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Public Policy in Contract Law

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ABSTRACT

Public Policy is not persistent. Public Policy denotes that what is good for the public and public Interest at large. Rather than protecting the parties to a contract as other contract defenses do, the defenses of illegality and violation of public policy seek to protect the public welfare and the integrity of the courts by refusing to enforce certain types of contracts. Contracts to engage in illegal or immoral conduct would not be enforced by the courts. Over the years the courts have developed the meaning of the term 'opposed to public policy. There are certain agreements which are against public policy and they are termed as illegal agreements.

I. INTRODUCTION

The concept of public policy exists in almost all legal systems. It is as old as governments. In the words of Robert Eyestone, public policy is the relationship of Government towards environment and it is implemented for the welfare of the society. Public policy consists of three distinct notions of public. The three notions are as follows;

1) Public interest: Public interest category views the private arrangement of citizens as equal to public arrangements and tries to strike a balance between the two.

2) Public security: Public security category aims to protect citizens from outside threats that might endanger their well-being.

3) Public morality: Public morality category tries to safeguard the identities of the individuals and maintains the value of societal life. The historical period of public policy can be divided in to four; Fourteenth Century, Eighteenth Century, Nineteenth Century and Twentieth Century. In the Fourteenth Century, the concept of public policy was not in existence but there was equity, natural law and reasons. Mere reasoning by the courts was based up on the natural law itself. In this period, the control is totally within the courts.

When coming to the Eighteenth Century, there was progress of trade in England. In such a situation, there was need to protect the social and economic interest of community and State. So, these factors became more relevant in approaches to public policy. Instead of using the

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term public policy, courts used the terms like public good, public mischief etc. The term public policy did not appear in the common law until Eighteenth Century. Prior to that, courts used a concept of *encounter commone ley*. It meant prejudicial to the community or against the benefits of the common wealth. According to Knight, a legal historian, *Dyer's* case[2] is said to be one of the oldest cases referring to *encounter commone ley*. This case reflects the traditional approach to public policy.

One of the earlier instances in which the Court employed the term public policy was Mitchel v Rynolds.[3] In this case, the defendant assigned his bake house in parish to the plaintiff for five years, upon a bond for 50 pounds.There was a condition in the bond that the bond would be void, if the defendant did not exercise his trade as a baker in parish for a period of five years or if he did so, he had to pay 50 pounds to the plaintiff within three days. But the defendant started his trade at another location in the parish and failed to pay the sum to the plaintiff. The plaintiff sued on the bond. The defendant argued that the contract was restraint of trade and therefore void. It was held that the restraint was reasonable and was based on a valid consideration. Here, it was a particular restraint which was dealing with specific person and place and valid for valid consideration. The Court stated that, obtaining sole exercise of a trade in England was a monopoly and therefore against the policy of law.[4] The doctrine of public policy later extended to other areas such as, rule against perpetuities, sales of offices, marriage contracts, wagering, contracts with alien enemies, and restraint of trade.[5]

In 1750, Lord Hardwicke laid down one of the first definitions of public policy. To him, contracts against public policy were of no effect, not because either of the parties had been deceived, but because they were a general mischief to the public. He transformed the concept of public policy from against the community to against *res publica*, that is, public affairs. In other words, he politicized the concept of public policy. This could be marked as the starting point of modern approach to the doctrine of public policy. interpreted the doctrine ex dolo malo non oritur action[6] means that courts should not lend their resources to aid a man whose cause

[2]Dyer's case (1414) 2 Hen. V,fol.5,pl.26. In this case John dyer promised the plaintiff that he does not exercise his trade in the same town for six months. But he started his business against his promise. The plaintiff sued against the dyer. The court held that, there was a restraint of trade from the part of the defendant and it was against the benefits of the society.

[3] 24 E R 347 (1711) (Q.B)

[4] Knight, *supra* n 2.

[5] www. Revolvy.com

[6] *Ex dolo malo non oritur actio* is a Latin term which means 'no right of action can have its origin in fraud'. No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act. The maxim lies at the foundation of a general rule of public policy, the rule that the courts will not sustain an action which arises out of the moral turpitude of the plaintiff or out of his violation of a general law enacted to carry into effect the public policy of the State or nation.

of action is based on illegal or immoral ground. To Lord Mansfield's interpretation, this also laid down a foundation for the modern doctrine of public policy. It may be noted that Eighteenth Century reshaped the doctrine of public policy. Later, the modern approach to public policy entailed political considerations.

In Nineteenth Century, the politicization of the doctrine of public policy provoked the resistance of common law. The focus slightly widened apart from the socio-economic factors. Public welfare and public interest were taken in to consideration. The shift from *encounter commone ley* to *res publica* encouraged two main reactions. Firstly, it was thought that the sole authority to decide the policies related to the public was the legislative body.

For instance, in Richardson v Mellish,[7] Justice Burrough called public policy as a very unruly horse and when you get astride of it, you never know where it will carry you. He also said that public policy was vested in the discretion of legislature and not in judiciary. By this time, a political color was given to public policy which was more and more vague. In Egerton v. Brownlow[8], similar doubts were arisen. This case involved a contingent interest in an estate in the form of condition subsequent. Here, nine out of eleven judges said that legislature should determine public good and public policy instead of courts and parties. While Lord Alderson opposed the power of judiciary, Lord Parke took a view in favour of judiciary. Finally, House of Lords held that the judiciary has the power to decide public policy.

The conflicting views of the judges on public policy were shaped in this case for the first time. One view is that, public policy is only a guide for ascertaining the object and purpose of statutes. Under the other view, it is an abstract legal standard independent of time and circumstances. In short, there was no need for judicially crafted public policy.

Secondly, the other group suggested that courts might concentrate on the State's interest in cases involving a public policy exception. In Cooke v Turner[9], the Court held that while deciding the enforceability of a will, a condition could be held to be void on the ground of public policy where it had restrained a party from doing some act where the State had or might have an interest. Lord Watson's opinion in Nordenfeldt v Maxim Nordenfeldt Guns and Ammunition Co Ltd[10] serves as another example. Here, the House of Lords held that, restraint of trade was reasonable in the interests of the parties. In this case, Nordenfelt, a manufacturer specializing in armaments, had sold his business to Hiram Stevens Maxim. Nordenfelt agreed

[7] 130 E R 294 (1824).
[8] [1853] 4 HLC 484
[9] 1843 C153
[10] [1894] A C 534

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that he would not make guns or ammunition anywhere in the world, and would not compete with Maxim in any way for a period of 25 years. Later he started the same business. Maxim sued against the Nordenfelt. Here, the unreasonable restraint was severable, and the Court enforced the amended agreement that Nordenfelt for the next 25 years, would not make guns or ammunition anywhere in the world, thus permitting him to trade in those very items in direct competition with maxim.

Thus, the series of decisions based upon grounds of public policy, however eminent the judges by whom they were delivered, cannot possess the same binding authority as decisions which deal with and formulate principles which are purely legal. The course of policy pursued by any country in relation to, and for promoting the interests of its commerce must, as time advances and as its commerce thrives, undergo change and development from various causes which are altogether independent of the action of its courts. The difference between the two approaches is that the former one endorses a more passive role in the assessment of public

policy exception, whereas the second approach encourages the courts to actively assess and enforce the interests of the state in this context. Freedom of contract rests on the principle that it is in the interest of the public to grant broad powers to individuals to facilitate their transactions. It also implies that parties of full age and competent understanding must have the greatest freedom of contracting. Consequently, courts will generally enforce them without passing on their substance. However, they occasionally consider that certain types of contracts should not be enforced on grounds of public policy. The refusal of their assistance may indeed be an appropriate sanction to discourage undesirable conduct in the society.

Public policy in English and American law has been described as a will-o-the-wisp of the law which varies and changes with the interests, habits, and needs[11]. The notion has indeed been considered as vague and elusive amongst the courts. In a common law system, courts have mainly relied on their own perception of public interest to refuse the enforcement of some contracts. In this regard, they have endeavoured to recognize that changes in social conditions may call for a changed concept of what the interest of the public demands. However, with the growth of an elected and democratic legislative body, two questions are raised in relation to the judicial law making. The first is whether public policy is the instrument of the judiciary or legislature. The second question concerns the factors that courts must consider in determining the non-enforcement of an agreement.

The vagueness of the term public policy and its application by the doctrine has further given

[11] 17A *Am. Jur*., Contracts III C Refs, 2nd, 1964, Section 239, database updated May 2014 (Westlaw US).

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rise to a variety of contracts considered as unenforceable. Rules based on public policy vary over the institution that they aim to protect. For instance, policies related to restraint of trade are more likely to change than these concerning the primary morality, such a contract in marriage. Although, the general rule is the non-enforcement of a contract injurious to interest of the society, courts adopt in some cases a severe attitude and refuse to assist a person implicated in the illegality in any way whatsoever. In others, public policy does require that such a person should not be so completely denied a remedy.

II. AGREEMENTS WHICH ARE CONTRARY TO PUBLIC POLICY

Public policy is the "policy of the law". The vagueness of the term public policy has given rise to several contracts which are deemed contrary to public policy. An agreement which is opposed to public policy cannot be enforced by either of the parties to it.[12] The question as to whether an agreement is opposed to public policy or not is to be decided on general principles only and not by considering the terms of any particular contract. Contracts which are against public policy are declared as void by status. These contracts may be classified into categories called heads of public policy.

1. Contracts for Trading with an Enemy

All contracts made with an alien enemy are illegal unless made with the permission of the government. An alien enemy is a person who owes allegiance to a government at war. Such agreements are illegal on the ground of public policy because either the further performance of the contract would involve intercourse with the enemy, or its continued existence would confer upon the enemy an immediate or future benefit. Thus, it is unlawful and is void. However, if a contract is made during peace times and later on war breaks out, one of the two things may result, either the contract is suspended, or it stands dissolved depending upon the intention of the parties to the contract[13].

2. Traffic in Public Offices

Agreements entered in to for using corrupt influence in procuring government jobs, titles or honors are unlawful and therefore unenforceable. Because, if such agreements are valid, corruption will increase and lead to inefficiency in public services.

3. Stifling Prosecution

Stifling implies abuse of law. The law does not permit a person to make money out of a crime.

[12] Lawaree Valentin: *public policy in English and American law, 2014, pp.33.*
[13] *Ibid*

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An agreement in which one party agrees to drop criminal proceedings pending in a court in consideration of some amount of money is unlawful. Therefore, such an agreement cannot be enforced except where the crime is compoundable. However, if a compromise agreement is made before any complaint is filed, it would not amount to stifling prosecution even if it is implemented after the filing of a complaint which is then withdrawn.

4. Agreements in Restraint of Trade

Courts do not allow any tendency to impose restrictions upon the liberty of an individual to carry on any business, profession, or trade. In England, originally, all agreements in restraint of trade were void. But now, the rule is that though total restraint will be bad, reasonable restraint will be enforceable. In Nordenfelt vs. Maxim Nordenfelt, the House of Lords held that "the real test for determining the validity of agreements in restraint of trade was, whether the restrain public and not more onerous than necessary for the protection of the party imposing the restraint". A restraint of trade is a contractual term that is often included in an employment, a sale of a going concern, a partnership, and a franchise agreement. In the matter of Petrofina (Great Britain) Ltd v. Martin and another[14] Lord Diplock defined a restraint of trade as 'a contract in restraint of trade is one in which a party (covenantor) agrees with any other party (covenantee) to restrict his liberty in the future to carry on trade with other persons not parties to the contract, in such manner he chooses'.

Restraint of trade agreements are solely regulated by common law principles. At common law, a contract is illegal and unenforceable, if it is contrary to good morals or public policy. Restraint of trade agreements are valid and enforceable in Indian law unless they impose an unreasonable restriction on a person's freedom to trade. In this instance, they will probably be held to be against public policy and therefore illegal and unenforceable. Section 27 of the Indian contract Act 1872 says that, "every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void". Thus, in India, all agreements in restraint of trade, whether general or partial, qualified, or unqualified, are void.

There are some exceptions are available to the above rule that a restraint of trade is void:

- **Sale of goodwill**

The seller of the goodwill of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer or any one deriving title to

[14] 1966) Ch 146 at page 180.

the goodwill from him carries on a like business, provided that such limits are reasonable.

- **Partner's agreement**

A partner shall not carry on any business other than that of the firm in the same trade while he is a partner. An outgoing may agree with other partner not to carry on similar business that of the firm in the local limits or with in specific time. Similarly partners on dissolution of partnership firm may agree that some or all of them will not carry similar business within local limits or within specific time. Here also it is court that will decide that what the local limit would be and if it is reasonable.

- **Service agreements**

An agreement of service by which a person binds himself during the term of the agreement not to take service with anyone else or directly or indirectly take part in or promote or aid any business in direct competition with that of his employer is valid.

III. AGREEMENT IN RESTRAINT OF MARRIAGE

If an agreement which creates any restriction on marriage will be unenforceable. One person cannot restrict the other from getting married. Under English Law, agreements which restrain marriage are discouraged as they are injurious to the increase in population and the moral of the Citizens. In Lowe vs. Peerless[15], an agreement formed between the parties and according to the agreement one party should marry the other party only and vice versa. If any of them breaches the agreement, a compensation of $ 2000/- is to be paid. The court held this contract is void because it unduly restricts or hampers the freedom to marry. Thus, this contract is opposed to public policy. In another case, Hartley v. Rice[16], it was held that a bet between two men that one of them would not marry within a specified time was void as it gave one of the parties a pecuniary interest in the man's celibacy.

IV. AGREEMENT IN RESTRAINT OF PARENTAL RIGHTS

The father and mother are the natural guardians of a minor child. The right of guardianship cannot be bartered away by any agreement. Thus, 6an agreement which is inconsistent with the duties arising out of such guardianship is void as being opposed to public policy. In the case in re baby M, there was restraint of parental right by restraining the mother from the sole custody of the child.

[15] (1768) 4 Burr.2225
[16] 537 A.2d 1227

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V. AGREEMENTS IN RESTRAINT OF LEGAL PROCEEDINGS

Two kinds of agreements are dealt with under this head. They are:

1) Agreements restricting enforcement of rights

2) Agreements curtailing period of limitation

- **Agreements restricting enforcement of rights**

These are the agreements which prohibits wholly or partly any party to the agreement to enforce his rights in respect of any contract is void to that extent.

- **Agreements curtailing period of limitation**

If an agreement curtails the period of limitation which is prescribed by the law of limitation is void. This is so because its object is to defeat the provisions of law.

VI. AGREEMENTS TO COMMIT A CRIME

If in an agreement, the consideration is committing a crime, the agreement is opposed to public policy and is void. Similarly, an agreement to indemnify a person against consequences of his criminal act is unenfo**r**ceable being opposed to public policy.

VII. AGREEMENTS TENDING TO CREATE MONOPOLIES

Monopoly is a kind of restriction which preventing a person from doing a business. Agreements tending to create monopolies are against public policy and hence are void.

VIII. AGREEMENTS TO DEFRAUD CREDITORS

An agreement which is made with an intention to defraud the creditors or revenue authorities is not enforceable as it is opposed to public policy.

IX. AGREEMENTS CREATING INTEREST AGAINST DUTIES

If an agreement is entered in to by a person whereby, he is bound to do something which is against his public duty, the agreement is void on the ground of public policy. For e g; an agreement by a government servant for the purchase of land situated within his circle is illegal as opposed to public policy.

X. AGREEMENTS RESTRICTING PERSONAL LIBERTY

Agreements restricting personal liberty of the parties to it are void as being opposed to public policy because, nobody have the right to deprive a person from his personal liberty.

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XI. MAINTENANCE AND CHAMBERTY

Maintenance and chamberty agreements are against public policy and hence void. Maintenance agreements are those agreements whereby a person promises to maintain a suit in which he has no interest. Chamberty agreement is one whereby a person agrees to share the results of litigation. The difference between maintenance and chamberty agreements lies in their object. The object of maintenance agreement is to encourage or foment litigation, whereas the same in chamberty agreement is sharing the proceeds of litigation. In England, both agreements are illegal and unenforceable. In India, agreements which are made for the purpose of gambling and for injuring or oppressing others will not be enforced.

XII. MARRIAGE BROKERAGE AGREEMENTS

It is an agreement in which, one or other parties to it or third parties receive certain money in consideration of marriage. Such agreements being opposed to public policy and void. Similarly, an agreement to pay money to the parent or guardian of a minor in consideration of his or her acceptance to give the minor in marriage is void. Marriage brokerage contracts are defined as contracts to pay a third person for negotiating, procuring or bringing about a marriage. Such contracts have been condemned and declared unenforceable in American jurisprudence without exception or equivocation.

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