

# *Manifest disadvantage in undue influence: An analysis of its role and necessity*

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*In this article the author examines the recent case law on the requirement of manifest disadvantage in the doctrine of undue influence and argues that the courts have misunderstood the role and relevance of this requirement. By determining what purpose or principle underlies the equitable jurisdiction, the author aims to show that proof of manifest disadvantage should not in fact be necessary in cases of either actual or presumed undue influence.*

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## I INTRODUCTION

The last ten years have been unsettled ones for the equitable doctrine of undue influence. Prior to 1985, it was relatively well established that manifest disadvantage was not an essential precondition to relief in undue influence actions. However, recent decisions beginning with the House of Lords case of *National Westminster Bank Plc v Morgan*,<sup>1</sup> and followed by that of the English Court of Appeal in *Bank of Credit and Commerce International S A v Aboody*<sup>2</sup> have required claimants to prove that a transaction is manifestly disadvantageous to them in order to succeed in an action for undue influence. Developments in the House of Lords late last year have changed this position somewhat: the 1993 case of *CIBC Mortgages v Pitt*<sup>3</sup> overruled *Aboody* and held that manifest disadvantage need not be shown in claims of actual undue influence. Nevertheless, the requirement of manifest disadvantage remains for cases of presumed undue influence.

This paper aims to examine from the perspective of precedent and principle, when (if at all) proof of manifest disadvantage should be necessary in undue influence actions. This undertaking is important because, as manifest disadvantage is not always easy to prove, a claimant's chances of success may depend on whether manifest disadvantage is a necessary requirement. To provide a background, the paper will first discuss the doctrine of undue influence in a general sense. The requirement of manifest disadvantage, including its meaning and treatment in the case law, will then be focused on. This examination will aim to show that the current judicial approach is at odds with traditional lines of authority. Next, the paper will attempt to establish the purpose or principle underlying the jurisdiction. It will be shown that there are currently two competing theories in the case law as to which principle justifies the imposition of

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1 [1985] 1 AC 686.

2 [1990] 1 QB 923.

3 [1994] 1 AC 200.

liability in this area, but that only one of those theories can be supported. On the basis of that discussion, it will be argued that if the law were shaped to give effect to the true purpose behind undue influence, manifest disadvantage would be largely irrelevant in both actual and presumed undue influence actions. The paper will therefore attempt to show that by making manifest disadvantage a necessary requirement, the courts have not only abandoned precedent, but have adopted a misguided view of the principle shaping the jurisdiction, the result of which has been confusion and inconsistency.

## II UNDUE INFLUENCE

### A *An Explanation of the Doctrine*

The basic principles of undue influence are well settled. Undue influence consists of "the gaining of an unfair advantage by an unconscientious use of power by a stronger party against a weaker in the form of some unfair and improper conduct"<sup>4</sup> so that the weaker party is pressured into entering a transaction. There are two categories of undue influence: actual and presumed. In Class 1 cases ("actual undue influence"), the claimant must prove that the impugned transaction was the direct result of the wrongdoer exerting undue influence on the claimant.<sup>5</sup> In Class 2 cases ("presumed undue influence"), a claimant must show there existed a relationship of trust and confidence or of influence<sup>6</sup>

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4 *18 Halsbury's Laws of England* (4 ed, Butterworths, London, 1977) para 332. This statement was endorsed by the New Zealand Court of Appeal in *Contractors Bonding Ltd v Snee* [1992] 2 NZLR 157.

5 Actual undue influence was found to have been exercised in *Contractors Bonding v Snee* in the form of pressure placed on an alcoholic, mentally impaired mother by her son to execute a guarantee and mortgage. It has also been found to exist in the situation of a husband bullying his wife to sign a legal charge in the cases of *Aboody* and *Pitt*.

6 Despite previous rulings to the contrary (for example, *Tufton v Sporni* [1952] 2 TLR 516 and *Lloyds Bank Ltd v Bundy* [1975] 1 QB 326), it is now unnecessary to prove that the relationship is one of confidence, since not every confidential relationship involves influence and vice versa. See *Morgan*, above n 1, 703; also Stephen Kos and Peter Watts *Unjust Enrichment - The New Cause of Action* (New Zealand Law Society Seminar, 1990) 69, 73. It is a relationship which will often have the attributes of a fiduciary relationship. For example, in both types of relationship, the weaker party will usually rely on the disinterested advice and guidance of the stronger party, and repose trust and confidence in that party. However, the two doctrines are distinct. A party to a relationship of influence is entitled to act in a self-interested manner toward the other so long as they do not engage in excessively exploitative conduct. However, according to Finn, the fiduciary principle requires the fiduciary to act selflessly in the interests of the beneficiary, to the exclusion of her own interests. See P D Finn "The Fiduciary Principle" in T G Youdan (ed) *Equity, Fiduciaries and Trusts* (Law Book Co Ltd, Toronto, 1989) 4, 25. The doctrine of undue influence does not demand this level of loyalty. Hence, relationships of influence are not always of a fiduciary nature and in recognition of that fact, it is now thought unnecessary to show that a fiduciary relationship existed between the parties in an undue influence action. See Stephen Kos and Peter Watts *Unjust Enrichment - The New Cause of Action* (New Zealand Law Society Seminar, 1990) 69, 75.

between the claimant and wrongdoer such that it raises a presumption that the wrongdoer exercised undue influence over the weaker party.<sup>7</sup> A relationship of influence in a Class 2 case can arise in two ways: in "Class 2A" cases, certain well-established categories of relationship (such as doctor and patient, solicitor and client, guardian and ward, parent and child, and religious adviser and disciple) are presumed as a matter of law to involve influence. Relationships not falling within Class 2A may nevertheless raise the presumption if the claimant can prove on the facts that there existed a relationship of influence ("Class 2B"). The advantage of the second category of undue influence for the claimant is that, having raised the presumption, the burden then shifts to the *wrongdoer* to prove affirmatively that no advantage was taken of the subservient party and that the claimant entered freely and independently into the transaction.

The effect of a finding of undue influence is to make a contract voidable, as opposed to void.<sup>8</sup> Hence, a victim of undue influence is entitled to set the transaction aside as against the wrongdoer. The doctrine also extends to cases where the wrongdoer was not a party to the impugned transaction. In other words, undue influence can be imputed to a third party and the resulting transaction set aside as against that party as well. There are two traditional grounds for setting aside a transaction against a third party: first, where the wrongdoer acted as *agent* for the third party in procuring the claimant's agreement; and second, where the third party had *actual or constructive notice* of the circumstances giving rise to the undue influence.

#### *B Transactions That Will Not Trigger the Doctrine*

Courts have never set aside transactions merely on the ground of the "folly, imprudence, or want of foresight on the part of donors".<sup>9</sup> This has been clear since Lord Nottingham's dictum that "Chancery mends no man's bargain".<sup>10</sup> Salmond J supported this position in the New Zealand Supreme Court case of *Brusewitz v Brown*:<sup>11</sup>

The mere fact that a transaction is based on an inadequate consideration or is otherwise improvident, unreasonable, or unjust is not in itself any ground on which this Court can set it aside as invalid. ... The law in general leaves every man at liberty to make such bargains as he pleases, and to dispose of his own property as he chooses.

In other words, although parties may be on unequal terms, there must be illegitimate influence for there to be relief.

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7 "The presumption of undue influence, like other presumptions, is a tool of the lawyer's trade whose function it is to enable him to arrive at a just result by bridging a gap in the evidence at a point where, in the nature of the case, evidence is difficult or impossible to come by." See *In re the Estate of Brocklehurst* [1978] ChD 14, 43 per Bridge LJ in *Aboody* above n 2, 953.

8 J F Burrows, J Finn, S M D Todd (eds) *Cheshire and Fifoot's Law of Contract* (8 NZ ed, Butterworths, Wellington, 1992) 327.

9 *Allcard v Skinner* (1887) 36 ChD 145, 182-183.

10 *Maynard v Moseley* (1676) 3 Swanst 651, 655.

11 [1923] NZLR 1106, 1109.

### C *Manifest Disadvantage*

The prevailing view for around the last ten years has been that it is not enough simply to show that undue influence was exercised in a Class 1 case, or that a special relationship existed in a Class 2 case. Various decisions have held that in order to succeed in a claim for undue influence, the claimant must also prove that the transaction was of "manifest disadvantage" to him or her. This requirement will now be focused on in greater detail.

## III THE REQUIREMENT OF MANIFEST DISADVANTAGE

In order to explore the place of manifest disadvantage within the doctrine of undue influence, it will be helpful to explain what the term means and to provide examples from the case law of when manifest disadvantage has been held to exist.

### A *The Meaning of Manifest Disadvantage*

Surprisingly, considering the plethora of academic and judicial writing on undue influence, little has been written about the meaning or scope of the term "manifest disadvantage". Lord Scarman's comments in *Morgan* are unrevealing and tautological: according to him, manifest disadvantage is a "serious", "wrongful" and "unfair"<sup>12</sup> disadvantage. Other authorities have described a contract as manifestly disadvantageous if it is "hard and inequitable"<sup>13</sup> or "immoderate and irrational".<sup>14</sup> A manifestly disadvantageous gift would be large or "improvident",<sup>15</sup> although Lord Scarman in *Morgan* suggests that a gift, by definition, is disadvantageous.<sup>16</sup> Slade LJ in *Aboody* expanded on the meaning of the concept, stating that manifest disadvantage must be "obvious as such to any independent and reasonable persons who considered the transaction at the time with knowledge of all the relevant facts".<sup>17</sup> Whether a transaction of charge or guarantee is manifestly disadvantageous depends, according to Slade LJ, on a balance between :

- (a) the seriousness of the risk to the giver that the charge or guarantee will be enforced ; and
- (b) the benefits to be gained by the giver from the transaction.<sup>18</sup>

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12 Above n 1, 704, 707.

13 *Ormes v Beadel* (1860) 2 Gif 166, 174 quoted in *Morgan* above n 1, 704.

14 *Bank of Montreal v Stuart* [1911] AC 120, 137.

15 *Goldsworthy v Brickell* [1987] 1 Ch 378, 401.

16 Above n 1, 704.

17 Above n 2, 965.

18 Above n 3, 965.

*B Examples of Manifest Disadvantage in Case Law*

The authorities above effectively state that manifest disadvantage will involve significant or gross inequality of exchange or value. Perhaps though, a clearer indication of what does or does not constitute a manifest disadvantage can be gleaned from particular examples in the case law. *Poosathurai v Kannappa Chettiar*<sup>19</sup> held that a sale at an undervalue would constitute a manifest disadvantage, while in *Midland Bank Plc v Shephard*,<sup>20</sup> Neill LJ pointed out that the signing of a mandate to open a joint account providing for joint and several responsibility was "potentially disadvantageous"<sup>21</sup> Slade LJ in *Aboody* indicated that a substantial increase in a debtor's potential liabilities is "capable of constituting a manifest disadvantage".<sup>22</sup> In the recent English Court of Appeal case of *Cheese v Thomas*,<sup>23</sup> a transaction whereby the plaintiff agreed to pay £43,000 to the defendant as a contribution to the purchase price of a house in return for the right to live there rent-free for the rest of his life, was held to be manifestly disadvantageous for several reasons: it represented all the plaintiff's capital, he could not regain his money if he wished to move elsewhere, and he would be in jeopardy if the defendant defaulted on mortgage payments.<sup>24</sup>

On the other hand, manifest disadvantage is typically held to be absent in surety cases where the surety is the wife of a debtor and therefore a potential beneficiary of the debtor's dealings for which the security was sought.<sup>25</sup> In the New Zealand Court of Appeal case of *Contractors Bonding Ltd v Snee*, the Court made the statement, in the context of unconscionability, that there was no contractual imbalance because the claimant gained a benefit from the ability to help the debtor, in this case her son.<sup>26</sup> This indicates that the Court would not have found a manifest disadvantage sufficient to make out the undue influence claim also pleaded in the case. In *Petrou v Woodstead Finance Ltd*,<sup>27</sup> a moneylender finance rate of 42% interest per annum was held not to be manifestly disadvantageous because it represented the last resort open to the plaintiff to preserve the matrimonial home from the demands of other creditors. The charge given by the wife in *Morgan* was not manifestly disadvantageous because it secured a loan necessary to rescue the claimant's home at a commercial rate of interest.<sup>28</sup> Similarly, in *Aboody*, the Court of Appeal concluded there was no disadvantage because although there were "substantial potential liabilities" including the loss of the family home, the transactions gave the family business "some hope of survival" which would have enabled the claimant to benefit substantially.<sup>29</sup>

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19 (1919) LR 47 IA 1, 4.

20 [1988] 3 All ER 17 (CA).

21 Above n 20, 23.

22 Above n 2, 966.

23 [1994] 1 WLR 129.

24 Above n 23, 133.

25 M Chen-Wishart "Taking Securities, Taking Advantage" [1993] NZLJ 224, 225.

26 [1992] 2 NZLR 157, 174.

27 [1986] Financial LR 158.

28 Above n 1, 703.

29 Above n 2, 966.

The results in these cases indicate that courts have been reluctant to label transactions manifestly disadvantageous. In particular, the courts tend to deny the existence of manifest disadvantage simply because the claimant *potentially* stood to gain from the transaction. It does not seem to be relevant that in almost every undue influence action, those potential gains never materialise and in fact the claimant is left in a worse position than before the transaction. The reason for this approach is that judges typically test for manifest disadvantage at the time of the transaction, rather than having regard to the outcome of the transaction. This is explicitly confirmed in *Aboody* by Slade LJ who states that "its nature has to be judged in the circumstances subsisting at the date of the transaction, though ... subsequent events may conceivably throw light on what could reasonably have been foreseen as at that date".<sup>30</sup>

### C Case History

If it is the case that judges do not often find manifest disadvantage to be factually present, and yet at the same time require its presence as a precondition to relief, then a claimant's chances of success in an undue influence action will be slim. It therefore important to determine whether manifest disadvantage should be a prerequisite to relief in this cause of action. We can shed light on this question by first examining the historic importance of manifest disadvantage in the case law.

#### 1 The early cases

*Allcard v Skinner*<sup>31</sup> is regarded as the classic undue influence case involving gifts, and as mentioned before, was the first to lay down the classes of undue influence. Class 1 cases were said by Lindley LJ to involve "generally, *though not always*, some personal advantage obtained by a donee".<sup>32</sup> This suggests that any substantive unfairness to the donor or claimant was not a necessary requirement in cases of actual undue influence. Lindley LJ's comments regarding the size of gifts are also significant. He states:<sup>33</sup>

Where a gift is made to a person standing in a confidential relation to the donor, the Court will not set aside the gift if of a small amount simply on the ground that the donor had no independent advice. In such a case, some proof of the exercise of the influence of the donee must be given. ... But if the gift is so large as not to be reasonably accounted for on the ground of friendship, charity, or other ordinary motives on which ordinary men act, the burden is upon the donee to support the gift.

This supports the inference that a court would still be prepared to grant relief even where the gift was small (and therefore of no great disadvantage to the donor) if the claimant can prove the exercise of actual undue influence. In other words, in situations

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30 Above n 2, 965.

31 Above n 9.

32 Above n 9, 181.

33 Above n 9, 185.

where the gift is of a trifling amount, the burden of proof is placed on the claimant.<sup>34</sup> Conversely, where the gift is substantial, the presumption is raised and the burden shifts to the donee. In other words, it may suggest that manifest disadvantage was required to be shown in Class 2 cases. At this point however, no one would have discerned that any clear legal principles regarding manifest disadvantage had been established. For example, the Court of Appeal in the later case of *Wright v Carter*<sup>35</sup> regarded the size of a gift as merely a factor to take into account in determining whether undue influence had been exercised:<sup>36</sup>

the fact that the gift is a very trifling gift, or a gift made by a man with so ample a fortune that it must have been trifling to him, is a matter which might fairly be taken into consideration in considering whether the influence continues.

In *contractual* transactions, it was generally considered that the presence of manifest disadvantage was unnecessary or at least inconclusive in determining whether undue influence was exercised. The view of Sir Owen Dixon in the Australian High Court case of *Johnson v Buttress*<sup>37</sup> was that in cases of actual undue influence, all that needed to be proved was that "the transaction was the outcome of such an actual influence over the mind of the alienor that it cannot be considered his free act".<sup>38</sup> With regard to Class 2 cases, his Honour's approach was that sufficiency of consideration was a material element to invoke in deciding whether the presumption was *rebutted*, but not a requirement necessary to *raise* the presumption.<sup>39</sup> In other words, this approach advocated inquiring into the merits of the transaction after the presumption had been made and not before.<sup>40</sup> Some authorities have gone even further. Lord Chelmsford LC in *Tate v Williamson*<sup>41</sup> stated that "[e]ven if the Defendant could have shown the price he gave was a fair one, this would not alter the case against him". Similarly, writers

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34 M Cope "Undue Influence and Alleged Manifestly Disadvantageous Transactions: *National Westminster Bank Plc v Morgan*" (1986) 60 Australian Law Journal 87, 96; also D Tiplady "The Limits of Undue Influence" (1985) 48 MLR 579, 581.

35 [1903] 1 Ch 27. The case of *Wright v Carter* involved a solicitor-client relationship. The client executed two deeds giving his property in trust to, among others, his solicitor. Another solicitor prepared the documents, but it was held that the deeds should be set aside as the advice was not given by an independent solicitor fully cognizant of the facts.

36 Above n 35, 50.

37 (1936) 56 CLR 113. In this case, the plaintiff sought to set aside a transfer from the deceased (the plaintiff's father) to the defendant of a piece of land on which was erected a cottage. The deceased was an older man, wholly illiterate, of low intelligence, devoid of any capacity for business affairs and who was appreciative of the kindness showed to him by the defendant. He received no independent advice about the transfer. The High Court of Australia held that the transfer should be set aside because the presumption of undue influence had not been rebutted.

38 Above n 37, 134.

39 Above n 37, 136.

40 This view is also expressed by the authors of *Cheshire and Fifoot*, above n 8, 334.

41 (1866) LR 1 HL 200, 213.

such as Spencer Bower,<sup>42</sup> and Meagher, Gummow and Lehane have suggested that "even if the weaker party has received full value this should not shut him out from having the sale set aside ; for the decision to sell may have been the outcome of such an actual influence over the mind of the seller that it cannot be considered his free act".<sup>43</sup> In other words, these authorities all take the view that if the contract has been obtained by unfair pressure which induced the claimant to enter a transaction, it ought not to be upheld, whether or not there has been manifest disadvantage.

However, several Privy Council cases stand apart from this line of authority. The case of *Bank of Montreal v Stuart*<sup>44</sup> appears to suggest that evidence of wrongfulness or manifest disadvantage is necessary to make out a claim of undue influence. Lord Macnaghten stated that :<sup>45</sup>

It may well be argued that when there is evidence of overpowering influence and the transaction brought about is *immoderate and irrational* , as it was in the present case, proof of undue influence is complete.

The 1919 case of *Poosathurai v Kannappa Chettiar*<sup>46</sup> continued in this vein. Lord Shaw held that in a case of presumed undue influence:<sup>47</sup>

It is a mistake ... to treat undue influence as having been established by a proof of the relations of the parties having been such that the one naturally relied upon the other for advice ... Up to that point "influence" alone has been made out. ... more than mere influence must be proved so as to render influence, in the language of the law, "undue". It must be established that the person in a position of domination has used that position to obtain unfair advantage for himself and so to cause injury to the person relying upon his authority or aid.

In other words, the Privy Council took the approach that manifest disadvantage was an essential element to raise the presumption. However, the court in that case was arguably influenced by section 16(1) and (3) of the Indian Contract Act of 1872<sup>48</sup> which

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42 G Spencer Bower, A K Turner and R J Sutton *The Law Relating to Actionable Non-Disclosure and other Breaches of Duty in Relations of Confidence, Influence and Advantage* (2 ed, Butterworths, London, 1990).

43 R P Meagher, W M C Gummow and J R F Lehane *Equity Doctrines and Remedies* (3 ed, Butterworths, Sydney, 1992) para 1524. See also D W McLauchlan "Unfair Contracts - The Law Commission's Draft Scheme" [1991] NZ Recent Law Review 311, 331-332.

44 [1911] AC 120.

45 Above n 44, 137.

46 Above n 19.

47 Above n 19, 3-4.

48 Section 16(1) provides that "the contract is said to be induced by 'undue influence' where the relations existing between the parties are such that one of the parties is in a position to dominate the will of the other, and uses that position to obtain an unfair advantage over the other". Section 16(3) provides: "Where a person who is in a position to dominate the will of another enters into a contract with him, and the transaction appears on the face of it, or on the evidence to be unreasonable, the

required an "unfair advantage" to be shown before a contract could be said to be induced by undue influence. Therefore, the reasoning in that case should probably be restricted to its facts. Nevertheless, two conflicting lines of authority are apparent from the early cases.

## 2 *National Westminster Bank Plc v Morgan*

The decision of the Court of Appeal in *National Westminster Bank Plc v Morgan*<sup>49</sup> followed the former line of authority. Dunn LJ expressed the view that where the court applies the presumption of undue influence, there is no need to prove manifest disadvantage because "once the relationship of confidence is established, then any possible use of the influence is regarded as an abuse".<sup>50</sup> Slade LJ agreed with this and added that:<sup>51</sup>

it is still possible that the relationship and influence arising therefrom has been abused, even though the transaction is, on the face of it, one which, in commercial terms, provides reasonably equal benefits for both parties. Clearly, the proposition that manifest disadvantage need not be shown for either class of undue influence was not inconsistent with earlier decisions.

However, on appeal to the House of Lords, the Court of Appeal's decision was reversed. Lord Scarman, who delivered the judgment, held in relation to the lower court's position on manifest disadvantage, that "principle and authority are against any such proposition".<sup>52</sup> His Lordship held instead that it is necessary to show the transaction is manifestly disadvantageous to the claimant to succeed in a Class 2 case.<sup>53</sup>

Whatever the legal character of the transaction [for example, gift or contract], the authorities show that it must constitute a disadvantage sufficiently serious to require evidence to rebut the presumption that in the circumstances of the relationship between the parties it was procured by the exercise of undue influence. In my judgment, therefore, the Court of Appeal erred in law in holding that the presumption of undue influence can arise from the evidence of the relationship of the parties without also evidence that the transaction was wrongful in that it constituted an advantage taken of the person subjected to the influence which, failing proof to the contrary, was explicable only on the basis that undue influence had been exercised to procure it.

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burden of proving that such a contract was not induced by undue influence shall be upon the person in the position to dominate the will of the other". Lord Shaw in *Poosathurai* claimed the provisions of the Indian Contract Act did not differ from English law. However, his Lordship made no reference to any English cases and in the writer's view, was mistaken in the belief that English law mirrored Indian law in this area.

49 [1983] 3 All ER 85.

50 Above n 49, quoted in Cope, above n 34, 91.

51 Above n 49, quoted in Cope, above n 34, 92.

52 Above n 1, 704.

53 Above n 1, 704.

Lord Scarman claimed support for this view from *Allcard v Skinner*, and the cases of *Bank of Montreal v Stuart* and *Poosathurai v Kannappa Chettiar*. However, Lord Scarman arguably misunderstood the reasoning in *Allcard v Skinner*, and his Lordship made no reference to cases such as *Wright v Carter*, *Tate v Williamson* and *Johnson v Buttress*. He was therefore inaccurate in claiming authority was against the proposition that manifest disadvantage is not a prerequisite to a successful claim of undue influence. In fact, it was probably not until the House of Lords' decision in *Morgan* that manifest disadvantage was explicitly established as a requirement in cases of presumed undue influence.

An interesting point to note is that Lord Scarman's statements regarding manifest disadvantage are arguably obiter only. The facts of *Morgan* concerned a married couple who signed a legal charge over the family home to secure a desperately needed bridging loan. When the husband failed to repay the loan, the bank brought proceedings for possession of the house. The wife claimed as a defence that the charge was procured by the undue influence of the bank manager. Lord Scarman held that the wife's defence failed because the relationship never went beyond the normal business relationship of banker and customer. In other words, no relationship of influence capable of giving rise to the presumption existed. It was therefore unnecessary to go further and decide whether the charge was manifestly disadvantageous to Mrs Morgan.<sup>54</sup> Nevertheless, Lord Scarman chose to deal with the question of manifest disadvantage and as a result, changed the face of undue influence.

### 3 *Bank of Credit and Commerce International S A v Aboody*

In the wake of *Morgan*, the law relating to manifest disadvantage developed in unforeseen ways. Not only did later cases follow *Morgan* in requiring manifest disadvantage in Class 2 cases, but dicta in many cases interpreted *Morgan* as establishing that manifest disadvantage must be shown in Class 1 as well. Examples of this approach can be found in obiter statements in *Coldunell Ltd v Gallon*,<sup>55</sup> *Goldsworthy v Brickell*,<sup>56</sup> and *Midland Bank plc v Shephard*.<sup>57</sup> In the English Court

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54 It was held that the charge was *not* manifestly disadvantageous. In the words of Lord Scarman, "[i]t meant for her the rescue of her home upon the terms sought by her - a short-term loan at a commercial rate of interest". Above n 1, 703.

55 [1986] QB 1184, 1194. Oliver LJ in the English Court of Appeal stated that "whether the relationship between the parties is one from which undue influence is to be presumed or whether there is evidence of actual influence, it has to be shown that the transaction constituted a manifest disadvantage to the party seeking to avoid it".

56 [1987] Ch 378, 405. Nourse LJ stated in passing that "the main ground of their Lordships' decision [in *Morgan*] was that before any transaction can be set aside for undue influence, whether actual or presumed, it has to be shown that the transaction has been wrongful in that it has constituted a manifest and unfair disadvantage to the person seeking to avoid it".

57 Above n 20, 22. In this case, the Court of Appeal held that there was no actual or presumed undue influence. In obiter statements, Neill LJ said that "In order to establish a defence of undue influence it would be necessary for the defendant to prove (a) that she was induced or must be presumed to have been induced to sign the mandate

of Appeal case of *Bank of Credit and Commerce International S A v Aboody*,<sup>58</sup> this interpretation formed part of the ratio. Slade LJ, who incidentally had decided *Morgan* at Court of Appeal level, expressly held that *Morgan* was authority for the proposition that in cases of both actual and presumed undue influence, the complainant must prove the transaction to be manifestly disadvantageous.<sup>59</sup> As a result of Slade LJ's reasoning, the appellant Mrs Aboody lost the case. Although her husband was found to have exercised actual influence to persuade her to sign a legal charge, she was not able to prove to the satisfaction of the court that any of the transactions had been manifestly disadvantageous.

#### 4 The New Zealand response

The cases of *Morgan* and *Aboody* have had a substantial effect on the law of undue influence not only in the United Kingdom but also in New Zealand. *Morgan* was accepted as representing the law of New Zealand in a number of High Court decisions such as *Milsom v Mazey*<sup>60</sup> and *Sareczky v Fodermayer*.<sup>61</sup> The decision of the Court of Appeal in *Contractors Bonding Ltd v Snee*<sup>62</sup> primarily concerned unconscionability

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... (b) that the contract into which she was induced to enter was manifestly disadvantageous to her ...".

58 Above n 2. The proceedings arose out of six transactions comprising three guarantees and three charges of the wife's home signed or made by Mrs Aboody in favour of the bank to secure the liabilities of the family company. In one episode, the bank had provided a solicitor to advise Mrs Aboody independently about the implications of the legal charge, but they were interrupted by Mr Aboody who bullied his wife into signing the document. In 1983, the company collapsed owing the bank nearly £1 million. The bank obtained judgment against the bank but the wife challenged the validity of the guarantees and charges on the ground, inter alia, that they had been obtained by the actual undue influence of the husband.

59 Above n 2, 957.

60 Unreported, High Court, Christchurch, A59/84, 30 May 1985, Heron J. The plaintiff, who had fallen on hard times, purchased a hairdressing salon from the defendant who had set about ensnaring the plaintiff as purchaser. Heron J held that the plaintiff had established a special relationship of influence and that she had been disadvantaged by the terms of the contract, by which she received legal ownership but not actual enjoyment of or control over the asset.

61 (1986) 1 NZBLC 102,492. This case concerned an elderly Hungarian immigrant with little grasp of English who relied on her son-in-law the first plaintiff. She agreed to transfer to him the back portion of a property when called upon, in consideration for the plaintiffs contributing the sum of \$3500 to the purchase of the property. Family relations deteriorated, and when the defendant was asked to transfer the rear portion of the property to the plaintiffs, she refused to do so. The plaintiffs sought specific performance of the agreement and the defendant pleaded, inter alia, undue influence. Henry J affirmed *Morgan* stating that there was a "need to establish that the transaction sought to be set aside was to the 'manifest disadvantage' of the person subjected to the dominating influence". His Honour accordingly held that a claim of actual and presumed undue influence was made out as the sale had been at a gross undervalue.

62 Above n 26.

and the imputation of undue influence to third parties. However, in passing, Richardson J who delivered the leading judgment, set out the elements of undue influence and expressly approved and applied *Aboody* as regards manifest disadvantage.<sup>63</sup>

Whether the relationship between the parties is one from which undue influence is to be presumed or whether there is evidence of actual influence, it has to be shown that the transaction constituted a manifest disadvantage to the party seeking to avoid it.

It is interesting to note however, that the Australian courts have not uniformly followed the *Morgan* line of authorities.<sup>64</sup> Therefore, unless the New Zealand courts in future refuse to follow the approach taken in *Contractors Bonding v Snee*, it appears that Australian and New Zealand law in this area may diverge.

## 5 *CIBC Mortgages Plc v Pitt*

### (a) *The facts of Pitt*

This then, was the state of the law in England and New Zealand relating to manifest disadvantage until the 1993 decision of the House of Lords in *CIBC Mortgages Plc v Pitt*.<sup>65</sup> The facts of *Pitt* were as follows. In 1986, the husband Mr Pitt pressured his wife into executing a legal charge over the matrimonial home in favour of the plaintiff lender, in return for a loan to purchase shares on the stock market. Mrs Pitt did not read any of the documents she signed and did not know the amount that was being borrowed. At no stage did she receive separate legal advice nor did anyone suggest that she should do so. Following the Stock Market crash in 1987, the husband fell into arrears in paying what was due on the charge. Upon the plaintiff commencing proceedings for possession of the matrimonial home, Mrs Pitt raised a defence alleging that the legal charge had been procured by the undue influence of Mr Pitt, and that since Mr Pitt had acted as the agent of the plaintiff, the charge should be set aside as against the plaintiff.

The trial judge held that Mr Pitt had exercised actual undue influence over Mrs Pitt to procure her agreement; that the transaction was manifestly disadvantageous to her; but that since Mr Pitt had not acted as agent for the plaintiff, the claim failed. The Court of Appeal also dismissed her appeal, on the grounds that the transaction was not manifestly disadvantageous, and that the plaintiff had neither actual nor constructive notice of the undue influence.

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<sup>63</sup> Above n 26, 166.

<sup>64</sup> For example, the recent Queensland Supreme Court Case of *Baburin v Baburin* [1990] 2 Qd R 101 involved a plaintiff who executed a transfer of shares that represented a controlling interest in the family company to her sons for a consideration of \$21,000, and later attempted to set aside the transfer on the ground of undue influence. Kelly SPJ held that it was not necessary to demonstrate that the transaction was to the manifest disadvantage of the person influenced in order to establish a claim for undue influence. In referring to *Morgan*, his Honour stated at p 109 of the case that "the Australian authorities do not go this far and I would not think that the proposition as there expressed represents the law of this country".

<sup>65</sup> Above n 3.

(b) *The reasoning of Pitt*

Upon appeal to the House of Lords, Lord Browne-Wilkinson took the opportunity to review the law relating to manifest disadvantage. He concluded that the Court of Appeal in *Aboody* had erred in holding that *Morgan* required manifest disadvantage to be shown in cases of both presumed and actual undue influence. He interpreted Lord Scarman's speech in *Morgan* as establishing that manifest disadvantage had to be shown in order to raise a presumption of undue influence in Class 2, not as "intending to lay down any general principle applicable to all claims of undue influence".<sup>66</sup> Lord Browne-Wilkinson reasoned that:<sup>67</sup>

there is no logic in imposing such a requirement where actual undue influence has been exercised and proved. Actual undue influence is a species of fraud. Like any other victim of fraud, a person who has been induced by undue influence to carry out a transaction which he did not freely and knowingly enter into is entitled to have that transaction set aside as of right. ... A man guilty of fraud is no more entitled to argue that the transaction was beneficial to the person defrauded than is a man who has procured a transaction by misrepresentation.

On the basis of this reasoning, his Lordship held that a claimant who proves the exercise of actual undue influence is entitled as of right to have the transaction set aside without proof of manifest disadvantage.<sup>68</sup> This finding gave Mrs Pitt a prima facie right to set aside the transaction, but nevertheless her claim failed because she was unable to impute the undue influence to the plaintiff: the husband was not acting as agent for the plaintiff in procuring the wife's agreement, and the plaintiff had neither actual nor constructive notice of the undue influence.

(c) *The effect of Pitt*

The House of Lords in *Pitt* has clarified the law somewhat, in overruling *Aboody* and holding that manifest disadvantage need not be shown in an action for actual undue influence. Further, Lord Browne-Wilkinson stated that "the exact limits of the decision in *Morgan* may have to be considered in the future"<sup>69</sup> perhaps implying that manifest disadvantage should not continue to be a necessary element in Class 2 actions either. His Lordship suggested that the law as laid down in *Morgan* was inconsistent with the principle underlying the abuse of confidence cases, namely that fiduciaries are under a heavy duty to "show the righteousness of the transactions they enter into with those to whom they owe such duties".<sup>70</sup> In other words, Lord Browne-Wilkinson suggested that if the law of undue influence was brought into line with the law in abuse of confidence cases, the burden would not lie on a claimant to prove that a transaction was manifestly disadvantageous.

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66 Above n 3, 209.

67 Above n 3, 209.

68 Above n 3, 209.

69 Above n 3, 209.

70 Above n 3, 209.

Nevertheless, despite his Lordship's apparent misgivings about *Morgan*, he did not overrule that case. He merely flagged the matter for later consideration. Presumably therefore, the requirement of manifest disadvantage remains in Class 2 cases of undue influence. Hence, *Pitt* has left the law in a position where a distinction of great significance for future claimants must be made. In cases of actual undue influence, it will not matter if a plaintiff cannot show manifest disadvantage. In presumed undue influence claims, it will be crucial to the success of their action. Can such a distinction, based simply on whether undue influence is actual or presumed, be justifiable in theory or practice? If it cannot, it is necessary to query when (if ever), the presence of manifest disadvantage should be required: in both classes, in Class 2 only or in neither? Answers to these questions depend, not simply on precedent, but more importantly, on the purpose or principle behind undue influence. As the writer will show, by determining what the law attempts to achieve in the area of undue influence, or what mischief it aims at preventing, the role of manifest disadvantage within the doctrine of undue influence will become clear.

#### IV THE PRINCIPLE UNDERLYING UNDUE INFLUENCE

##### A *The Competing Theories*

In the writer's view, there are essentially two alternative views of the purpose underlying the jurisdiction evident in the case law at present. The first theory is that the law of undue influence attempts to prevent victimisation or improper conduct by one party that results in the victim entering a transaction without free and informed consent. Under the "victimisation" theory, the courts seek to protect the integrity or sanctity of relationships that transcend mere commercialism. This theory is articulated in cases such as *Allcard v Skinner*, the Court of Appeal in *Morgan*, and *Pitt* itself. The second theory is that the doctrine of undue influence is based on preventing substantive harm to a party in a transaction. The "harm" theory as it is labelled by the writer, was adopted, albeit implicitly, in the House of Lords judgment in *Morgan* and the Court of Appeal case of *Aboody*. A more detailed explanation of these conflicting theories will now be undertaken. In the process, the way in which each theory impacts upon the requirement of manifest disadvantage will be revealed.

##### 1 *Victimisation and sufficiency of consent*

Undue influence developed historically as an equitable gloss on the common law doctrine of duress,<sup>71</sup> which in turn developed as a corollary to the classical laissez faire notions of freedom and sanctity of contract. Under this paradigm, courts enforce agreements entered into freely and voluntarily by individuals, but will set aside those contracts where consent is vitiated by the existence of, for example, duress, misrepresentation or undue influence.<sup>72</sup> These doctrines are all varieties of fraud and as

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71 Stephen Kos and Peter Watts *Unjust Enrichment - The New Cause of Action* (New Zealand Law Society Seminar, 1990) 69, 73.

72 *Cheshire and Fifoot*, above n 8, 14.

such, they operate to "deny to those who act unconscionably the fruits of their wrongdoing".<sup>73</sup> In other words, it can be said that the principle or purpose underpinning the law of undue influence is to prevent a party behaving in such a manner or placing such pressure on another that the latter acquiesces to some agreement or transaction without proper consent.

This theory places far more emphasis on the *process* or *procedure* by which a transaction is concluded, that is, the way in which one party induces another to enter a transaction, than on the *substantive* terms of a transaction. The Privy Council case of *O'Connor v Hart*<sup>74</sup> aptly explains the difference in the law's treatment of procedural and substantive unfairness:<sup>75</sup>

If a contract is stigmatised as "unfair", it may be unfair in one of two ways. It may be unfair by reason of the unfair manner in which it was brought into existence; a contract induced by undue influence is unfair in this sense. It will be convenient to call this "procedural unfairness". It may also, in some contexts, be described ... as "unfair" by reason of the fact that the terms of the contract are more favourable to one party than to the other. ... it will be convenient to call it "contractual imbalance". ... Equity will relieve a party from a contract which he has been induced to make as a result of victimisation. Equity will not relieve a party from a contract on the ground only that there is contractual imbalance not amounting to unconscionable dealing.

In other words, it is not the *exchange*, but the *influence* which leads a person into a transaction that is decisive in determining whether a claim of undue influence will be successful.<sup>76</sup> It is the conduct of the wrongdoer that is focused on and the resulting procedural unfairness that is punished: the law is not so concerned, according to this theory, to punish substantive unfairness.

There exists substantial judicial authority favouring the victimisation theory. Lindley LJ in *Allcard v Skinner* articulated this theory when he asserted that the doctrine of undue influence was founded on the principle "that it is right and expedient to save [people] from being victimised by other people".<sup>77</sup> His Honour went on to say that the court acts:<sup>78</sup>

to protect people from being forced, tricked or misled in any way by others into parting with their property ... the equitable doctrine of undue influence has grown out of and been developed by the necessity of grappling with insidious forms of spiritual tyranny and with the infinite varieties of fraud.

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73 *Blomley v Ryan* (1954-56) 99 CLR 362, 429.

74 [1985] 1 NZLR 159.

75 Above n 74, 166.

76 D Tiplady "The Limits of Undue Influence" (1985) 48 MLR 579, 582. As Lord Eldon LC puts it in *Huguenin v Basely* 14 Ves 273: "The question is, not, whether she knew what she was doing, had done, or proposed to do, but how the intention was produced".

77 Above n 9, 182.

78 Above n 9, 183.

Both the Court of Appeal in *Morgan* and Lord Browne-Wilkinson in *Pitt* adopted this view of the doctrine. For example, the reasoning of the latter case was based on the principle that:<sup>79</sup>

Actual undue influence is a species of fraud. Like any other victim of fraud, a person who has been induced by undue influence to carry out a transaction which he did not freely and knowingly enter into is entitled to have that transaction set aside as of right.

In addition, almost all Class 2 undue influence cases emphasise that undue influence must be disproved by showing that the transaction was the result of the free and informed consent of the complainant. They do not require proof that the transaction left the claimant substantively unharmed.

Commentators such as Tiplady,<sup>80</sup> Greig and Davis,<sup>81</sup> Kos and Watts,<sup>82</sup> and McLauchlan<sup>83</sup> also favour the victimisation theory. For example, Greig and Davis state that "the reason for setting aside the transaction is ... that the conduct of the stronger party in exerting this influence is regarded as unconscionable".<sup>84</sup> Kos and Watts also argue that the doctrine of undue influence "is concerned with the ascendancy of one party (the beneficiary) over another (the donor) in such circumstances that the transaction at issue cannot be said to be wholly free or voluntary".<sup>85</sup>

Giving effect to this theory has significant ramifications for the requirement of manifest disadvantage. Put simply, if the courts are concerned to ensure that there has been procedural fairness or that a complainant acted of his or her own free will, then once it is shown that a transaction was brought about in an unfair manner through the exercise of undue influence, the transaction should be set aside.<sup>86</sup> The inequality of exchange or the presence of manifest disadvantage is irrelevant. After all, a person can take part in a commercially fair exchange, yet still have been coerced into the transaction or have failed to form an independent and free judgement on the matter.

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79 Above n 3, 209.

80 Above n 76, 582-583.

81 D W Greig and J L R Davis *The Law of Contract* (Law Book Company Limited, Sydney, 1987).

82 Above n 71.

83 Above n 43, 330-331.

84 Above n 81, 961.

85 Above n 71, 67. P G Watts adds that the doctrine is concerned with both "sufficiency of consent" and the defendant's conduct. See P G Watts "Restitution" [1991] NZ Recent Law Review 419, 427.

86 Beck agrees with this approach. He states: "If in truth the defence of undue influence goes to the reality of consent, once it is shown that undue influence has brought about that consent, the contract should be void. The inequality, or otherwise, of exchange is irrelevant". Andrew Beck "Contract" [1993] NZ Recent Law Review 27, 33.

Taken to its logical conclusion then, proof of manifest disadvantage should be wholly unnecessary where actual undue influence has been proved. This was essentially the argument of the defence counsel in *Aboody*. There, counsel argued that in Class 1 cases, "proof of actual undue influence itself proves the wrongfulness of a transaction"<sup>87</sup> and hence there should be no need to go further and show manifest disadvantage. Further, manifest disadvantage should be irrelevant in establishing whether the presumption arises in Class 2 cases of undue influence: it is the special relationship of influence that is crucial to raising the presumption, not the harmfulness of the transaction. In other words, under the victimisation theory, manifest disadvantage should not be an essential element in either class of undue influence.

In order to illustrate the operation of the victimisation theory, let us consider the following fact situation where, if the theory is followed, relief will be available for the claimant:

Vendor has been the client of Purchaser, a solicitor, for over ten years. During that period, Purchaser has become a close friend and adviser. Vendor also relies on her to manage his financial affairs. In 1992, Purchaser discovers that Vendor owns a 1975 Bentley in mint condition. Vendor in fact owns several antique cars and is very proud of his collection. Purchaser offers to buy the Bentley at its market value of \$40,000. Vendor refuses as he is adamant he does not wish to sell. Purchaser applies subtle pressure over a period of six months, including threats to cease managing his affairs or even to see him socially if he does not sell her the car. Purchaser even raises the offer to \$45,000. Vendor fears loneliness and does not believe he could cope without her help, and so reluctantly agrees to sell.

In this situation, Vendor has clearly received a fair price and in fact probably made a profit on the sale. Hence, no manifest disadvantage is present in the transaction. Nevertheless, the exercise by Purchaser of illegitimate pressure would probably be sufficient to make out a claim of actual undue influence. Alternatively, the claimant could point to the existence of a special relationship of influence, arising either from the solicitor/client relationship which is a recognised relationship of influence (Class 2A) or the influence that could be inferred from the facts (Class 2B), so as to raise a presumption that the contract is voidable in a Class 2 case. Unless Purchaser could positively demonstrate that Vendor entered the transaction freely, Vendor's claim would be successful.

## 2 Harm

The "harm" theory of undue influence, was arguably first articulated by the House of Lords in *Morgan*. Lord Scarman stated in that case that the principle justifying a court setting aside a transaction for undue influence was the "victimisation of one party by another"<sup>88</sup> and quoted *Allcard v Skinner* as authority for this proposition. However, his use of the term "victimisation" was quite different from that in *Allcard v Skinner* and other cases. Lord Scarman in fact used this term in a way consistent with "harm" or

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87 See above n 2, 957-959 for the whole discussion of defence counsel's argument.

88 Above n 1, 705.

substantive unfairness for in his eyes, a party could not claim to be "victimized" (that is, harmed) in a transaction which provided reasonably equal benefits to both sides.<sup>89</sup> In other words, this theory focuses on the nature of the exchange or the terms of the transaction: to be set aside, a transaction had to be "wrongful" in the sense that it resulted in a substantive imbalance or detriment to one party.

What then, are the implications of this theory for the requirement of manifest disadvantage? If undue influence is premised on one party being substantively harmed or disadvantaged, then it is logical to require evidence of the harmfulness of the transaction in the form of manifest disadvantage. After all, manifest disadvantage is synonymous with significant inequality of exchange or value. A transaction that is manifestly disadvantageous to a claimant will by definition have harmed that claimant.

Hence it was held in *Morgan* that proof of manifest disadvantage was required in Class 2 cases of undue influence. It is important to note that Lord Scarman at no point referred to actual undue influence in his discussion of manifest disadvantage. In that sense, the court in *Aboody* interpreted *Morgan* in an inaccurate and misleading way.<sup>90</sup> However, taken to its logical conclusion, as it was in *Aboody*, manifest disadvantage or substantive unfairness under the harm theory would have to be shown for *both* classes of undue influence, because without it, a victim could not claim to have been harmed. Therefore, although *Aboody* went beyond *Morgan* in requiring the presence of manifest disadvantage for actual undue influence, this result was entirely consistent with Lord Scarman's reasoning.

Requiring manifest disadvantage in both classes will lead to quite a different result when applied to the hypothetical fact situation mentioned above. Although Vendor may have been unconscionably pressured into selling his antique Bentley, he will not obtain relief from the courts because he will not be able to point to any manifest disadvantage or substantive unfairness in the terms of the transaction. It is therefore apparent that an application of the harm theory to undue influence cases will result in fewer undue influence claims being successful.

### 3 Summary

To summarise, if the purpose behind undue influence is to prevent victimisation that results in involuntary transactions, those transactions should be set aside solely upon proof that a party was subjected to influence and so did not act freely. Because manifest

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<sup>89</sup> Above n 1, 704.

<sup>90</sup> See above n 2, 961. For example, at p 961 of the case, Slade LJ interprets the House of Lords as saying that "in all cases of undue influence a disadvantageous transaction is the 'starting point' from which the court proceeds" when in fact Lord Scarman's words meant nothing of the sort. Lord Scarman had actually said at p 709 of *Morgan*: "It is the *unimpeachability* at law of a disadvantageous transaction which is the starting point from which the court advances to consider whether the transaction is the product merely of one's own folly or of the undue influence exercised by another". Slade LJ makes similar mistakes and misinterpretations throughout the case.

disadvantage has no bearing on whether free consent has been given, it should be irrelevant or at most, one factor among many that establishes a transaction was a product of undue influence. If this theory is the correct way of viewing the doctrine, then the result in *Pitt* would be vindicated. If on the other hand, the doctrine of undue influence is aimed at preventing harm or the extraction of an unfair advantage by a stronger party over a weaker party, then this purpose is best put into effect by requiring manifest disadvantage to be shown in both classes of undue influence. If this is the correct way of understanding undue influence, then the case of *Pitt* would necessarily be unsound and the decisions of *Morgan* and *Aboody* would be preferred.

#### 4 *The Resulting Confusion*

Nevertheless, the writer submits that most judges in undue influence cases are unaware of the implications of each theory for the requirement of manifest disadvantage, and to some extent are unaware that they are even articulating certain theories. Because of this confusion, the result has been inconsistency in the case law as to when and why manifest disadvantage must be shown. The clearest example of this confusion lies in the New Zealand Court of Appeal case of *Contractors Bonding v Snee*.<sup>91</sup> On the one hand, Richardson J affirmed, consistently with earlier cases, that the principle underlying undue influence was the prevention of victimisation:<sup>92</sup>

[Undue influence] is directed at conduct within a relationship which justifies the conclusion that the disposition or agreement was not the result of a free exercise of the disponor's will. The doctrine is founded on the principle that equity will protect the party who is subject to the influence of another from victimisation.

However, he then went on to apply *Aboody* and require manifest disadvantage to be shown for both classes of undue influence.<sup>93</sup> In other words, his Honour applied law that was consistent only with the harm theory of undue influence. If he had attempted to give effect to the principle that equity will protect parties from victimisation, manifest disadvantage would not have been laid down as a requirement for actual undue influence, as it was in the case.

But the issue does not rest there. Having demonstrated the conflict of theories and the resulting confusion afflicting this area of law, it is now necessary to analyse which theory best explains the doctrine, in order to establish firmly when manifest disadvantage is required and to achieve conceptual clarity within the jurisdiction as a whole. It will be argued that the true principle or purpose behind undue influence is not the prevention of harm, as advocated by *Morgan* and *Aboody*, but the prevention of victimisation.

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91 Above n 26. It is important to note, however, that Richardson J's comments regarding manifest disadvantage were obiter and did not represent an important step in the reasoning of the case.

92 Above n 26, 165.

93 Above n 26, 166.

*B Assessment of the Competing Theories*

*1 Deficiencies in the harm theory*

In the writer's view, the harm theory of undue influence cannot be supported by either authority or principle. Dealing first with authority, as has been demonstrated, both judges and commentators agree that the doctrine is concerned with the propriety of the stronger party's conduct and its effect on consent, rather than the adequacy of consideration. *Morgan* and *Aboody* can be viewed as aberrations from this line of authority.

Furthermore, as a matter of principle, the theory cannot be tolerated. In the first place, following the harm theory would mean that notwithstanding a claimant entered a transaction without free and informed consent, a contract would stand unless manifest disadvantage could be shown. This undermines the notion of freedom of contract.<sup>94</sup>

Second, a doctrine of undue influence shaped around the theory of harm prevention could not sit consistently with the closely related doctrines of unconscionability, duress and breach of fiduciary duty. According to leading authorities such as *O'Connor v Hart*,<sup>95</sup> *Moffat v Moffat*,<sup>96</sup> *Nichols v Jessup*,<sup>97</sup> and *Bowkett v Action Finance Ltd*,<sup>98</sup> the proper basis for intervention in the *unconscionability* jurisdiction is the prevention of victimisation or procedural abuse.<sup>99</sup> For example, Somers J in the New Zealand Court of Appeal case of *Nichols v Jessup* stated that:<sup>100</sup>

The equitable jurisdiction to set aside unconscionable bargains is not a paternal jurisdiction protecting or assisting those who repent of foolish undertakings. It is a jurisdiction protecting those under a disadvantage from those who take advantage of that fact; equity looks to the conduct of the stronger party.

Consequently, there is significant authority for the view that inadequate consideration or some other form of substantive unfairness is not an essential precondition to relief.<sup>101</sup> The strongest statements in this regard come from Deane J in

94 However, the writer accepts that classical notions such as freedom of contract have been somewhat eroded this century. See for example D W McLauchlan "The 'New' Law of Contract in New Zealand" [1992] NZ Recent Law Review 436.

95 Above n 74.

96 [1984] 1 NZLR 600 (CA).

97 [1986] 1 NZLR 226 (CA).

98 [1992] 1 NZLR 449 (HC).

99 Chen-Wishart would disagree with this proposition. She argues that, despite the courts' insistence that procedural matters are at the heart of unconscionability, *substantive* unfairness is in fact the basis of judicial intervention in unconscionability cases. See M Chen-Wishart *Unconscionable Bargains* (Butterworths, Wellington, 1989).

100 Above n 97, 235. Emphasis added.

101 See for example *Blomley v Ryan* (1954) 99 CLR 362; *Contractors Bonding Ltd v Snee* above n 26, 174 in which Richardson J confirmed that, as regards

the Australian High Court case of *Commercial Bank of Australia v Amadio*.<sup>102</sup> In his Honour's view, "Notwithstanding that adequate consideration may have moved from the stronger party, a transaction may be unfair, unreasonable and unjust from the viewpoint of the party under the disability."<sup>103</sup> At most, the importance of substantive unfairness is regarded as inversely proportional to that of the procedural elements: "the more serious the procedural abuse the less serious the contractual imbalance would have to be for a finding of unconscionability, and vice versa".<sup>104</sup>

Duress at common law can consist of actual or threatened violence to the person. This century has also seen the expansion of the doctrine of economic duress which involves illegitimate threats to break an existing contract between the parties so as to vary the contract.<sup>105</sup> Again, what emerges from the law of duress, is that where the consent of the victim is induced by such illegitimate pressure, the contract is treated as voidable regardless of the objective fairness of the exchange.<sup>106</sup>

A similar pattern emerges in the area of fiduciary duties. The preventative, prophylactic nature of fiduciary law has always required fiduciary liability to operate strictly with harsh consequences. For example, the seminal cases of *Keech v*

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unconscionability, "any apparent unfairness of the bargain is a factor for consideration [but] it is not the touchstone". Tipping J in *Bowkett* above n 98, 460, states that "inadequacy of consideration is not mandatory but will almost always be present".

102 (1983) 151 CLR 447.

103 Above n 102, 475.

104 This was the approach of *Elia v Commercial and Mortgage Nominees Ltd* (1988) 2 NZBLC 103,296 per Gault J.

105 McLauchlan, above n 43, 329.

106 See *Kos and Watts*, above n 71, 42 ; McLauchlan, above n 43, 328. See also *Barton v Armstrong* [1976] AC 104 ; *Atlas Express Ltd v Kafco (Importers & Distributors) Ltd* [1987] QB 833. This is also the view of commentators such as Cope and Goff and Jones. See M Cope *Duress, Undue Influence and Unconscientious Bargains* (Law Book Company Ltd, Sydney, 1985) 58 ; Lord Goff of Chieveley & Gareth Jones *The Law of Restitution* (3 ed, Sweet and Maxwell, London, 1986) 185. A significant number of duress cases have rejected the notion that duress is concerned with overbearing of the will or vitiating of consent. According to this approach, it is artificial to speak of the will being destroyed because a victim of duress usually knows only too well what he or she is doing. The proper inquiry is whether illegitimate pressure induced the victim to enter the contract, or in other words, to focus on the effect upon the victim's free will of the defendant's conduct, not to ask whether that free will existed at all. See above n 71, 64. In terms of cases, see for example *Lynch v DPP of Northern Ireland* [1975] AC 653; *Universe Tankships Inc v International Transport Workers Federation* [1983] AC 366 per Lord Scarman; *Crescendo Management Property Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40 ; and *Dimskal Shipping Co SA v International Transport Workers Federation* [1991] 3 WLR 875 per Lord Goff.

*Sandford*<sup>107</sup> and *Boardman v Phipps*<sup>108</sup> illustrate that a fiduciary's conduct may be condemned notwithstanding it has no adverse effect at all on the interests of the beneficiary, if there is even a potential for conflict between the trustee's fiduciary position and his or her personal interest. The abuse of confidence cases that Lord Browne-Wilkinson referred to in *Pitt* further illustrate that fiduciaries who enter into transactions with those to whom they owe fiduciary duties must prove that they disclosed all relevant information to the beneficiary and that the transaction was a fair one.<sup>109</sup> The beneficiary in these cases is not required to prove the unfairness of the transaction. Again, it is the law's concern to prevent certain conduct and the abuse of certain protected relationships rather than any substantive unfairness that shapes fiduciary law.<sup>110</sup>

In other words, the doctrines of breach of fiduciary duty, duress and unconscionability do not require proof of substantive unfairness. What triggers the law's response in these cases is the illegitimacy or impropriety of the promisee's conduct and the effect of that conduct on the free will of the promisor.<sup>111</sup> Hence, if the harm theory of undue influence was adopted, it would be doctrinally inconsistent with these theories. Furthermore, it would be harder to make out a successful claim of undue influence than to succeed under the other doctrines. A complainant could conceivably be denied relief in an undue influence claim because the requirement of manifest disadvantage could not be satisfied, yet on the same facts be granted relief for unconscionability or duress. Given that the doctrines historically developed along similar lines and now overlap each other to a considerable extent, it hardly seems appropriate that they should differ in this important respect.<sup>112</sup>

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107 (1726) Sel Cas Ch 61. This was a case in which it was impossible for the beneficiary to obtain the renewal of a lease. Nevertheless the trustee was held accountable for renewal of the lease obtained by him.

108 [1967] 2 AC 46. In this case, the trustees on behalf of the trust executed a takeover of the remaining company shares and, by a liquidation of assets, made capital distributions to the shareholders. The company profited from the transaction but the House of Lords still held the trustees liable to account for the profits.

109 See *Demerara Bauxite Co Ltd v Hubbard* [1923] AC 673, 681-682 (PC) and *Moody v Cox and Hatt* [1917] 2 Ch 71, 83. Both of these cases concerned solicitor-client relationships in which the solicitor had acted as either vendor or purchaser in a transaction with a client. Both courts imposed fiduciary duties on the solicitors to ensure disclosure of all material facts and that the solicitors had acted in the utmost good faith towards their clients.

110 As Finn puts it in "The Fiduciary Principle" in T G Youdan (ed) *Equity, Fiduciaries and Trusts* (Law Book Co Ltd, Toronto, 1989) 4, fiduciary law is concerned to ensure the maintenance of complete loyalty to the beneficiary or in other words, that a fiduciary acts in the sole interests of the beneficiary.

111 See McLauchlan, above n 43, 330.

112 The authors of *Cheshire and Fifoot* also agree. See above n 8, 334. See also P G Watts "Restitution" [1991] NZ Recent Law Review 419. Having stated that undue influence is a subset of unconscionability, and that both doctrines are concerned with sufficiency of consent and the defendant's conduct, Watts points out at pp 427-428 that "If manifest disadvantage is to be a *sine qua non* of undue influence, it is

## 2 *The true principle: prevention of victimisation*

Having canvassed the deficiencies of the harm theory, it is evident that the equitable jurisdiction of undue influence responds not to claims that the terms of an agreement are unfair, but that the agreement was procured in an unfair manner. Therefore, the true principle upon which the doctrine of undue influence rests is the prevention of victimisation or procedural unfairness. Hence, manifest disadvantage should have little place within the doctrine.

If this is the case, then one can query why Lord Browne-Wilkinson in *Pitt* did not go beyond the ratio of the case and make an express ruling to the effect that manifest disadvantage was unnecessary in presumed undue influence cases as well as in Class 1 cases. Such a step would have been helpful in quashing the flawed harm theory once and for all.

There are several possible reasons why Lord Browne-Wilkinson and others like him may be reluctant to abandon the requirement of manifest disadvantage in Class 2 cases. In the first place, without a requirement of manifest disadvantage, the presumption would normally be raised solely upon proof of a special relationship of influence. One could argue that as it is difficult to rebut the presumption, a defendant would be more likely to be held liable and therefore transactions would be more likely to be overturned. This would provide a disincentive for many business people including lawyers or bankers to enter into transactions with parties that could be regarded as weak or reliant on the advice of the former. As so many relationships involve a degree of influence, commerce could arguably be undermined. Hence, courts may require manifest disadvantage or substantive unfairness to be shown in cases of presumed undue influence to ensure that transactions are not set aside lightly.

In addition, judges may arguably be swayed by the desire to see something tangibly wrong with a transaction. The application of improper influence is not always detectable and seemingly leaves no ill effects on a victim. By comparison, substantive unfairness in the terms of the transaction is more obvious, seemingly more invidious, and is more likely to arouse pity in the minds of judges. Why, so the argument goes, should a party who has merely entered a transaction involuntarily be more worthy of the law's protection than a party who has lost property or been in some other way substantively harmed by a transaction?<sup>113</sup>

Such reasoning, if it has been adopted implicitly by courts, is deficient. Commercial convenience, pragmatism and pity are not forces that should normally shape the law. Law should be guided by principle and consistency. If the victimisation theory has explanatory power, then it should be applied in both classes of undue

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unsatisfactory for the same factor to be merely a criterion for consideration in the case of the unconscionable bargain".

113 Of course, this is an argument against having any presumption of undue influence at all, which reveals the deficiencies of the argument.

influence. Further, retaining manifest disadvantage as a requirement for Class 2 cases would lead us back into the very inconsistency (whereby manifest disadvantage is required for Class 2 but not for Class 1) that this paper is trying to avoid. It is simply not necessary to perpetuate the distinction: commerce was never demonstrably weakened in pre-*Morgan* days when it was generally considered by the courts that neither class of undue influence required proof that a transaction was manifestly disadvantageous. Moreover, even if the concerns articulated above do have substance, they can be addressed in ways that do not undermine the victimisation theory and do not result in inconsistency, as will be shown below.

## V THE FUTURE OF MANIFEST DISADVANTAGE

What will be the place of manifest disadvantage within undue influence if judges properly apply the victimisation theory? Simply because it is not a necessary requirement does not mean that it will have no future importance. For example, certain judges and commentators have held the view that manifest disadvantage or the adequacy of consideration is a material element that the dominant party can invoke in seeking to *rebut* the presumption. This approach has been endorsed, for example, by the High Court of Australia in *Johnson v Buttress*,<sup>114</sup> the authors of *Cheshire and Fifoot's Law of Contract*,<sup>115</sup> Meagher, Gummow and Lehane,<sup>116</sup> McLauchlan,<sup>117</sup> and Kos and Watts.<sup>118</sup> Alternatively, it could represent one factor among many in *raising* the presumption. After all, the presence of substantive unfairness can often provide evidence of procedural unfairness or as the Privy Council in *O'Connor v Hart* puts it: "Contractual imbalance may be so extreme as to raise a presumption of procedural unfairness, such as undue influence or some other form of victimisation".<sup>119</sup>

Of course, manifest disadvantage will also continue to be highly relevant because it will often *in fact* be present in undue influence cases. After all, few claimants will risk the time and expense of litigation unless they have been, or stand to be, materially disadvantaged by a transaction. However, the *factual* presence of manifest disadvantage in *many* transactions is not a reason for making it a *legal requirement* in *all* transactions.

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114 Above n 37.

115 Above n 8, 334.

116 Above n 43, para 1524.

117 Above n 43, 331.

118 Above n 71, 81.

119 Above n 74, 166.

## VI CONCLUSION

This paper has attempted to explore the current case law relating to the requirement of manifest disadvantage in the doctrine of undue influence. The paper has shown that the presence of manifest disadvantage can be difficult to prove and therefore that the role of manifest disadvantage in undue influence claims is a crucial one. An examination of precedent stretching from the nineteenth century to the recent case of *Pitt* revealed that it was not always necessary to prove manifest disadvantage, but that contemporary changes in the case law have left the law in an unsatisfactory state whereby a claimant's chance of success may depend on which class of undue influence the action was brought in. An exploration of the principle underlying the doctrine was therefore undertaken to confirm that proof of manifest disadvantage is unnecessary in both actual and presumed undue influence claims because the jurisdiction aims to punish procedural unfairness rather than substantive unfairness.

It is therefore advocated that a claimant who pleads actual or presumed undue influence in the future should not be called on by the courts to show that the transaction was manifestly disadvantageous to him or her, for if precedent and principle were heeded by the courts, manifest disadvantage would be largely irrelevant. Those decisions that have held manifest disadvantage to be a necessary requirement are therefore flawed, and should not be followed by future New Zealand courts.