Privy Council Appeal No. 41 *of* 1955

Sheikh Brothers Limited - - - - - - - - *Appellant*

v.

Arnold Julius Ochsner and another - - - - - *Respondents*

FROM

THE COURT OF APPEAL FOR EASTERN AFRICA

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 14TH JANUARY, 1957

Present at the Hearing:

LORD OAKSEY

LORD COHEN

LORD KEITH OF AVONHOLM

MR. L. M. D. DE SILVA

[*Delivered by* LORD COHEN]

This appeal raises questions as to the effect of Sections 20 and 56 of the Indian Contract Act on a license agreement made between the appellant and the first respondent on the 9th December, 1950.

Sections 20 and 56 are in the following terms :—

" 20. Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement the agreement is void.

Explanation—An erroneous opinion as to the value of the thing which forms the subject matter of the agreement is not to be deemed a mistake as to a matter of fact.

Illustrations—

. . . . . .

56. An agreement to do an act impossible in itself is void.

A contract to do an act which after the contract is made, becomes impossible, or by reason of some event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

Where one person has promised to do something which he knew or, with reasonable diligence, might have known, and which the promisee did not know to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

Illustrations.

(*a*) A. agrees with B. to discover treasure by magic. The agreement is void.

. . . . . .

(*c*) A. contracts to marry B., being already married to C., and being forbidden by the law to which he is subject to practise polygamy.

A. must make compensation to B. for the loss caused to her by the non-performance of his promise."

. . . . . .

The Court of Appeal for Eastern Africa, affirming the decision of the Supreme Court of Kenya, held that the license agreement was entered into under a mutual mistake as to a matter of fact essential to the agreement and was accordingly void under Section 20 but that it was also void under Section 56 since the agreement contained an obligation to do an act impossible in itself. They held, however, that as the agreement was void under Section 20, the appellant could not recover compensation under the third paragraph of Section 56 although the conditions required by that paragraph to found a claim for compensation undoubtedly existed. It is from this decision that this appeal is brought.

By the license agreement, after reciting that the appellant was the lessee of an estate of about 10,000 acres of which 5,000 acres or thereabouts (therein and hereinafter referred to as the sisal area) were planted with mature sisal, and that upon the treaty for the license it had been agreed that by way of security for the fulfilment of his obligations under the license agreement the licensee would deposit with the appellant the sum of 50,000 shillings and that that sum had been duly deposited, it was amongst other things provided as follows:

By clause 1 the appellant granted the licensee a license to cut, decorticate, process and manufacture all sisal then or at any time thereafter growing upon the sisal area.

By clause 2 the duration of the license was fixed at five years from the 1st January, 1951, subject to determination as thereinafter mentioned.

Clause 3 contained a number of undertakings by the licensee. It is sufficient for the purpose of this judgment to state the following:—

"(A) that he will continuously and in a proper and efficient manner cut decorticate process and manufacture all mature sisal now or hereafter growing on the Mature Sisal Area:

(B) that he will deliver all sisal fibre and tow produced by him on the said premises to the Company or to such agents of the Company as it shall from time to time direct for sale:

(C) that he will as from the first day of April One thousand nine hundred and fifty-one manufacture and deliver sisal fibre in average minimum quantities of fifty tons per month: PROVIDED ALWAYS that for the purposes of this clause deliveries shall be calculated on the thirty-first day of December in each year to the intent that excess deliveries in any calendar month during such year shall be credited towards any shortfall in any calendar month during the same year:

. . . . . .

(E) that he will not cut any sisal on the said premises other than mature sisal which for the purpose of this clause shall mean sisal leaves which branch out from the top of the sisal pole at an angle of not less than forty-five degrees: "

Clause 4 contained the following undertaking by the appellant:—

"(A) that it will in respect of each delivery of sisal line fibre made to it or its duly authorised agent by the Licensee and certified by the Sisal Inspector as fit for export pay to the Licensee the sum of Shillings five hundred per ton such payment to be made on or before the expiration of seven days from the date of the consignment note in respect of such delivery: "

Clause 5 contained provisions as to the division of the proceeds of sale as between the appellant and the licensee. It is sufficient to say that subject to the deduction by the appellant of a sum equivalent to 100 shillings per ton as development charges and to certain provisos which their Lordships need not set out in detail the proceeds were to be divided as follows :—

"(i) in respect of sisal line fibre and sansivers fibre sixty per cent. to the Company and forty per cent. to the Licensee:

(ii) in respect of tow fifty per cent. to the Company and fifty per cent. to the Licensee:

(iii) in respect of flume tow twenty-five per cent. to the Company and seventy-five per cent. to the Licensee."

Clause 6 provides as follows :—

"If during any year of the said term ending the thirty-first day of December the Licensee's deliveries of line fibre shall fall below the aggregate of the average minimum monthly quantity hereinbefore provided for then the Company shall be entitled without prejudice to any other remedies it may have hereunder to be paid out of the moneys representing the Licensee's deposit a sum equivalent to the amount it would have received in the same year if the Licensee had cut and delivered the aggregate of the average minimum monthly quantities hereinbefore provided for PROVIDED that if any subsequent year of the said term ending the thirty-first day of December the Licensee's deliveries of line fibre shall exceed the aggregate of the average minimum monthly quantities hereinbefore provided for the Company shall make up the Licensee's deposit by refunding a sum equivalent to the price realised in respect of such excess but not exceeding the amount deducted therefrom in respect of the deficiency in any previous year's deliveries."

Clause 8 provided for the automatic determination of the license if the price of sisal fibre fell below £40 per ton.

Clause 9 provided for the suspension of the licensee's obligation to deliver minimum monthly quantities of sisal in certain events such as drought and fire.

Clause 11 so far as material is in the following terms:—

"Subject to the provisions of Clauses 9 and 10 hereof if the Licensee shall fail for a period of three consecutive calendar months to cut and deliver the average minimum monthly quantities of sisal provided for and by reason of such failure the loss sustained by the Company shall exceed the sum of Shillings One hundred thousand or . . . then it shall be lawful for the Company at any time thereafter to re-enter upon the said premises or any part thereof in the name of the whole and thereupon the licence hereby granted shall cease and determine but without prejudice to any right of action or remedy of the Company in respect of any antecedent breach by the Licensee of any of the agreements on his part herein contained."

Clause 12 is an arbitration clause.

In their Lordships' opinion this agreement provided for something of the nature of a joint adventure and was entered into on the basis that the sisal area was capable of producing sisal over the period of the agreement at the average rate of 50 tons per month.

Pursuant to a right reserved to him by clause 3 (N) of the license agreement the first respondent on or about the 1st May, 1951, assigned to the second respondent his rights and obligations under the license agreement with effect from the 1st January, 1951.

The cutting and manufacture of sisal under the license agreement was carried on by the respondents or one of them until the 31st January, 1952, when possession of the premises the subject of the license agreement was resumed by the appellant at the request of the second respondent without prejudice to the rights and remedies of the appellant under the license agreement.

On the 27th November, 1952, the appellant and respondents signed an agreement of submission of disputes between them to two arbitrators pursuant to clause 12 of the license agreement. The arbitrators were asked to decide as preliminary points whether the licence agreement was void either

(A) under Section 20 because of mutual mistake or

(B) under Section 56 because of impossibility.

It is clear from the pleadings that the mutual mistake alleged was that both parties believed contrary to the fact that the leaf potential of the sisal area would be sufficient to permit the manufacture and delivery of the minimum quantities of 50 tons per month throughout the term of the license. It is also clear that the impossibility alleged was that the leaf potential of the sisal area made it impossible to produce the said minimum quantities over the said term.

The arbitrators held that there was no mutual mistake since there was only an error of judgment as to the leaf potential and error of judgment is not the equivalent of mistake. They decided the issue of impossibility in favour of the respondents but they then went on to consider the application of the third paragraph of Section 56 and held that the first respondent had he exercised reasonable diligence before agreeing to the terms of the license might have known that it would be impossible to produce from the sisal area the stipulated minimum quantities of sisal and accordingly must pay compensation.

The respondents applied to the Supreme Court of Kenya to remit or set aside this interim award. The application came before de Lestang J. who held that the erroneous belief as to the leaf potential of the sisal area was a mistake of fact on a matter material to the agreement and remitted the application to the arbitrators to deal with on this footing. So directed, the arbitrators decided that the mistake was mutual. They adhered to their opinion that the agreement was void under Section 56 but in view of their decision under Section 20 they held that compensation was not payable under the third paragraph of that Section. The appellant then appealed to the Supreme Court for an order that the arbitrators' award be set aside or remitted, alleging that the mistake was not mutual and was not as to a matter of fact essential to the agreement and that in any event there was a case for compensation under the third paragraph of Section 56. The matter again came before de Lestang J. who dismissed the application with costs.

The appellants appealed to the Court of Appeal for Eastern Africa who, as their Lordships have already said, affirmed the decision of the Supreme Court.

Before their Lordships two points were argued on behalf of the appellant

(1) that the mistake was not as to a matter of fact *essential* to the agreement

(2) that even if the license was void under Section 20, Section 56 was also applicable and therefore on the finding of fact by the arbitrators that the appellant did not know but the respondents might with reasonable diligence have known of the impossibility, compensation was payable under the third paragraph of the Section.

Mr. Foot supported his argument on the first point by a reference to the judgment of Lord Atkin in *Bell* v. *Lever Bros.* [1932] A.C. 161. Mr. Foot said that the mistake relied on was a mistake as to quality and that such a mistake, to quote Lord Atkin at page 218, " will not affect assent unless it is the mistake of both parties, and is as to the existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be." He submitted that applying this citation assent was not affected in the case before your Lordships. He also relied on passages in Halsbury's Laws of England 2nd Ed. Vol. 23 at pp. 135, 6, where the learned author draws a distinction between a case of mutual mistake as to the existence of the subject matter or of some fact or facts forming an essential and integral element of the subject matter (see para. 189) and one where the contract is for the sale of the subject thereof absolutely and not with reference to any collateral circumstances (para. 190). Mr. Foot submitted that the facts in the present case were analogous to the latter case and not the former.

Their Lordships are unable to agree. Having regard to the nature of the contract which as their Lordships have already said seems to them to be a kind of joint adventure and to the provisions in particular of clauses

3 (*c*), 4 (*a*), 5, 6 and 11, their Lordships think that it was the very basis of the contract that the sisal area should be capable of producing an average of 50 tons a month throughout the term of the license. It follows that the mistake was as to a matter of fact essential to the agreement.

Their Lordships turn to the second point. The respondents did not argue that the facts did not establish an agreement to do an act impossible in itself so that it is unnecessary for their Lordships to consider the meaning of the phrase "an act impossible *in itself*." The point taken by the respondents was that the third paragraph of Section 56 applied only where an agreement otherwise valid was rendered void by impossibility of performance. Their Lordships agree with the Court of Appeal of Eastern Africa that this argument is well founded.

The structure of the Act is worthy of note. It is divided into chapters. Chapter II into which Section 20 falls is headed "Of Contracts, Voidable Contracts and Void Agreements." Section 10, the first section of the Chapter, provides that all agreements are contracts if they are made by the *free consent* of parties competent to contract for a lawful consideration and with a lawful object and are not hereby expressly declared void. Section 14 defines free consent and provides inter alia that consent is free when it is not caused by, inter alia, "5, mistake subject to the provisions of Section 20 . . ."

Mutual mistake within Section 20 having been found to exist at the date of the license agreement it necessarily follows that the license agreement is not a contract within Section 10. Neither can it be an agreement enforceable by law. Therefore quite apart from Section 56 it is a void agreement, see Section 2 (*c*).

True it falls within the language of the first paragraph of Section 56, but that section comes under Chapter IV which deals not with the formation of contracts but with performance and it seems to their Lordships reasonable to construe Section 56 as applying only to agreements which apart from questions of performance are enforeable agreements.

It was suggested that there might be repugnancy between Sections 20 and 56. The third paragraph of Section 56, it was submitted, clearly covered a case of mutual mistake where neither the promisor nor promisee knew of the impossibility but it was found that the promisor might with reasonable diligence have known of it. If in such a case compensation were not payable, the argument went on, there must be repugnancy between Sections 20 and 56 and therefore the latter section must prevail. (See Maxwell on the Interpretation of Statutes 10th Ed. page 162.)

Their Lordships have already given one reason for holding that no repugnancy exists, viz. that Section 56 only applies where there is, apart from any question of performance, an enforceable agreement. Another reason for rejecting this argument is to be found in the third paragraph itself. There are under that paragraph two possibilities (1) A. the promisor knows of impossibility, B. the promisee does not, then no question of mutual mistake can arise. (2) A. did not know, but with reasonable diligence ought to have known, of the impossibility. B. did not know of it, then, says Mr. Foot, there is mutual mistake. That is literally true but their Lordships agree with Jenkins J.A. that here also the words "or with reasonable diligence might have known" imply a set of circumstances in which the promisor is in a different position from the promisee. In other words the case is to be treated as being one of unilateral not mutual mistake.

For these reasons their Lordships will humbly advise Her Majesty to dismiss the appeal. The appellant must pay the costs.

(39912) Wt. 8069—3 90 1/57 D.L.

In the Privy Council

SHEIKH BROTHERS LIMITED

v.

ARNOLD JULIUS OCHSNER AND ANOTHER

DELIVERED BY LORD COHEN

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