OUTER HOUSE, COURT OF SESSION

[2013] CSOH 26

OPINION OF LORD MALCOLM

in the cause

PHIL WILLS

Pursuer;

against

STRATEGIC PROCUREMENT (UK) LIMITED

Defender:

Pursuer: R Dunlop QC, A Mckenzie; Lefevre Litigation

Defender: Lake QC, Ower; Maclay Murray & Spens LLP

13 February 2013

[1] The effect of error on the validity of a contract is one of the most uncertain areas in our private law. This is the result of a tension between two fundamental principles. Firstly, a contract is constituted by the agreement of the parties to it. It is based on mutual consent. Secondly, however, one party is entitled to hold the other to what he has said, even if he did not mean it. "When all the external *indicia* of agreement are present the fact of agreement will, as a general rule, be assumed" (*Gloag on Contract*, 2nd ed. page 7). So long as a clear and enforceable bargain emerges, the subjective intention, or lack of consent of one party, is defeated by an objective interpretation of what was said or done. From time to time this is explained in terms of personal bar. The mistaken party is barred from relying upon his real intention.

[2] Nonetheless, there are circumstances when error on the part of one or both parties to a mutual onerous contract will bear upon its validity. As the case law has developed, the conventional view is that if one party can say no more than - "I did not mean that" - the objective approach will hold sway. If, however, some additional factor can be prayed in aid, the absence of real agreement may prevail; for example, if one party has caused the contract by misleading the other on an important matter. (Professor McBryde describes this as "error plus": *"The Law of Contract in Scotland"* 3rd ed. paragraph 15 - 23.) The present case is a good example of how difficult questions can arise when, on the face of it, a party has bound himself to unintended obligations. In particular, can the other party's knowledge of an uninduced error justify reduction of the apparent bargain, and, if so, what kind of error is sufficient for this purpose?

The pursuer's case

[3] Mr Wills made a claim in Aberdeen sheriff court against the defender for damages for an alleged failure to provide him with share options worth, he says, in excess of £3.5m. Discussions took place between the respective solicitors about ending the Scottish proceedings. Mr Wills decided to pursue the matter in the High Court in London. Pre-action letters were sent by English agents, and in due course a writ was served. The Scottish claim was resolved by way of a joint minute, signed on behalf of both parties, which stated that decree of absolvitor should be pronounced. Subsequently the sheriff pronounced such an order. The pursuer claims that the defender's agent knew that his solicitor was in error in agreeing to a form of settlement which would prevent the damages claim being prosecuted in London. He knew that the pursuer intended to pursue

the matter south of the border. The English action has been met with a plea to the effect of *res judicata*. A motion to strike out has been made, but stayed meantime pending the outcome of the current proceedings, in which the pursuer asks the court to set aside both the decree of the sheriff and the preceding joint minute.

[4] Mr Wills offers to prove that, through its agent, the defender "took advantage" of a known mistake on the part of Mr Wills' solicitor when he agreed to a form of settlement which, unlike dismissal, would involve a total abandonment of the claim. (Counsel for Mr Wills made no express concession that this was the effect of the sheriff court decree, but the debate before me proceeded upon that basis.)

Counsel's submissions

[5] The foundation of the pursuer's case is the decision of the First Division in *Steuart's Trustees* v *Hart* (1875) 3R 192. Land was sold at a price of £75. The price was fixed on the footing that the land was burdened with a feu-duty of £9 15s, the truth being that this was the sum applicable to the whole estate. The purchaser knew that the feu-duty was only 3s. The result was that the land was bought at a considerable under-value. Lord President Inglis said: "In short, the allegation is, that the sellers were acting under essential error, and that the pursuers knew that and took advantage of it." His Lordship expressed the view that this was a wrong for which the law would provide a remedy. Lord Deas said that the other party "is not fairly entitled to take advantage of such an error." Lord Ardmillan had a strong conviction that the justice of the case was with the pursuers, in that the other party knew that they were labouring under an "an excusable and essential error", yet entered into a transaction injurious to them. The court's interlocutor reduced the contract on the basis that the defender "took advantage" of the pursuers' essential error.

[6] On behalf of the defender, Mr Lake QC submitted that the *ratio* of *Steuart's Trustees* v *Hart* was overruled by the subsequent decision of the House of Lords in *Stewart* v *Kennedy* (1890) 17R (HL) 25. According to Mr Lake, to be effective, unilateral error must be induced by the other party. Mere knowledge of it is of no consequence. Mr Lake recognised that there could be reduction at common law when a mutual understanding was undermined by a slip or blunder in the formal expression of the parties' agreement. Counsel emphasised that there was no slip or blunder in that sense here. Throughout, both parties intended that decree of absolvitor would be pronounced. There was no error in the expression of the formal agreement. If it be the case that one party misunderstood the legal effect of such a decree, the other can enforce the agreement, even if he was aware of the mistaken belief. S*teuart's Trustees* is no longer good law. In any event the particular error here did not fall within the scope of that decision, in that it extended only to the consequences of, or to the value of the agreement, not to the agreement itself.

[7] In *Stewart* v *Kennedy* their Lordships in the House of Lords neither expressly disapprove of the earlier decision, nor even refer to it; but Mr Lake relied upon a decision of Lord Marnoch in *Spook Erection (Northern) Limited* v *Kaye* 1990 SLT 676. Lord Marnoch said that he was satisfied that the *ratio* of the decision in S*teuart's Trustees* "depended on a view and understanding as to the effect of error *in substantialibus* which 15 years later was disapproved by the House of Lords in the case of *Stewart* v *Kennedy*." If that is correct, the present pursuer's case is irrelevant and should be dismissed.

[8] For the pursuer, Mr Dunlop QC asked for a proof before answer. He relied upon the uncritical mention of *Steuart's Trustees* in a number of cases decided after *Stewart* v *Kennedy*, for example in *Anderson* v *Lambie* (cited earlier) and *Steel's Trustee* v *Bradley Homes Limited* 1972 SC 48. He made particular reference to the post *Spook Erection* discussion of the issue by Lord Cameron of Lochbroom in *Angus* v *Bryden* 1992 SLT 884. He adopted the discussion at paragraph 7.22 of the 13th edition of Gloag & Henderson as a correct statement of the law. The present case goes well beyond an error as to the value of the agreement - it relates to an essential aspect of the agreement itself. The purpose of the settlement was to facilitate the English proceedings, not to abandon the whole claim. There was no consensus as to the key outcome of the joint minute, namely a decree which meant that the pursuer lost the opportunity of seeking damages for the defender's alleged breach of contract. The error went "to the root of the contract." Reliance was placed on paragraph 686 of volume 15 of the *Stair Memorial Encyclopaedia*, including the reference to "error in transaction." Mr Dunlop drew a distinction between an error as to "what one is doing", and a mistaken belief

which relates to "why one is doing it." In the event of doubt as to which category applies in this case, it would be better to resolve this after evidence from those involved. Mr Dunlop accepted that there are cases where it can be difficult to draw the line. As to the general theory, he adopted the "error plus" approach, as explained by Professor McBryde (see above).

Discussion and decision

[9] The key issue focussed in the debate was - is *Steuart's Trustees* v *Hart* still good law? I am satisfied that the decision in *Stewart* v *Kennedy* did not overrule *Steuart's Trustees*, so I answer this question in the affirmative. The outcome in *Steuart's Trustees* depended upon the knowledge of one party that the other was in error. *Stewart* v *Kennedy* did not proceed upon the basis of an uninduced, but known error. Lord Herschell rejected any contention that a contract could be set aside simply because one party understood and intended it to be other than it really was. There was reference to an exception in respect of induced essential errors, but there is nothing to suggest that his Lordship intended to reject the reasoning of the Inner House in *Steuart's Trustees* v *Har*t. That case is not mentioned in any of the speeches. Lord Watson adopted a relatively expansive approach as to when an error as to the nature of a contract might be regarded as an error *in substantialibus* in terms of Professor Bell's classification. He rejected the proposition that the mere existence of such an error in the mind of one party allows the court to annul the contract.

"The result of admitting any other principle would be that no contract in writing could be obligatory if the parties honestly attached in their own minds different meanings to any mentioned stipulation" (page 30).

Lord Watson was of the opinion that

"the alleged error of the appellant is by itself insufficient to invalidate his consent, but it will be sufficient for that purpose if it can be shewn to have been induced by the representations of the respondent, or of anyone for whose conduct he is responsible" (page 30).

As a result, their Lordships allowed an issue to go to a jury as to whether the error was induced by the defender's representative.

[10] I attach importance to the words "by itself" in the above passage. This is consistent with principle. If nothing suggests otherwise, a contracting party is deemed to be agreeable to what he says or does. If I speak or act in such a way as to indicate to another that I am content to contract on the basis of X, and the other party proceeds on that reasonable assumption, I cannot thereafter say that my real intention was Y. It would be wholly unfair and destructive of the necessary certainty of contractual obligation, and of commerce in general, if apparent agreements could be challenged in that manner. But what is the position if it is proved that the person seeking to enforce a contract was aware that there was no true agreement on a key element? In such circumstances, and if matters remain entire, for example, no third party interests are involved, why should the law insist on the objective interpretation, thereby allowing one party to take advantage of the other's mistake? Gloag says (at page 7):

"If, however, the words or acts of one party are calculated to convey to a reasonable and neutral person the impression that he agreed to a proposal, and did convey that impression to the other party, agreement for all legal purposes, is established, irrespective of the possibility that the apparent was not the real intention" (emphasis added).

The underlined passage suggests that where the party seeking to enforce the contract is aware of the other's mistake as to the bargain, there will be no presumption that the parties were in agreement. This seems fair, in that he knew that there was no true meeting of minds. The discussion in *Chitty on Contracts,* 31st ed. at volume I para 5 -075 indicates that, in the law of England and Wales, a mistake as to the terms of a contract "if known to the other party", may affect its validity. Reference is made to *Hartog* v *Colin and Shields* [1939] 3 All ER 566. In *Bell* v *Lever Bros Ltd* [1932] AC 161, when Lord Aitken stressed that it is of "the paramount importance that contracts should be observed", this was in the express context of the parties "honestly"

complying with the essentials of the formation of contracts (p 227). It is of interest to note that the "Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference" provide that a contract can be avoided in respect of a mistake of fact or law existing in the mind of one party, if the other party "caused the contract to be concluded in mistake by leaving the mistaken party in error, contrary to good faith and fair dealing, when the other party knew or could reasonably be expected to have known of the mistake" (section II - 7.201(1)(b)).

[11] In the above discussion, I referred to a mistake concerning "a key element of the agreement." This is to distinguish another type of erroneous belief, namely one which provides a reason or motive for entering into a bargain. Such errors can co-exist with a full understanding and agreement on the part of everyone as to the nature, meaning and effect of the contract. In other words, despite the error, there was a true consensus as to the essential elements of the bargain. This distinction, though important, can be difficult to make. The present case may well be one where much can be said on both sides, and in particular as to whether the error, if proved, is, to use Mr Dunlop's preferred terminology, an "error in transaction" or an "error in motive".

[12] It is well established that bad, yet fully valid bargains can be made and enforced, and this despite the fact that one or both of the parties misunderstood the true state of affairs. The expert who spots a rare first edition for sale in a bookshop at a low price is an often quoted example. In such a case the seller's error has no impact on the validity of the contract. It relates to a collateral matter, namely the value of the item, not to the subject-matter, meaning or effect of the bargain. If both were ignorant as to the true value of the book, again that shared error has no effect. Professor McBryde has pointed out that often both parties will have, or must be deemed to have, understood the risks inherent in their transaction; see his contribution on the law of error in "A History of Private Law in Scotland", edited by Reid and Zimmerman, at pages 95/6. (He contrasts a case such as the purchase of a cabinet, which, unknown to the seller, contains a valuable jewel in a secret drawer.) In some respects, commerce thrives on uncertainties. It is no part of our law to undermine the validity of commercial agreements because risks taken have turned out badly for one party. It may well be possible to analyse some of the cases in terms of implied conditions, for example, as to acceptance of risk, warranties, etc.

[13] The question raised by Mr Lake in the present case is whether there can be circumstances when one party's knowledge of an error on the part of the other, prevents the enforcement of an apparently concluded bargain? This is not a straightforward matter. On the one side are issues of simple fairness or justice, not to mention the consensual basis of contractual obligations; on the other, the need to promote certainty and personal responsibility. The interests of third parties may require to be taken into account. In the present case one might ask, why should the pursuer escape the consequences of his solicitor's mistake? Surely his remedy is against his lawyer in negligence. On the other hand, is it right that the defender be allowed to escape a potential liability in damages, if its representative knew that this was never the intention of Mr Wills ' agent.

[14] For present purposes I require to proceed upon the basis that it will be proved that, at the time of the settlement of the Scottish proceedings, Mr Wills' solicitor did not appreciate that a decree of absolvitor would prevent pursuit of the shares claim in England - as opposed to clearing the way for such proceedings - and that it was understood by all involved that an action was to be raised in London. The debate also proceeded upon the assumption that the defender's solicitor laboured under no such error, but was aware of his counterpart's mistake, kept quiet about it, and completed the agreement, thereafter obtaining a court decree consistent with its terms. This is a different type of case from *Anderson* v *Lambie* 1954 SC(HL) 43, where both parties were under the same error as to the extent of the heritable subjects being disponed. It is also important to appreciate that there is no suggestion that the error was caused or induced by the defender or its agents: but nor is it a case of pure uninduced unilateral error - it is "error plus", in that the allegation is that the defender's agent knew and took advantage of the other's mistake.

[15] Reverting to Lord Marnoch's decision in *Spook Erection*, Mr Dunlop QC submitted that his Lordship failed to appreciate that *Stewart* v *Kennedy* was a case of pure error, involving no additional factor which

might justify reduction of the contract. Given that it raised a very different question, *Stewart* v *Kennedy* does not cast doubt on the earlier case.

[16] I now consider the Lord Ordinary's reasoning in *Spook Erection*. His Lordship observed that in *Stewart* v *Kennedy* the House of Lords departed from the notion that, of itself, error *in substantialibus* excludes the consensual foundation of contract. That left "no room for any fundamentalist doctrine such as that for which counsel for the defenders contended." As to *Steuart's Trustees* v *Hart*, Lord Marnoch said that the main issue in the Inner House was the competency of the Lord Ordinary "rewriting the contract" and the soundness of the defender's contention that restitution *in integrum* was impossible.

"Accordingly it is important to analyse with some care the reasoning of the Lord Ordinary, Lord Shand, on the more fundamental question as to the initial validity of the contract in question. In my opinion...it is quite clear that that reasoning is based on the belief that there was error *in substantialibus* as to the price and that that error would itself have been a sufficient basis for setting aside the missives." (page 678 I - J)

Lord Marnoch considered that Lord Shand placed reliance on the defender's knowledge of the mistake only in the context that a man will be estopped from relying on his subjective intention, as opposed to the apparent meaning of his words or conduct (page 678 k-l). His Lordship continued:

"As a separate matter, Lord Shand then goes on to hold that the defender in that case was unable to rely on his own subsequent actings and expenditure, saying that 'he was not entitled to demand and take implement of a contract which he knew had no real existence, because the parties had never agreed as to the price.'"

(Reference was then made to an alternative ground of Lord Shand's decision, namely fraud on the part of the defender's agent.)

[17] Lord Marnoch drew a dividing line between, on the one hand, the impact of error on the validity of a contract, and, on the other, the effect of estoppel or personal bar in preventing the party in error from relying upon it when challenging the agreement. For my part, I would be reluctant to make such a clear demarcation. It is the operation of personal bar - or, as it might otherwise be put, the objective approach to the formation of contract - which means that, despite the absence of true consensus, the apparent bargain can be enforced. If the objective approach is suspended by the other party's awareness of the mistake, this does not require any assumption as to an underlying pure doctrine of error of the kind discussed in *Stewart* v *Kennedy.* Lord Shand was entitled to require knowledge of an error in the substantials of the bargain as a necessary minimum to any challenge, but that is a different matter altogether from reliance on a purely consensual approach.

[18] Lord Marnoch continued:

"It is in the light of the above reasoning that one must interpret the bare statements in the Inner House by Lord President Inglis, Lord Deas, Lord Ardmillan and Lord Mure to the effect that the pursuers were, in the words of the Lord President (at page 200), 'entitled to reduce the sale on the ground of essential error known to the purchaser and taken advantage of by him'. In the result, I am satisfied that the ratio of this decision in both the Outer House and Inner House depended on a view and understanding as to the effect of error *in substantialibus* which 15 years later was disapproved by the House of Lords in the case of *Stewart* v *Kennedy*. In particular I do not consider that the references to the knowledge by the defender of the pursuers' error were intended to have any jurisprudential significance beyond negating a possible argument based on ′estoppel' or personal bar."

For myself, I am not persuaded that the knowledge of the other party's error played only a secondary role in the decision of Lord Shand in S*teuart's Trustees* v *Hart*. I would not separate or compartmentalise the issues of error and personal bar. In my opinion, and for the reasons explained earlier, in this area of the law these concepts are linked.

[19] For Lord Shand, the knowledge of the error was directly relevant to the invalidity of the purported agreement. His Note begins with a reference to the defender seeking "unfair advantage" from the pursuers' agent's "serious error", of which both the defender and his agent were aware. It was proved beyond question that the case was not one of mutual error. The defender thought that "it was no duty of his to enlighten them as to their mistake." For present purposes, it is important to note that, in such circumstances, Lord Shand considered that the sellers could have resisted implement of the missives of sale and purchase of the land in question. His comments as to the essential error and its effect were expressly couched in the context of the facts of the case before him. Importantly, he said:

"It is unnecessary to consider whether such an error would have been sufficient to render the contract void if the defender had been entirely in ignorance of the pursuers' real intention and state of mind" (page 197).

The reason why the defender could not rely on the objective construction of the pursuers' words and conduct was his own knowledge of the pursuers' mistake. None of this involved any reliance upon the pure consensual doctrine subsequently discredited in *Stewart* v *Kennedy*.

[20] In *Angus* v *Bryden* 1992 SLT 884, in *obiter* remarks, Lord Cameron of Lochbroom expressly differed from Lord Marnoch and offered the view that S*teuart's Trustees* v *Hart* is "still good law", and is binding on an Outer House judge. These observations have been supported by Professor Joe Thompson in an article entitled "Error Revised", 1992 SLT (News) 215. I acknowledge the assistance which I have received from it, and from chapter 15 in Professor McBryde's treatise on the law of contract. In his article, Professor Thompson said (page 219):

"Since consensus is tested objectively, a contract is formed in spite of the error, but because he knows the offeror's intentions, the offeree is not prejudiced by relying on the terms as stipulated in the offer, with the result that the offeror is not personally barred from relying on his own unilateral, uninduced error."

This is consistent with the Outer House and Inner House decisions in *Steuart's Trustees* v *Hart*. It is also in tune with the approach adopted in the leading English case of *Smith* v *Hughes* (1871) LR 6QB 597, in which Blackburn J said:

"If, whatever a man's real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other side's terms" (emphasis added).

[21] The view which I have reached is in line with the careful discussion of many of these issues provided by Lord Dunpark in *Steel's Trustee* (cited earlier). His Lordship disagreed with the proposition that *Steuart's Trustees* was wrongly decided. The case

"may reasonably be regarded as an application of the doctrine of personal bar; but in any event the fact that the purchaser's knowledge of the mistake formed the basis of the *ratio decidendi* takes it out of the 'pure' category" (page 57).

Lord Dunpark considered the elderly case of *Sword* v *Sinclair* (1771) M 14,241. As is often the case, the report in Morrison's Dictionary is not particularly enlightening, but Lord Dunpark "speculated" that the decision was based on one party knowingly taking advantage of the other's mistake. Subsequently Professor McBryde researched the Session Papers in the case and, as a result, has supported his Lordship's views (1997 JR 281). In *Parvaiz* v *Thresher Wines Acquistions Ltd* 2008 SC 151, Lord Brodie allowed a similar issue to go to proof (paragraph 20).

[22] For the above reasons, I reject the primary proposition presented by Mr Lake, namely that the ratio of *Steuart's Trustees* has been overruled. It may be that Gloag's concerns about *Steuart's Trustees* (pages 437/8) arose from an anxiety that the Inner House judgments might open the way for a known, though uninduced

error, on a collateral, but highly influential matter, to disturb the enforceability of a bargain, perhaps by analogy with the law on contracts induced by a misrepresentation of one party. Unfortunately, this area of the law is bedevilled by the frequent use of inexact terminology. Hence, in this opinion I have tried to avoid the phrase "essential error", which can be interpreted in a variety of senses, for example, as a mistaken understanding which causes a party to make a contract, or as one which goes to "the essentials" of the proposed bargain. Nothing in this opinion will prevent discussion at the proof as to whether an uninduced error of the former type, if known to the other side, can prevent enforcement of an agreement, though my provisional conclusion is that the current state of the authorities does not support that proposition (albeit something may depend on the specific context of the transaction).

Mr Lake's alternative argument

[23] Mr Lake's secondary submission was that the pursuer's case is nonetheless irrelevant, in that the solicitor's mistaken belief does not fall into the category of the kind of error which, if known, will allow reduction. Assuming that *Steuart's Trustees* is good law, it is not every error which, even if appreciated by the other party, will justify a challenge to a contract. In general terms, I regard that proposition as sound. The difficulty is in identifying on which side of the line any particular case falls. The point is discussed in Professor Thompson's article, again at page 219: "The doctrine of uninduced unilateral error - even if known to the other party - does not enable an offeror to escape from a bad bargain." The author discriminates between errors "going to the root of the contract" and errors "in intention or motive", the latter being operative only if material to the bargain and induced by the other party. Much could be said upon this topic, but I am of the view that, in the present case, this issue should be resolved after proof, when the full facts and circumstances have been explored in evidence. Then, to use the language of Stair (I.10, 13), the court will be better placed to judge whether Mr Wills' agent erred "in the substantials of what (was) done." There are plenty of decisions in the books where a judge or a jury has upheld a case based on a mistake as to the meaning or effect of an agreement, but much can depend on the full circumstances.

[24] In response to Mr Dunlop's submissions, Mr Lake submitted that the only issue properly arising in this case concerns the interpretation of what was agreed. He observed that Mr Dunlop had not suggested that the background circumstances indicate that the agreement on "absolvitor" should be construed as meaning that the English proceedings will be allowed to continue. According to Mr Lake, much would be required to rebut the well understood meaning of the term "absolvitor". At least at this stage, I am not persuaded that the only relevant issue in the case concerns the construction of a valid contract. However, again I consider it unnecessary and inappropriate to dwell on this submission until after proof and the full circumstances have been established.

[25] Mr Lake made various criticisms as to the detail of the pursuer's pleadings, but none of them has persuaded me that the pursuer should be refused a proof before answer. In response to one of Mr Lake's submissions in this regard, Mr Dunlop invited the court, if not dismissing the claim, to put the case out by order. This would allow him to give consideration to an amendment addressing the possibility that the parties reached a concluded agreement before the completion of the joint minute, in which event an additional conclusion for reduction might be required, though the factual averments would stand unrevised. I shall grant that request and also refuse Mr Lake's motion for dismissal of the action. My intention is that after the by order hearing, I will allow a proof before answer, with all pleas outstanding.