conduct constitutes illegitimate pressure and what is merely the application of reasonable commercial pressure is a fine one. This

³⁷ *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 at 47.

³⁸ *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 at 47.

³⁹ [2001] 1NSW SC 709. *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40 was also applied in *NZI Capital Corporation Ltd v Ianthe Pty Ltd* (Unreported 31 July 1991, Supreme Court of NSW).

⁴⁰ The declaration to be signed by the plaintiffs was to the effect that they acknowledged that any documents signed by them in the past had always been intended to secure to the bank payment of all present, future, actual and contingent liabilities of the company to the bank. Previous security documentation obtained by the bank was unenforceable because at the time the documents had been executed, the plaintiffs had limited English skills and had not obtained independent advice.

⁴¹ M.P. Sidone, "The Doctrine of Economic Duress-Part 2" (1996) 14 *Australian Bar Review* 114 at 138.

can be seen in the case of *Currabubula Holdings & Paola Holdings v State Bank of NSW*⁴² where a claim for economic duress was rejected. Here the plaintiff contended that a guarantee document had only been signed under duress since the bank had refused to release the proceeds of a sale of one of the plaintiff's properties at a time when the plaintiff was experiencing credit difficulties. The court found that the plaintiff signed the Deed of Release out of commercial necessity and not as a result of illegitimate pressure applied by the bank.⁴³

Guarantees are frequently created in circumstances in which the creditor would otherwise take legal proceedings against the principal. As an illustration, directors of a company may secure guarantees for the indebtedness of the company to a creditor in situations where the creditor claims that unless it gets sufficient security for the payment of the debts incurred, it will proceed to bring out a winding-up petition. Where the creditor is entitled to take such proceedings against the principal, it is not likely that a threat to assert its legal rights would amount to duress, unless very exceptional circumstances prevailed.⁴⁴

The doctrine of duress is concerned mainly with the issue of whether the guarantor is placed under unacceptable pressure so that when giving the guarantee he or she is doing so with inadequate understanding or informed consent. Thus, in terms of traditional common law principles, a guarantee will be voidable on the basis of duress to the person, that is, if it is procured by pressure in terms of actual or

⁴² [1999] N.S.W.S.C. 276.

⁴³ This proposition is certainly supported in recently cases such as *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 N.S.W.L.R. 40.

⁴⁴ See, for example, *Powell v Hoyland* (1851) 66 Exch. 67.

threatened violence to the guarantor or actual or threatened deprivation of the guarantor's liberty.⁴⁵

However, duress is not confined to threats of violence. It may consist of an express or implied threat to prosecute, even if the prosecution is justifiable and therefore proper. In *Mutual Finance v Wetton*,⁴⁶ for example, a hire purchase company obtained a guarantee from a customer. The guarantee was forged by the customer's brother. The company asked the customer to sign a genuine guarantee on behalf of the family company, in circumstances in which there was an implied threat that his brother would be prosecuted if he did not. The customer reluctantly signed the fresh guarantee because his father was gravely ill and might not survive the shock of his brother's pending prosecution. The hire purchase company knew that this was the reason why the customer signed. The contract was set aside (when the customer defaulted on his hire purchase instalments) for what was described as "undue influence" although it is probably more accurately characterised as a case of duress (the distinction being difficult to be made) and the guarantors were entitled to repudiate it. Porter J explained why the guarantee was set aside thus:

"It is not necessary to determine the exact bounds beyond which the doctrine would not be applied, but I should myself be inclined to say that it extended to any case where the persons entering into the undertaking were in substance influenced by the desire to prevent the prosecution or possibility of prosecution of the person implicated, and were known and intended to have been so influenced by the person in whose favour the undertaking was given. In the present case, up to the issue of the writ, the defendants were always subject to the fear

⁴⁵ *Barton v Armstrong* [1976] A.C. 104.
; *William v Bayley* (1866) L.R. 1 H.L. 200.

⁴⁶ [1937] 2 K. B. 389.

of a prosecution of Joseph Wetton (the son) and were never free agents. For these reasons I think that the defendants were entitled to avoid the guarantee’’⁴⁷

In deciding on whether pressure is illegitimate, the courts will usually examine the nature of the threat. Pressure will be illegitimate where there is an “unlawful threat”⁴⁸ but not when it relates to a lawful threat to institute civil proceedings.⁴⁹ In the case of a threat that is made in good faith, for example, a request for a variation to the guarantee by the bank may still be considered to be illegitimate if it amounts, in the circumstances, to a “practical compulsion”.⁵⁰ A threat to refuse future business may also amount to duress⁵¹ in the same way as a threat to breach an existing contract. Such a threat can cause a person to enter into a transaction, or to enter into a transaction on certain terms, when they would not otherwise do so.⁵²

Where there is a renegotiation of an existing contract, the pressure may well be illegitimate if the creditor threatens to exercise its powers in a way not authorised by the existing contractual arrangements or the general law, and the circumstances are such that the guarantor has been left with no visible alternative but to submit to the pressure,⁵³ perhaps without the opportunity of obtaining legal advice.⁵⁴

⁴⁷ [1937] 2 K.B. 389 at 396-7.

⁴⁸ [1937] 2 K.B. 389 at 396-7.

⁴⁹ M.P. Sidone, “The Doctrine of Economic Duress-Part 2” (1996) 14 *Australian Bar Review* 114 at 138.

⁵⁰ *TA Sundell & Sons Pty Ltd v Emm Yannoulatos (Overseas) Pty Ltd* (1956) 56 S.R. (NSW) 323.

⁵¹ *Peanut Marketing Board v Cuda* (1924) 34 C.L.R. 38 at 70.

⁵² *Crescendo Pty Ltd v Westpac Banking Corp* (1988) 19 N.S.W.L.R. 40 at 46 per McHugh JA.

⁵³ *Atlas Express Ltd Kafco (Importers & Distributors) Ltd* [1989] Q.B. 833; *B & S Contracts & Design Ltd v Victor Green Publications Ltd* [1984] I.C.R. 419.

⁵⁴ *Atlas Express Ltd v Kafco (Importers & Distributors) Ltd* [1989] Q.B. 833. Cf. *Pao On v Lau Yiu Long* [1980] A.C. 614.

Statutory Intervention

The impact of statutory intervention on the doctrine of duress is varied. One possibility is legislation in the form of the *Australian Consumer Law* (ACL) in Schedule 2 of the *Competition and Consumer Act 2010* (Cth) (formerly *Trade Practices Act* (Cth) 1974 (TPA) which prohibits certain types of duress. For example, s 50 of the ACL (formerly s 60 of the TPA) prohibits the use of coercion, physical force, or undue harassment which was explained in the earlier case of *Australian Competition and Consumer Commission v Maritime Union of Australia* (decided under the TPA)⁵⁵ in the following terms:

“Coercion...carries with it the connotation of force or compulsion or threats of force or compulsion negating choice or freedom to act....A person may be coerced by another to do something or refrain from doing something, that is to say, the former is constrained or restrained from doing something or made to do something by force or threat of force or other compulsion. Whether or not repetition is involved in the concept of harassment, and it usually will be, it is not in the concept of coercion”.⁵⁶

Coercion as used in the ACL has a wider meaning than duress under the general law. The same is true of the remedial provisions pursuant to contravention. There is an extensive range of remedies, in respect of, for example, an unjust contract such as a guarantee obtained by the creditor. Such remedies encompass injunctions⁵⁷ and ancillary orders including rescission, restitution, and variation of the contract.⁵⁸ It is important to note that, unlike the position at common law, a person such as a

⁵⁵ [2001] FCA 1549.

⁵⁶. [2001] FCA 1549 at [61] per Hill J.

⁵⁷ *Australian Consumer Law 2010* (Cth), ss 232-235.

⁵⁸ *Australian Consumer Law 2010* (Cth), s 237 and s 238.

guarantor who suffers loss by the conduct of another person such as a creditor may recover damages.⁵⁹

Another possibility, as encapsulated in the well-known *Contracts Review Act 1980* (NSW) is the more flexible interpretation of the common law rules whereby duress in the State of New South Wales, the largest state in Australia, may be taken into account by the court as a relevant factor in deciding whether to set aside a contract such as a guarantee. Section 9 (2) (j) of the Act deals with the central concepts of unfair pressure or unfair tactics which if exerted on a party such as the guarantor raises the question of whether the contract was unjust. Unfair pressure has been found where a party entered into a contract of guarantee as a result of sustained persuasive pressure beyond the limits of acceptable behaviour,⁶⁰ such as “cajoling and bullying”.⁶¹ Section 9 (2) (j) stipulates that pressure, which may amount to duress, can allow the court to infer that the contract was unjust, and can also allow that court to make an order for its rescission or some other remedy, such as restitution or compensation.

⁵⁹ *Australian Consumer Law 2010* (Cth), s 236

⁶⁰ *Antonovic v Volker* (1986) 7 N.S.W.L.R. 151.

⁶¹ *Teachers Health Investment Pty Ltd v Wynne* (1996) 41 N.S.W.L.R. 482.

The application of duress to guarantees: a comparative study

On a comparative basis, it can be said that there is no substantial difference between the common law jurisdictions relating to duress as applied to guarantees in say, English, Australia and New Zealand or the United States jurisdictions.⁶²

The common law courts generally take the view that guarantees are often entered into in situations in which the creditor would take legal proceedings against the borrower. Company directors, for example, may give guarantees for the indebtedness of the company to a bank in circumstances in which the bank says that it will issue a winding-up petition if it does not receive adequate security for the payment of the debts. If the bank is entitled to take such proceedings against the borrower, or even if it has a bona fide belief that it is so entitled, then it is unlikely that a threat to assert its legal rights would amount to duress, except in wholly exceptional circumstances.⁶³ In cases concerning, for example, economic duress the courts have pointed out that commercial pressure is not sufficient. It has to be demonstrated that the economic pressure constituted a sufficient cause inducing the guarantor to enter into the relevant contract.⁶⁴

However, in deciding whether or not a contract of guarantee will be vitiated on the basis of economic duress, a more important question to ask is when does the pressure extend beyond normal commercial hard bargaining and become

⁶² In the United States, the *Restatement (Second)* provides in s 175 (1): “If a party’s manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim”.

⁶³ See, for example, *Powell v Hoyland* (1851) 6 Exch. 67.

⁶⁴ *Huyton SA v Peter Cremer GmbH* [1999] 1 Lloyd’s Rep. 620 at 635-639.

“illegitimate”. Phillips and O’Donovan have argued that the English courts have not decided directly on this more stringent test.⁶⁵ By contrast, they have maintained that the matter has been addressed in Australian and New Zealand courts. For example, in the Australian case of *Wardley (Australia) Ltd v McPharlin*⁶⁶ it was noted that a threat to exercise legal rights may be commercially harsh, but may not involve the exercise of improper pressure, such as is required to set aside a guarantee on the grounds of economic duress. In *McPharlin*, the plaintiff sued the defendant on a guarantee given by the defendant to secure moneys advanced by way of mortgage to their company Kailon Pty Ltd. On default by the mortgagor company, the plaintiff informed the defendant that he would proceed immediately to enforce the security unless further guarantees were provided. The defendant eventually agreed to sign a further guarantee but only “under duress”, an expression which the defendant wrote down on the document which was signed by him. Ultimately, the defendant contended that the guarantee was not enforceable because it was obtained by economic duress. Rogers J said that in his view it is not economic duress where the creditor was only threatening to exercise neither more nor less than its existing legal rights.⁶⁷ His Honour held that the guarantee could not be set aside by reason of economic duress since the creditor, even though “driving a hard bargain”, was just threatening to exert its legal rights in the appropriate exercise of its powers.⁶⁸

⁶⁵ J Phillips J and J O’Donovan, *The Modern Contract of Guarantee* (English edition) (United Kingdom: Sweet & Maxwell, 2003) p. 130.

⁶⁶ (1984) 3 BPR 9500.

⁶⁷ (1984) 3 BPR 9500 at 9502. It is possible that a guarantee could be set aside on the basis of economic duress if it has been induced by the creditor’s threat to exercise its legal rights, eg in circumstances where the creditor imposes obligations on the guarantor never contemplated in the original arrangement. See J O’Donovan and J Phillips, *The Modern Contract of Guarantee* (Sydney: 3rd ed LBC Information Services, 1996), p. 148.

⁶⁸ See *Shivas v Bank of New Zealand* [1990] 2 N.Z.L.R. 327.

In *McKay v National Australia Bank Ltd*,⁶⁹ the bank threatened to exercise its rights as a secured creditor if a sale of one of the encumbered properties was not made to lower the debt. The debtor and guarantor subsequently sold their property which had been used as security for the debt under a contract of guarantee. The debtor and guarantor argued that the pressure applied by the creditor to enforce a security had been illegitimate and should therefore be set aside. The court disagreed, holding that the pressure exerted had not been illegitimate since the threat to enforce, in good faith, a security which later turned out to be unenforceable for want of consideration, does not constitute duress. However, pressure may well be illegitimate if the creditor threatens to exercise its powers in a way not authorised by the existing contractual arrangements or the general law, and the circumstances are such that the guarantor has been left with no viable alternative but to submit to the pressure, the practical effect here being compulsion or an absence of choice.⁷⁰ In this sense, economic duress involves more than driving a hard bargain.⁷¹

Similarly, in the New Zealand case of *Shivas v Bank of New Zealand* it was held that although some degree of commercial pressure had been applied to the bank, it was insufficient to amount to duress. Among the matters which played an important part in this conclusion were the fact that the sureties had had plenty of opportunity to obtain advice before signing, and the fact that the allegation of duress was only made two years later.

⁶⁹ [1998] VICSC 124.

⁷⁰ *Universal Tankships Inc of Monrovia v International Transport Workers' Federation* [1983] 1 A.C. 366 *Westpac Banking Corporation v Cockerill* (1998) 152 A.L.R. 67.

⁷¹ *Wardley Australia Ltd v McPharlin* (1984) 3 BPR 9500.

Evaluation and Conclusion

On normal contractual principles, a guarantee will be set aside on the ground of duress to the person, that is, if it is induced by actual or threatened violence to the guarantor, or actual or threatened deprivation to the guarantor's liberty.⁷² Duress to goods, whereby a person enters into a guarantee by reason of actual or threatened seizure, or destruction of that person's goods, is also capable of being a ground for rendering the guarantee voidable.⁷³

However, it must be stressed that only threats of the most serious kind can amount to duress. Only then will the party (guarantor) be placed in a position where he or she has no reasonable alternative. What is considered to be serious seems to depend very much on how the party coerced comprehends the probable consequences of not giving in to the duress at the time it is exerted.⁷⁴ In *Shivas*, as discussed earlier, it was held that despite the fact that some degree of commercial pressure had been applied by the bank, that pressure was not serious enough to amount to duress. The court considered the difficult situation the guarantors were in - where they had to weigh up the unpalatable suggestion that they should give a mortgage against the equally unpalatable suggestion that if they declined, the family home might be sold. The court expressed the view that "there are many occasions in commerce when people have to make choices between unwelcome alternatives but that does not mean for one moment that having chosen one they can claim to have acted under duress".⁷⁵

⁷² *Barton v Armstrong* [1976] A.C. 104.

⁷³ *Public Services Employees Credit Union Co-op Ltd v Champion* (1984) 75 F.L.R. 131.

⁷⁴ See, for example, *Atlas Express Ltd v Kafco Importers & Distributors Ltd* [1989] 3 W.L.R. 389.

⁷⁵ [1990] 2 N.Z.L.R. 327 at 351 per Tipping J.

Other reasons given for arriving at this proposition were that the guarantors were given an opportunity to get advice before executing the document and that there was no opposition to the pressure when it was applied.

Although in appropriate circumstances, a guarantee may be rendered voidable on account of economic duress, commercial pressure alone may not be sufficient. It must be demonstrated that there is coercion by the party (creditor) exercising that pressure, that the guarantor has entered the contract against his or her will so that there was no 'true' consent, and that there was left open no alternative course.⁷⁶

In *NZI Capital Corp Ltd v Ianthe Pty Ltd*⁷⁷ it was held that there had been economic duress when, in breach of contract, a finance company obtained guarantees "coercively" by refusing to grant finance for a project unless the guarantees were given.⁷⁸ In *Westpac Banking Corp v Cockerill*⁷⁹ the respondents claimed economic duress when they signed an agreement that they were unable to obtain finance elsewhere as the bank threatened to appoint a receiver. It was held that lawful pressure may operate as duress, although it is the illegitimacy of the pressure that is important. The court said that neither the threats of appointment and sale, nor the demand for release were wrongful or operated as coercive.⁸⁰

⁷⁶ See *Universal Tankships of Monrovia v International Transport Workers Federation* [1983] 1 A.C. 366, 400; See also *Crescendo Pty Ltd v Westpac Banking Corp* (1988) 19 N.S.W.L.R. 40 at 46 per McHugh JA.

⁷⁷ *NZI Capital Corp Ltd v Ianthe Pty Ltd* (Unreported NSW Supreme Court No 5053/90, 31 July 1991) referred to in M.P. Sidone, "The Doctrine of Economic Duress-Part 1" (1996) 14 *Australian Bar Review* 34.

⁷⁸ M.P. Sidone, "The Doctrine of Economic Duress-Part 1" (1996) 14 *Australian Bar Review* 34.

⁷⁹ (1998) 152 A.L.R. 67.

⁸⁰ (1998) 152 A.L.R. 67.

Economic duress may be seen as a product of both common law and equity, and conduct that may not amount to economic duress may still be actionable as fraud or misrepresentation, undue influence or unconscionability.⁸¹ It is a recent and emergent doctrine and as such its parameters have not been that well established. It remains to be seen if the doctrine will be positively received by the judiciary. It has, however, been accepted in general terms, in the sense that it will be available where prospective guarantors enter into guarantees, on the basis of threats which affect their economic interests or well-being, or where the threats in question have usually been to hold back or refuse existing contractual rights, except where there is a payment or further payment of money.

⁸¹ M. Cope, *Duress, Undue Influence and Unconscientious Bargains* (Sydney: The Law Book Co Ltd, 1985), pp. 103-104, 106-109.