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THE ABROGATION OF THE RULE AGAINST RECOVERY IN MISTAKE OF LAW:

Kleinwort Benson Ltd v *Lincoln City Council*

PERHAPS the most maligned rule affecting restitution, the bar against recovery for mistake of law, established in *Bilbie* v *Lumley,*[1] has been under increasing attack throughout the Commonwealth. In New Zealand, the rule has been abrogated by statute: Judicature Amendment Act 1958, section 94(A)(1). Abrogation has been achieved judicially in Canada,[2] Australia,[3] South Africa,[4] and Scotland.[5] In England though, in the light of statements such as that of Lord Keith that the rule was too strongly entrenched to be removed by the courts,[6] it seemed that change would have to come by way of statute. The matter was the subject of a Law Commission Report,[7] which contained a draft bill abrogating the rule, and introducing some limits on a claim brought on it. But the House of Lords in *Kleinwort Benson Ltd* v *Lincoln City Council*[8] has pre-empted any legislative change.

Kleinwort Benson[9] arose out of the morass of disputes about swap contracts entered into *ultra vires* by local authorities. Similar disputes have already thrown up a number of important cases in restitution: for example *Westdeutsche*

1 (1802) 2 East 469.
2 *Air Canada* v *British Columbia* (1989) 59 DLR (4th) 161.
3 *David Securities Pty Ltd* v *Commonwealth Bank of Australia* (1992) 175 CLR 353.
4 *Willis Faber Enthoven Pty Ltd* v *Receiver of Revenue* 1992 (4) SA 202(A).
5 *Morgan Guaranty Trust Co of NY* v *Lothian Regional Council* 1995 SLR 299.
6 [1993] AC 70, 154. Despite criticisms of the rule in the academic literature, the rule was approved in Singapore as recently as 1997: *Minah L Mande* v *John Edward Schneider* DCA 43 of 1997 following *Borneo Motors (S) Pte Ltd* v *William Jacks & Co (S) Pte Ltd* [1992] SLR 881.
7 *Restitution: Mistakes of Law and Ultra Vires Public Authority Receipts and Payments*, Law Com No 227 (1994).
8 [1998] 3 WLR 1095; hereafter *Kleinwort Benson*.
9 *Ibid.*

Landesbank Girozentrale v *Islington London BC*.[10] In the present case, Kleinwort Benson sought recovery of money paid to a number of local councils under contracts entered into at a time when the general view was that these contracts were within the powers of the local authorities. After completion of these swaps however, the House of Lords in *Hazell* v *Hammersmith and Fulham London BC*[11] held that such contracts were *ultra vires* the powers conferred on local authorities under the relevant legislation. Although a number of similar claims were founded upon failure of consideration, this avenue was closed off to Kleinwort Benson in the present case as its transactions with the local authorities had been completed, and the six year time bar had passed on some portions of the payments.[12] The only available ground of recovery was mistaken payment, on which time did not run until after the mistake was discovered.[13] Such mistake as was made had to be one of law, rather than fact. Before the High Court the matter was disposed of quickly; *Bilbie* v *Lumley*[14] has been followed by the Court of Appeal[15] and the judge was bound. The judge certified under section 2 of the Administration of Justice Act 1969 that there was a point of law of general public importance; a leap frog appeal was instituted. Thus the matter came before the House of Lords.

As it was, the local authorities did not attempt to maintain the rule; rather they argued for a reformulation. The mistake of law made here was not one that was apparent at the time of the making of the contracts as *Hazell* v *Hammersmith and Fulham London BC*[16] had subsequently clarified the law. Therefore, the local authorities in resisting the claim argued that the mistake of law rule should be reformulated such that payments made on a settled understanding of the law could not be recovered.[17]

The House of Lords unanimously held that payments made under a mistake of law can be recovered. However, there was a three to two split on whether payments made under a law that was changed could be regarded as payments made under a mistake of law. The majority – Lords Goff, Hoffmann and

[10] [1996] 2 WLR 802.
[11] [1992] 2 AC 1.
[12] The dispute was really concerned with amounts after the time limit had passed. The Local Authorities had paid up the amounts within the six year period: see 1107.
[13] Section 32(1) of the Limitation Act 1980.
[14] *Supra*, note 1.
[15] For example, *Holt* v *Markham* [1923] 1 KB 504.
[16] *Supra*, note 11.
[17] Possibly inspired by the Law Commission report, *supra*, note 7 or the New Zealand Statute, text accompanying note 1. See Lord Goff's judgment, at 1116F.

Hope – thought they could.[18] Additionally, Lords Goff and Hope were also of the view that it was not a defence that the payment was made under a settled understanding of the law.[19] Thus the bank could recover the money paid over.

On other issues the House was generally unanimous or in general agreement: that judges do not merely declare the law;[20] that honest receipt was not a defence,[21] change of position may be relied upon,[22] and that section 32(1)(c) of the Limitation Act applied such that time did not run until discovery of the mistake.[23] Professor Peter Birks' suggestion that in some cases the mistake would be spent was also rejected.[24]

This comment will examine briefly the main points thrown up by the case.

The Abrogation of the Mistake of Law Bar

The rule against recovery under a mistake of law has been greatly criticised on a number of grounds:[25] that it arose out of a misapplication of the maxim *ignorantia juris non excusat*; it engendered numerous exceptions; and it had no place once an action in unjust enrichment was recognised. None of their Lordships were minded to maintain the existence of the rule against recovery of payments made under a mistake of law. Given the weight of cases and commentary against the rule, it would be surprising if courts in Singapore declined to follow suit.[26]

In the face of such unanimity, it may be time for a bit of revisionism though. Whatever its defects, the rule was a certain one, albeit subject to

[18] But as pointed out by Lord Browne-Wilkinson, Kleinwort Benson did not argue that there would be a mistaken payment if it was made on the basis of a Court of Appeal decision that was subsequently overruled: at 1104A.

[19] At 1122G, 1152. Lord Hoffmann appeared to consider that it was a possible limit (and not a defence) but that it was up to Parliament to introduce it: 1139H.

[20] 1100D, 1118B, 1132H, 1148E; not discussed by Lord Hoffmann.

[21] 1125A. 1151C.

[22] 1124G, 1133H, 1149H.

[23] 1101E, 1128F, 1136E, 1154-1155. Lord Hoffmann did not take issue with this.

[24] 1127A, 1154A. The proposition was suggested in Birks, "No Consideration: Restitution after Void Contracts" (1993) 23 UWALR 195, footnote 137. The proposition was criticised in Burrows, "Swaps and the Friction between Common Law and Equity" [1995] RLR 15.

[25] Lord Goff 1111 to 1116; Lord Hope1143 to 1145; Burrows, *The Law of Restitution* (1993) at 109-120; Goff and Jones, *The Law of Restitution* (4th ed) Chp 4; Birks, *An Introduction to the Law of Restitution* (1989, rev ed) at 164-167.

[26] The Court of Appeal in Singapore has stated, as recently as 1992 that recovery could not be made for mistake of law, *Borneo Motors (S) Pte Ltd* v *William Jacks & Co (S) Pte Ltd* and this was followed in *Minah L Mande* v *John Edward Schneider, supra*, note 6. But the point has not been really put in contention.

numerous exceptions developed by the courts in order to escape its operation. It also threw the risk of misapprehension of the law upon the payer. The removal of the bar leaves the risk on the payee, save where he has changed his position, or is able to rely some other defence. Whether the risk should be on the payee or the payer is a finely balanced point; logic does not dictate that it ought to be one or the other. In the light of this, it could be entirely appropriate to leave the rule as it is.

Another point that could be made against abrogation is a practical one. The advantage is now with the payer while in the past, it was with the payee; the claim is now front-loaded, in the sense that the defendant has to raise an available defence. It may be questionable whether this is appropriate: leaving it to the defendant to rely on a defence raises more legal transaction costs, and creates greater uncertainty; though a defendant may ultimately be vindicated, he is still subject to the danger of a claim being made out and must incur expense in defending, not all of which may be recoverable from a losing plaintiff.

The Effect of Judicial Changes of the Law

In abrogating the rule against recovery for mistake of law, the House of Lords had to consider the difficult question whether a change in the law means that a past payment on the basis of the law before the change can be said to be a mistaken one.[27] Although the abrogation of the rule against recovery in mistake of law was unanimously supported, the effect of such a change caused disagreement among the Law Lords. It was generally accepted by their Lordships that the traditional Blackstonian view of judges only declaring the law and not changing it, was a fiction.[28] Nonetheless, their Lordships acknowledged the retrospective effect of judicial pronouncements: a judicial decision determined the law not only between the parties to the action, but also in respect of past transactions that had not come to court. The issue then was whether such retrospectivity extended to making a payment before such a change one made mistakenly.

[27] The issue did not arise in other jurisdictions as the mistakes in those cases arose out of misconstructions of statute, and the point was not in any event taken.

[28] Lord Hope however, noted that while some decisions did effect changes in the law, others were merely declaratory: 1148. But Lord Hope did not elaborate on what this meant. In so far as some judicial statements merely repeat or re-assert that laid down in earlier cases or in statute, it may be said that these are merely declaratory. But the concern here is not with cases that do not affect the current law. The judicial statements that matter are those that do effect changes.

The majority thought that it did. In Lord Goff's view, given that judicial decisions were inevitably retrospective, a payment made in the past on the basis of a rule of law that is changed is one made on a mistaken supposition of the law, and is therefore a mistake of law. Lords Hoffmann and Hope were also of the same mind. Lord Hoffmann noted that otherwise, a payer would be left in the anomalous situation of not being able to recover although the obligation which required him to do so was later found to be invalid. His Lordship was further of the view that such an effect would arise regardless whether the change was effected by judicial decision or by statute. In contrast, Lords Goff and Hope would seem to regard only judicial decisions as having this effect; statutory changes would have consequences according to the construction of the statutes. Additionally, Lord Goff would also exclude from consideration recovery of payments of taxes, which are different from payments made under private transactions, in that exclusion of recovery may have justifiable public policy grounds. The minority judges, Lords Browne-Wilkinson and Lloyd accepted the retrospective nature of judicial decisions, but thought that this could not alter the fact that a person making a payment, because of a rule of law that is subsequently altered was not labouring under a misapprehension at that time.

The difference between the minority and the majority thus centered on whether the retrospective nature of judicial change meant that in the situation before them, the payer was to be taken to have been mistaken about the law. It is submitted, with respect, that the minority was correct. A mistake should only be operative where it affects the voluntariness or intention to pay. The involuntariness of the payment is reason enough for recovery to be allowed; the conduct of the defendant and his state of mind is immaterial save as a disqualification of any defence that might otherwise be available.[29] Such involuntariness can only be measured at the time of payment. What happens thereafter cannot alter the quality of voluntariness.

A mistake of law thus only operates where at the time of the payment there is misapprehension as to the actual state of the law at that time. As noted by Lords Browne-Wilkinson and Lloyd, the retrospectivity of common law decisions does not, and cannot, affect this at all.[30] Judicial decisions are retrospective only in the sense that they affect transactions which occurred in the past, before the decisions, but which have not as yet been brought to court. The retrospectivity of judicial decisions does not, and cannot, change the fact that at the time in the past, the transaction was valid. The majority,

[29] But *cf* Lord Hoffmann, 1137H.
[30] 1100H, 1135H.

with respect, erred where they proceeded on the assumption that retrospectivity changed the state of the law in the past and altered the quality of the payor's voluntariness.

This error made by the majority is further apparent when the basis of such retrospectivity is considered. Retrospectivity is necessary in order to treat similar cases alike. It is denied in respect of decided cases as a contrary public policy requirement of finality of judicial decisions takes precedence. But in other cases, where the matters have not been brought to court, the need for equal treatment dictates that they be treated in the same way as the latest decided case. It may be questioned whether this should be so in all situations. There may be a strong argument for prospective over-ruling in some situations. Indeed had it been applied in *Hazell* v *Hammersmith and Fulham London BC*[31] the entire swaps saga could have been avoided.[32] It is disappointing that Lord Goff in particular has denied the operation of this doctrine.[33] But whatever the case may be, it is at least clear that the need for equal treatment does not make it necessary to treat payments made in the past in the same way as payments made now under the same supposition.

Lord Hoffmann thought that not applying retrospectivity in its full rigour would mean that a payee under what is now a void transaction would not be able to recover.[34] With respect, and as noted by Lord Lloyd, that misses the point.[35] If a transaction is void, and on-going, recovery can probably be made on the basis of failure of consideration. The inability to recover in mistake flows simply and necessarily from the nature of the doctrine.

It may be that the type of mistake of law under consideration is better regarded as a misprediction by lawyers and commentators of what how the law will be determined by the highest court, in this case, the House of Lords. Mispredictions are normally not operative mistakes; the payee relying on a prediction of the law that turns out to be bad, is assumed to be taking the risk of it. While some mistakes of law are akin to mistakes of fact, others, particularly as regards doubtful points, would fall as mispredictions. Admittedly though, this approach goes against the view of the majority on the nature of the common law; it would seem on their

[31] *Supra,* note 11.

[32] The doctrine of prospective over-ruling has been applied in Singapore: *Abdul Nasir Bin Amer Hamsah* v *Public Prosecutor* [1997] 3 SLR 643, *PP* v *Manogaran s/o R Ramu* Cr Appeal No 27 of 1996. The implications of this in private law, and specifically in restitution, if any, have not been considered.

[33] 1119F.

[34] 1138F.

[35] 1136D.

Lordships' view, the law is reified – it exists now, and it has retrospective effect, so it must have existed in the past. But, with respect, the law is not a thing; it is a social construct, and does not have to exist as a single entity through time.

The Effect of a Settled Understanding of the Law

If the view is taken that the effect of the over-ruling of a decision renders a past payment made on that decision one caused by a mistake of law, the same should follow as regards a payment made under a commonly accepted view of the law without judicial authority. Nevertheless, Lords Goff and Hope examined the matter further and came to the conclusion that payment on the basis of a settled understanding of the law could not be a defence.[36] In contrast, Lord Hoffmann accepted that a rule barring recovery because of a settled view would preserve the security of past transactions. However, His Lordship considered that a judicial decision adopting it would be a founded solely on policy and would not be a course open to the House of Lords.[37] The minority judges for their part considered that payment on a settled understanding could not be recovered.

The first point that can be made about this issue is that it may be questionable whether settled understanding is really a defence.[38] If it were, it would distinguish the situation where there is over-ruling of a prior decision from one without any such over-ruling. There is no reason why this should be so. Rather settled understanding is only relevant if it were accepted that changes in the law do not render past payments mistaken. The notion of settled understanding merely equates the common perception of the law with judicial decision.[39] It therefore operates not as a defence, but as a limit on the cause of action. The consequence of this is that the burden of showing that there is no settled understanding should lie on the payer.

The main criticism of the notion of settled understanding its imprecision. As noted by Lord Goff, the concept of settled understanding was one that had given rise to problems in jurisdictions which had adopted it.[40] It was not possible to come to a crystal-clear definition of what amounted to a

[36] 1124A, 1152E.

[37] 1139F. This seems strained: if the mistake of law rule could be abrogated, the House of Lords ought to be able to define its limits. With respect, Lord Hoffmann draws an arbitrary limit on the scope of judicial decision making.

[38] *Cf* Lord Lloyd 1131H.

[39] As noted by Lord Lloyd, there is some precedence for this in commercial law as regards customs. Lord Browne-Wilkinson also noted its relevance, at least until recently, in conveyancing.

[40] For example, New Zealand and Western Australia (common understanding), see Lord Goff 1123A to 1124A.

settled understanding. But similarly imprecise notions permeate the law. The 'reasonable man' is not any more precise than 'settled understanding'; a lawyer would be hard pressed to define what this means, beyond what has been exemplified in decided cases.[41] Another criticism of the concept of settled understanding made by Lord Goff was that it led to the anomaly that the further in the past a payment was made, the less likely it was based on a settled understanding of the law. But the difficulty with past payments would be avoided anyway if it was accepted that judicial decisions do change the law, but that such changes cannot alter the voluntariness of a payment made in the past.

It was also thought that the plaintiff who consults his adviser would be in a better position than one who did not.[42] But with respect, the plaintiff who did not consult a legal adviser would probably be found to be submitting to the defendant's claim.[43]

It is submitted that no convincing reasons have been shown against the adoption of a concept of settled understanding limiting recover for mistake of law. The danger is that without such a doctrine, transactions will be too easily opened, long past their completion. There is a great need for security of receipt, which the concept goes some way to protecting. It is to be hoped that should the mistake of law rule be abrogated in Singapore, the notion of settled understanding will be adopted. Any uncertainty about its operation can be addressed through case law development.

The Possible Defences

As regards the defences to claim in mistaken payment, it was thought that the usual defences, particularly change of position,[44] could apply.[45] But the House of Lords rejected a defence of honest receipt, suggested by Brennan J in *David Securities David Securities Pty Ltd* v *Commonwealth Bank of Australia.*[46] The proposed defence would excuse a defendant who received

41 In any event, as noted by Lord Lloyd, as regards the notion of settled understanding, guidance can be obtained from the Law Commission Report.

42 Lord Hope at 1152E.

43 As regards negligent advice, this is immaterial; *cf Kelly* v *Solari* (1841) 9 M&W 54.

44 Indeed, it may be that the availability of this defence would render moot the possibility of recovery of payments made on a settled understanding (*Cf* Lord Lloyd). However this does lead to a 'front-loading' of the action – it is left to the defendant to establish the defence.

45 The defence of submission to an honest claim was not examined in depth.

46 *Supra*, note 3 and *cf Willis Faber Enthoven Pty Ltd* v *Receiver of Revenue, supra*, note 4.

the payment honestly believing that he was entitled to it. The rationale is that such a defendant should not be prejudiced. But in the absence of any change of position, the only possible motive making such a defence available is to throw the risk upon the payer. It would then merely be the resurrection of the mistake of law bar as a defence. If the risk should really fall on the payer, then it would be more straightforward to perpetuate the mistake of law bar.

Additionally, such a defence would churn up more transaction costs than a straight bar to recovery. As noted in several of the judgments, the proposed defence would be very wide, and subsume other defences.[47] This points against its adoption. Moreover, none of the other judges in *David Securities Pty Ltd* v *Commonwealth Bank of Australia*[48] supported it, and no need was felt for it in the cases. It would also draw a distinction, which would be unjustifiable, between mistakes of fact and mistakes of law.

The Limitation Period

The House of Lords considered that the relevant limitation period was that prescribed by section 32(1)(c),[49] the Singapore equivalent of which is section 29(1)(c) of the Limitation Act (Cap 163). Section 29(1)(c) reads (in its material portions):

> 29(1). Where, in the case of any action for which a period of limitation is prescribed by this Act, either –
> ...
> (c) the action is for relief from the consequences of a mistake, the period of limitation shall not begin to run until the plaintiff has discovered the ... the mistake ... or could with reasonable diligence have discovered it ....

Although it does not specifically refer to mistakes of law, and the section was made law at a time when it was thought that no recovery could be made for a mistake of law, there is no reason why it ought not to be extended to such mistakes. The only point that should be made is that a long-stop provision ought to be included, as is the case with latent mistakes.[50] Such

[47] See Lord Goff, 1124 for example.
[48] *Supra,* note 3.
[49] *Supra,* note 13.
[50] See for example, *RSP Architects, Planners & Engineers* v *Ocean Front Pte Ltd* [1996] 1 SLR 113, interpreting ss 24A and 24B.

a provision would avoid the unraveling of transactions long past by recent changes in the law, a danger thrown up by the majority decision in *Kleinwort Benson.*

Conclusion

It is probably only a matter of time before the mistake of law bar is abrogated in Singapore. When it is abrogated, it is hoped that the Court of Appeal will consider carefully the ramifications of the majority judgments in *Kleinwort Benson*. It is submitted, with respect, that a far more preferable approach would be to accept that changes in the law, whether in respect of judicially determined rules or those evolved on a settled understanding, should not render a payment voluntarily made in the past an involuntary one.

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