

## **ECONOMIC DURESS**

Commercial pressure exists wherever one party to a commercial transaction is in a stronger bargaining position than the other party and claims for economic duress are relatively rare. In most cases, a party faced with a 'take it or leave it' attitude, or an unwarranted, unreasonable demand for an increase in the contract sum, can source the subject matter of the contract from elsewhere and, if appropriate, sue the other party for damages for breach of contract.

However, there will be instances where one party to a contract has no other practical option but to agree to unreasonable new terms being imposed upon it. Where illegitimate pressure has been put upon it to do so, a claim for economic duress will arise.

Economic duress in contract occurs, for example, where a party to a contract (A) threatens to cancel the contract unless the other party (B) agrees to their demands and B has no other practical option but to agree to the new terms of the contract. However, the pressure brought to bear by A has to be more than the usual rough and tumble of commercial negotiating and bargaining.

Economic duress evolved from the trade union decisions such as *Universe Tankships v International Workers Federation* (“*The Universe Sentinel*”) [1983] 1 AC 366 and *Dimskal Shipping v International Works Federation* (“*The Evia Luck*”) [1992] 2 AC 152.

In *The Universe Sentinel* the owners of a Liberian registered ship faced a situation where their ship was black listed by a trade union. As a result of the union’s blacklisting of the ship no tug boats would be available so the ship could not sail and there were potentially disastrous consequences. The union insisted on a payment to its welfare fund as a condition of removal of the ship from the black list. The ship owner paid the money to the union but then brought a successful claim for recovery of the money by reason of economic duress. Three Important findings of fact by the trial judge included: “It was a matter of the most urgent commercial necessity that the plaintiffs should regain the use of their vessel. They were advised that their prospects of obtaining an injunction were minimal, the vessel would not have been released unless the payment was made, and they sought recovery of the money with sufficient speed once the duress had terminated.”

A similar situation arose in *The Evia Luck* where a ship owner was faced with a threat that the ship would be black-listed unless various union demands, including a payment to the union, were met. Initially the demands were not met and the ship was black-listed but then the plaintiffs signed the various contractual documents which the union insisted upon so that the ship could sale. The ship owner applied successfully on the grounds of duress for declarations that it had lawfully avoided the various agreements it had entered into.

The necessary ingredients for a successful economic duress claim are:

- Pressure which is illegitimate i.e. there is no commercial or similar justification. The pressure will often take the form of a threat;
- The pressure must be a significant cause inducing the innocent party to enter into the contract i.e. but for the duress it would not have entered into the contract; and
- The practical effect of the pressure is that there is compulsion on, or a lack of practical choice or realistic alternative for, the innocent party.

If the above ingredients are established then the victim of the duress is entitled to avoid the resulting contract and claim restitution of any monies paid under it. Such entitlement will be lost if the victim either expressly or by its conduct affirms the contract.

### **What amounts to illegitimate pressure?**

In determining whether there has been illegitimate pressure the court takes into account a range of factors. "Illegitimate pressure must be distinguished from the rough and tumble of the pressures of normal commercial bargaining." See *DSND Subsea Ltd v Petroleum Geo-Services ASA [2000] EWHC 185*. The relevant factors include:

- (a) Whether there has been an actual or threatened breach of contract;
- (b) Whether the person allegedly exerting the pressure has acted in good or bad faith;
- (c) Whether the victim had any realistic practical alternative but to submit to the pressure;
- (d) Whether the victim protested at the time; and
- (e) Whether he affirmed and sought to rely on the contract.

Case law makes it clear that not every threat to break a contract is illegitimate in the sense required - the threat must be made in support of a demand that is illegitimate and there must be no reasonable alternative but to agree to the demand.

So, for example, economic duress is found where party A refused to pay sums properly due under a contract, knowing that party B was in desperate financial straits. A offered to pay a reduced amount only in full and final settlement on the basis that if the reduced sum was not accepted, then it would pay nothing. Although B accepted the reduced sum, as it had no alternative but to do so, given its financial position, a successful claim was subsequently made against A for the balance.

Economic duress has also been found where party A threatened, without any legal justification, to terminate an existing contract unless the other party, B, agreed (within a few days) to increase the contract price by 10%. B would have lost an extremely lucrative contract with a third party had termination occurred and so agreed, under protest, to the demand.

However, a refusal, in breach of contract, to supply goods unless some extra consideration was supplied by the buyer will not amount to economic duress where alternative supplies are readily available elsewhere in the market. In such cases, the innocent party has a realistic alternative but to submit to the duress: it can source elsewhere and then claim damages for breach of contract subsequently.

The need to establish the lack of a reasonable alternative. The lack of a reasonable alternative is an important factor in any successful claim or defence based on economic duress. The importance of the need to show that there was no reasonable alternative should not be underestimated. This is clear from the decision in *DSND Subsea v Petroleum Geo Services ASA* where the Claimant was carrying out construction work for the Defendant on an oil rig but suspended its work pending the signing of a contractual variation on more favourable terms. The Defendant contended on the basis of economic duress that it should not be bound by the variation. This argument was rejected for three reasons:

(a) The pressure from the Claimant was not illegitimate because the Claimant was acting in good faith in insisting on new terms.

- (b) The Defendant had realistic practical alternatives to accepting the variation of the contract.
- (c) The contract had been affirmed when the Defendant was free from any duress

## INTIMIDATION

An intentional economic tort against a person who issues a threat to engage in unlawful conduct if specified demands are not met. In *Central Canada Potash v Government of Saskatchewan [1979] 1 SCR 42*, the Supreme Court of Canada stated that “A commits a tort if he delivers a threat to B that he will commit an act or use means unlawful as against B, as a result of which B does or refrains from doing some act which he is entitled to do, thereby causing damage either to himself or to C. The tort is one of intention and the plaintiff, whether it be B or C, must be a person whom A intended to injure.

The first version of the tort would be committed where A threatened B and thereby coerced B into acting to his own detriment. By contrast, the second version would entail A threatening B and thereby coercing B into acting in a way that causes loss to a third party claimant.

### Scenario

Mr. Rees owed £482 to the plaintiff building firm, D & C Builders Ltd. In Lord Denning’s words, Mr. Rees’ wife held D & C to ransom. D & C was facing bankruptcy if they weren’t paid, and Mr. Rees’ wife knew it. "She said, in effect: 'We cannot pay you the £480. But we will pay you £300 if you will accept it in settlement. If you do not accept it on those terms, you will get nothing. £300 is better than nothing.'" She made a threat to break the contract, by paying nothing, to compel D & C to accept £300 in settlement, which it was otherwise unwilling to do, and this constituted intimidation. “No person can insist on a settlement procured by intimidation.” See *D & C Builders Ltd v Rees*, [1965] EWCA Civ 3.

The tort of intimidation can be traced to the case of *Rookes v Barnard [1964] AC 1129*. In that case, Douglas Rookes was a draughtsman, employed by British Overseas Airways Corporation (BOAC). He resigned from his union, the Association of Engineering and Shipbuilding Draughtsman (AESD), after a disagreement. BOAC and AESD had a **closed shop** agreement, and AESD threatened a strike unless Rookes resigned also from his job or was fired. BOAC suspended Rookes and, after some months, dismissed him with one week's salary in lieu of proper notice. Rookes sued the union officials, including Mr Barnard, the branch chairman (also

the divisional organiser Mr Silverthorne and the shop steward Mr Fistal). Rookes said that he was the victim of a tortious intimidation that had used unlawful means to induce BOAC to terminate his contract. The strike was alleged to be the unlawful means. At first instance, before Sachs J, the action succeeded. This was overturned in the Court of Appeal. The House of Lords reversed the court of appeal, finding in favour of Rookes and against the union. Citing a case from the eighteenth century called *Tarelton v. M'Gawley* (1793) Peake 270 where a ship fired a cannonball across the bows of another, Lord Reid said the union was guilty of the tort of intimidation. It was unlawful intimidation 'to use a threat to break their contracts with their employer as a weapon to make him do something which he was legally entitled to do but which they knew would cause loss to the plaintiff.

### **Unlawful threat**

The tort of intimidation requires a threat to do something that one is not legally entitled to do. The reasoning would appear to be as follows. The very fact that what I threaten to do would be an unlawful act necessarily colours the threat that I make and gives it the capacity to be treated as independently unlawful. Put otherwise, it is the fact that I am prohibited by law from doing what I threaten to do that causes my words to cross the line that separates lawful persuasion from unlawful coercion.

The tort of intimidation is established where:

- The defendant makes a demand backed by a coercive and unlawful threat.
- The claimant complies with that demand because of the coercive and unlawful threat.
- The defendant knows or should have known that complying with the demand would cause loss and damage to the claimant.
- The defendant intends its demand to cause loss and damage to the claimant.

The key requirement of the tort of intimidation is that there has been a threat to act unlawfully. A threat to do something one is legally entitled to do will not amount to intimidation.

### ***Kolmar Group AG v Traxpo Enterprises PVT Limited [2010] EWHC 113 (Comm)***

Traxpo agreed to supply Kolmar with methanol. The price and quantity were agreed, but it later transpired that when the contract was made, Traxpo did not have access to sufficient cargo at the same or lesser price than the contract price. The situation worsened after the contract was agreed

because the market price of methanol increased dramatically and Traxpo faced a significant shortfall.

The first inkling of a problem emerged when Kolmar was informed by a third party that Traxpo might have been providing cargo earmarked for Kolmar to other customers. Kolmar needed the methanol to fulfil an obligation to an important customer in the US so, to head off any potential difficulties, it arranged for a letter of credit, re-iterating the contract terms, to be opened in Traxpo's favour. The difficulties continued, however, and delays arose when Traxpo failed to provide the necessary paperwork to allow Kolmar's cargo vessel to begin loading. As the shipment date drifted further into the distance, and with Kolmar facing the prospect of renegeing on its contract with its customer in the US and also mounting demurrage, Traxpo informed Kolmar that it was considering backing out of the contract and sought increasingly onerous changes to the terms if it were to proceed. Traxpo's demands culminated in a "take it or leave it" proposal: the price would be increased significantly and the quantity reduced. Kolmar protested to no avail and eventually, on the basis that it had no alternative given the soaring market price for methanol, accepted.

Almost immediately after delivery of the cargo, Kolmar issued proceedings. Traxpo was unrepresented at trial. In addition to awarding Kolmar damages for short delivery, demurrage and shifting expenses, the High Court held that:

- Kolmar only agreed to an increase in the price and reduction of the quantity supplied as a result of Traxpo's illegitimate economic pressure, amounting to economic duress.
- Traxpo's demands, backed by the unlawful threat that it would not perform its obligations, satisfied the requirements of the tort of intimidation.
- Kolmar was entitled, in restitution or as damages for intimidation, to the increased amount (over \$1.4 million) it had been required to pay.

*Kolmar* illustrates that the courts expect companies to behave properly in their commercial dealings, regardless of any recessionary forces or other restrictions, and will act to ensure that parties will not be able to rely on illegitimate threats and financial leverage to prop up margins.

The courts will consider closely the facts in each case to ensure that a coercive and unlawful threat or illegitimate economic pressure, as opposed to fair negotiation, has indeed caused the claimant's actions.

In the current recessionary climate, where contractual relationships are more easily frayed, there are lessons to be learned from *Kolmar* for both potential claimants and defendants.

Sometimes an allegation of economic duress is combined with a claim based on the tort of intimidation but successful claims based on the tort will be rare as the requirements of the tort are more extensive than those for economic duress.

An essential difference between economic duress and the tort of intimidation is that economic duress is a restitutionary remedy entitling a party to avoid the agreement and to obtain a refund of the monies paid, whereas the tort of intimidation allows a party to make a claim for damages.

A potential claimant, before looking to argue economic duress or intimidation, should consider carefully whether or not a threat or demand is in fact illegitimate and goes beyond the negotiating pressures common in the commercial world. If a potential claimant is convinced that its counterparty is acting unlawfully then, as a matter of best practice, it should do as much as possible to demonstrate that it is being forced to act under coercion. Clear indicators of this would be to protest at the time and to take legal action as soon as practicable afterwards.

The potential claimant should also explore realistic alternatives, such as trying to source the required services or goods elsewhere in the market. Each of these steps will not, of themselves, establish economic duress or intimidation, but they are strong evidential factors. Potential defendants should obviously consider whether what they are proposing is unlawful. Beyond that, a company should consider the effect of its demand on the potential claimant and the influence that demand may have on the potential claimant's actions, and assess whether the demand risks being cast as improperly exploiting commercial strength.