

Hart v O'Connor

[1985] AC 1000

Chapter 5 (page 238)

Relevant facts

When John O'Connor died in the 1950s he left his estate, including his farm, to his 9 children. The distribution of the estate was postponed to allow John O'Connor's eldest son Jack O'Connor and two of his brothers – Joseph and Dennis – to continue living on the farm. Jack O'Connor was the trustee of the estate.

By 1977 Jack O'Connor and his brothers were all in their 70s and 80s. The sale of the farm was initiated by the solicitor for the O'Connor estate and members of the O'Connor family due to concerns about the ability of Jack O'Connor and his brothers to continue farming the land.

On 1 September 1977 Thomas Hart signed an Agreement to purchase the farm from Jack O'Connor as trustee of the estate. The sale price was based on a valuation of the property obtained by the O'Connor estate's solicitors. Hart purchased the farm and subsequently made improvements to it.

In March 1981, Joseph O'Connor and his sons Francis and Paul O'Connor were appointed by the court as trustees in place of Jack. The new trustees sought to have the Agreement set aside and the farm returned to the estate on the basis that Jack was of unsound mind when he signed the Agreement.

On appeal, the New Zealand Court of Appeal set aside the Agreement and ordered that the O'Connors pay Hart compensation for the improvements he had made to the farm. Hart appealed the decisions of the New Zealand Court of Appeal in relation to both the setting aside of the Agreement and the amount of compensation to the Privy Council.

Legal issue

It was agreed by the parties that (1) Jack O'Connor was not of sufficient mental capacity to enable him to enter into the Agreement and (2) this lack of capacity was not known to Hart and was not something that should reasonably have been known to him. The key issue was therefore whether the contract was enforceable in circumstances where Hart had not known, and could not reasonably have known, that Jack O'Connor lacked capacity.

Decision

On 22 May 1985, the Privy Council decided in favour of Hart. Their Lordships unanimously decided that a contract made by a party of unsound mind whose affliction was not apparent and whose consequent incapacity was not known to the other party

should be judged by the same standards as a contract made by a person of sound mind.

According to Lord Brightman (with whom the other Lords agreed):

... in the opinion of their Lordships, the validity of a contract entered into by a lunatic who is ostensibly sane is to be judged by the same standards as a contract by a person of sound mind, and is not voidable by the lunatic or his representatives by reason of 'unfairness' unless such unfairness amounts to equitable fraud which would have enabled the complaining party to avoid the contract even if he had been sane.

As there was no unconscionable conduct, equitable fraud, victimisation, taking of advantage, overreaching or other unconscionable action by Hart which would have justified the intervention of equity, the Agreement could not be rescinded for incapacity and unfairness.

In rejecting an earlier decision of the New Zealand Supreme Court, Lord Brightman said:

In the opinion of their Lordships, to accept the proposition enunciated in Archer v Cutler that a contract with a person ostensibly sane but actually of unsound mind can be set aside because it is 'unfair' to the person of unsound mind in the sense of contractual imbalance is unsupported by authority, is illogical and would distinguish the law of New Zealand from the law of Australia, as exemplified in McLaughlin's case and Tremills's case, for no good reason, as well as from the law of England from which the law of Australia and New Zealand and other 'common law' countries has stemmed.

The Privy Council also noted that if a person lacking mental capacity subsequently regains capacity (even temporarily) they may ratify a contract entered into when insane.

Significance

This decision is authority for the proposition that a contract with a party who lacks capacity will still be enforceable if the other contracting party did not know, and could not reasonably have known, of the lack of capacity.