WHAT IS THE CONSEQUENCE OF AN ILLEGAL CONTRACT?

by

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FORMATION OF A CONTRACT

For an agreement to be enforceable, in other words, for it to become a contract, the pre-requisites of 'offer', 'acceptance', 'intention to create legal relationship' and 'consideration' must be present. If any of these requirements are not present in an agreement, the arrangement remains unenforceable.

The following observations made in *Halsbury's Laws of England* (4th edn, reissue, 1998) vol 9 at [632] should also be noted:[1]

> 'Agreement is usually reached by the process of offer and acceptance and, where this is so, the law requires that there be an offer on ascertainable terms which receives an unqualified acceptance from the person to whom it is made. In the nineteenth century, the popular theory was that there could be no contract without a meeting of the minds of the parties, *consensus ad idem*. This is still the general rule, so that, where the intended acceptance is not in accordance with the terms of the offer, the court may find that there is no binding contract, even though both parties to the purported contract contend that there is a binding contract.'

An offer is an indication by one party to another party of his willingness to enter into a legally binding contract on certain specified terms. The statement amounting to an offer must be such that, on acceptance, without further negotiations as to the terms, a binding contract comes into effect.[2]

Acceptance is the exercise of the power by the person to whom the offer has been made to enter into a contract by manifesting assent in return. When the offeree manifests such an intention, the offeree is said to have

accepted the offer. Upon acceptance, the offeror becomes bound by the contract proposed by him in the offer.[3]

With the acceptance of the offer, there is certainly an intention to create a legal relationship. One of the vital elements is that the parties must have the intention to enter into such a contractual relationship.

The last pre-requisite in forming a contract is consideration. The general meaning of consideration is stated in *Halsbury's Laws of England* (4th edn, reissue, 1998) vol 9(1) at [728] as follows:

> 'Meaning of "consideration"
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> Valuable consideration has been defined as some right, interest, profit, or benefit accruing to the one party, or some forbearance, detriment, loss or responsibility given, suffered, or undertaken by the other at his request. It is not necessarily that the promisor should benefit by the consideration. It is sufficient if the promisee does some act from which a third person benefits, and which he would not have done but for the promise.
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> Thus consideration for a promise may consist in either some benefit conferred on the promisor, or detriment suffered by the promisee, or both. On the other hand, that benefit or detriment can only amount to consideration sufficient to support a binding promise where it is causally linked to that promise. Furthermore, consideration must be distinguished from both a motive and a condition.
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> Consideration may be executed or executory, but it may not be past; it need not be adequate, but it must be some value; and it must move from the promisee.'

ILLEGAL CONTRACT

The relevant provisions governing the illegality of a contract can be found in section 24 of the Contracts Act 1950 which reads as follows:

'24 The consideration or object of an agreement is lawful, unless–

(a) It is forbidden by a law;

(b) It is of such a nature that, if permitted, it would defeat any law;

(c) It is fraudulent;

(d) It involves or implies injury to the person or property of another; or

(e) The court regards it as immoral, or opposed to public policy.'

In each of the above cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void.'

Besides the aforementioned section 24 of the Contracts Act 1950, another relevant provision is section 2(g), which says:

'An agreement not enforceable by law is said to be void.'

Based on the abovementioned sections 24 and 2(g) of the Contracts Act 1950, generally, when a contract contravenes any legislation, regulations or bylaws, the contract could be nullified and is unenforceable. In other words, the contract is void.[4] A void contract is invalid from the outset, lacking legal effect, often due to illegality or impossibility. The contract is invalid from its inception.

Be it as it may, in the reality of the commercial world, the courts often face the difficult task of determining the enforceability of a contract. More often than not, the legislation or regulations are silent as to the effect of a contravention, and there are some instances where the courts hold the contract to be unenforceable while some contracts are enforceable.

EXPRESS PROHIBITION

Sometimes, a statute expressly provides that the legal effect of non-compliance with any of its provisions will render all contracts unenforceable, void or both. In such a scenario, the courts would have no difficulty holding such a contract to be unenforceable or void. For example, under the Malay Reservation Enactments, the transfer of any Malay reservation land to a non-Malay is expressly prohibited by the law. Therefore, any contract which purports to transfer such Malay reservation land to a non-Malay is void.[5]

However, if the statute itself gives an exception to such transfer of Malay reservation land to a non-Malay subject to having obtained the necessary consent or approval from the relevant competent body, such contract is held by the court to be enforceable. His Lordship Azmi CJ in the Federal Court case of *Foo Say Lee v. Ooi Heng Wai*[6] stated:

> 'Section 13A(i) of the Enactment gives the power to His Highness the Ruler in Council in his discretion to approve a transfer of a right or interest of any Malay in Reservation land to any person not being a Malay. Since the Enactment itself has provided a method of effecting a transfer of a Reservation land from a Malay to a non-Malay, I am unable to come to the conclusion that any agreement to transfer such land by a method so provided by the Enactment itself can be said to be contrary to the provisions of the Enactment and therefore null and void under section 12; nor could it be said that the agreement is an attempt to evade the provisions of the Enactment. (See judgment of Thomas CJ in *Idris bin Haji Mohamed Amin v. Ng Ah Siew* [1935] MLJ 257 at page 258).'

IMPLIED PROHIBITION

It is often the case that most statutes do not contain any express provisions to render contracts in contravention of the statute to be void. In such cases, the courts would then have to decide whether, upon a construction of the

statute, there is an implied prohibition against entering into contracts in contravention of the statute.

In each case, the courts would have to consider the true legislative intent. In so construing a statute, the ordinary rules of interpreting statutes apply. In the Supreme Court case of *Chung Khiaw Bank Ltd v. Hotel Rasa Sayang Sdn Bhd & Anor*,[7] Hashim Yeop Sani CJ in the judgment stated:

> 'The next question is the effect on a contract where it is prohibited by statute. In *Phoenix Insurance v. Adas* [1987] 2 All ER 152, the Court of Appeal was concerned with the question of illegality of certain insurance and reinsurance contracts. Kerr LJ dealt with the question of illegality as follows:
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> "The next point is then that it is settled law that any contract which is prohibited by statute, either expressly or by implication, is illegal and void. The leading old authority is the judgment of the Court of Exchequer delivered by Parke B in *Cope v. Rowlands* (1836) 2 M & W 149; 150 ER 707. The relevant statutory provision prohibited any unauthorised person from 'acting as a broker' within the City of London. It was held that an otherwise valid brokerage contract made by an unauthorised person was illegal and void. Since the statute in that case did not contain any reference to contracts, the situation under the 1974 Act is a fortiori. Parke B said (2 M & W 149 at 157; 150 ER 707 at 710):
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> > 'It is perfectly settled that, where the contract which the plaintiff seeks to enforce, be it express or implied, is expressly or by implication forbidden by the common or statute law, no court will lend its assistance to give it effect. It is equally clear that a contract is void if prohibited by a statute, though the statute inflicts a penalty only, because such a penalty implies a prohibition … And it may be safely laid down, notwithstanding some dicta apparently to the contrary, that if the contract be rendered illegal, it can make

> no difference, in point of law, whether the statute which makes it so has in view the protection of the revenue, or any other object. The sole question is, whether the statute means to prohibit the contract?"'

Even if there is such an implied prohibition against entering into contracts in contravention of the statute, a statute may also sometimes contain a saving provision to the effect that even though there had been a contravention of certain provisions of the statute by the parties, nevertheless, such contravention would not affect the legality of any contract entered into. For instance, section 67(6) of the Companies Act 1965 before it was amended provided as follows:

> '67(6) Nothing in this section shall operate to prevent the company from recovering the amount of any loan made in contravention of this section or any amount for which it becomes liable on account of any financial assistance given in contravention of this section.'

The Federal Court, in the judgment of *Lori Malaysia Bhd v. Arab-Malaysian Finance Bhd*,[8] held that although it was illegal to give a loan in contravention of section 67(6) of the Companies Act 1965, but yet it enables any person to recover any moneys in respect of a security in contravention of the section. This means the contract is enforceable despite it being illegal under section 67(6) of the Companies Act 1965. Edgar Joseph FCJ at p 1019 of the judgment, said:

> 'However, in our view, in so far as sub-s (6) of s 67 of the Act enables any person to recover any moneys in respect of a security in contravention of the section, the subsection appears to be a statutory recognition of the rule in *Victor Battery* wherein it was decided that an illegal security given by a company to finance the purchase of its own shares contrary to s 45(1) of the Companies Act 1929 (UK) (being the equivalent of our s 67(1) of the Act), was not avoided.'

AIDS TO STATUTORY CONSTRUCTION: PENALTY

Where a statute imposes a penalty for contravention of the provision in question, it can be presumed that the general, but not the conclusive, intention of the legislature was to impliedly invalidate the contract. Therefore, even in the case where a penalty is stipulated in a statute, the courts would still have to construe the statute to determine whether a contract entered into in contravention of it is enforceable.[9] In this regard, the observation of Gibbs ACJ in *Yango Pastoral Co. Pty Ltd v. First Chicago Australia Ltd*[10] is relevant:

> 'Where a statute imposes a penalty upon the making or performance of a contract, it is a question of construction whether the statute intends to prohibit the contract in this sense, that is, to render it void and unenforceable, or whether it intends only that the penalty for which it provides shall be inflicted if the contract is made or performed.'

An illustration could be found in the High Court case of *Co-operative Central Bank Bhd v. Belaka Suria Sdn Bhd*,[11] Lim Beng Choon J remarked that mere imposition of a penalty for the contravention of a statute cannot be regarded as a conclusive indication that the legislature also intended to invalidate all offending contracts. At p 461 of the judgment, he said:

> 'It is clear that the loan given to the borrower secured by the charge is permissible under s 30 of the 1948 Act. The consideration or object of the charge agreement is not therefore forbidden by law. The infringement on s 9 of the 1973 Act does not render the charge agreement a nullity. The plaintiff may be liable to a penalty imposed under sub-s (2) of s 9 of the 1973 Act, but I cannot see how the penalty imposed by the said Act can affect the charge agreement which the plaintiff is allowed to enter into under the 1948 Act.'

HOUSING DEVELOPMENT (CONTROL AND LICENSING) ACT 1966

Despite having discussed the express and implied prohibition against entering into contracts in contravention of the statute, there is one unique and peculiar statute which has been enacted to protect a class of persons, i.e. the purchasers of houses. Such specific statute is known as the Housing Development (Control and Licensing) Act 1966.

In the Federal Court case of *SEA Housing Corp Sdn Bhd v. Lim Poh Choo*,[12] Suffian LP stated:

> 'It is common knowledge that in recent years, especially when government started giving housing loans making it possible for public servants to borrow money at 4% interest per annum to buy homes, there was an upsurge in demand for housing, and that to protect home buyers, most of whom are people of modest means, from rich and powerful developers, Parliament found it necessary to regulate the sale of houses and protect buyers enacting Act …'

The same sentiment was shared by Tengku Maimun CJ in the Federal Court case of *Ang Ming Lee v. Menteri Kesejahteraan Bandar, Perumahan dan Kerajaan Tempatan & Anor and Other Appeals*[13] stated:

> '[40] The Act being a social legislation designed to protect the house buyers, the interests of the purchasers shall be the paramount consideration against the developer.'

That question that arises is: what consequence flows from an infringement of the laws by the developers? If the courts were to hold such an agreement to be unenforceable and void, in many situations, it would be the purchasers, for whose very benefit the laws were enacted, who would suffer – they would be deprived of the houses and, in many cases, they would also lose the money that had already paid. The courts therefore would have to seek a balance in such a situation to give effect to the

intention of the lawmakers, i.e. protect the class of persons that the law attempts to protect.[14]

The validity of sale and purchase agreements entered into between a number of purchasers and a developer who did not have a developer's license at the relevant time was considered by the Supreme Court in *Beca (M) Sdn Bhd v. Tang Choong Kuang & Anor*,[15] the Supreme Court in this case held that the agreements for the purchase of the flats were voidable at the option of the purchasers. Lee Hun Hoe CJ (Borneo) stated:

> '… we are unable to agree with the learned judge that the provisional agreement is illegal. We prefer the approach adopted by the learned President rather than that of the learned judge on the matter. Since the Enactment is meant to be for the benefit of the house buyers it would seem, in our view, proper and right to regard the provisional agreement as binding but voidable at the instance of the house buyers. They should be given the option of either enforcing or repudiating the agreement depending upon the market situation of the housing development in the country. If the provisional agreement are to be declared illegal it might in a given situation prove profitable to the developers, for instance, when there is a housing boom. In which case, it would be absurd to say that the Enactment is to protect the buyers from exploitation when it is actually aiding the developers to enrich themselves. So the avoidance of the agreement would cause inconvenience and injury to innocent members of the public. To declare the agreement binding but voidable at the instance of the buyers would provide no incentive to the developers to do any act before obtaining a license.'

RESTITUTION UNDER SECTION 66 OF THE CONTRACTS ACT 1950

One of the most important functions of the law of restitution is to carry out an adjustment of the rights of the parties under a contract or in relation to some agreements or understandings falling short of a legally binding contract. This occurs when there has been a transfer of value by one party

to another on a basis which has failed to materialise or ceased to exist, such as when an agreement has become void due to illegality and some other reasons.

In some cases, the contract or agreement between the parties may not expressly stipulate what is to happen to certain benefits or advantages which have been transferred or conferred by either party in the event the contract or agreement becomes void. In such situations, a duty of restitution arises by operation of law pursuant to section 66 of the Contracts Act 1950 and dehors the contract or agreement. The duty of restitution arises because there is an absence of a legal basis to retain the benefit or advantage received under the contract.[16]

Section 66 of the Contracts Act 1950 reads as follows:

> '66. When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under the agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.

Section 2 of the Contracts Act 1950 provides a general definition of what agreements or contracts are 'voidable' or 'void':

> 'Section 2. Interpretation
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> In this Act the following words and expressions are used in the following senses, unless a contrary intention appears from the context:
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> *(g)* an agreement not enforceable by law is said to be void;
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> *(h)* an agreement enforceable by law is a contract;
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> *(i)* an agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract; and

(j) a contract which ceases to be enforceable by law becomes void when it ceases to be enforceable.'

As discussed above, an illegal contract in violation of the statute is void and unenforceable. Reference could be made to section 65 of the Indian Contracts Act 1872 which is *para materia* to our section 66 of the Contracts Act 1950. One Privy Council decision referring to section 65 of the Indian Contracts Act is the judgment of *Harnath Kuar v. Thakur Indar Bahadur Singh*.[17]

> 'Before this Board, the claim has been based on section 65 of the [Indian] Contract Act[18]... So framed, the plaintiff's claim to compensation rests, not upon any principle or formula of English law, but on the words of this section, and it has to be seen whether the facts of this case come within its scope. The section deals with (a) agreements and (b) contracts. The distinction between them is apparent from section 2. By clause (a) every promise and every set of promises forming the consideration for each other is an agreement, and by clause (h) an agreement enforceable by law is a contract and (b) with agreement not so enforceable. Section 65 therefore, deals with (a) agreements enforceable by law and (b) agreements not so enforceable. By clause (g) an agreement not enforceable by law is said to be void.
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> An agreement, therefore, discovered to be void is one discovered to be not enforceable by law, and, on the language of the section, would include an agreement that was void in that sense from its inception as distinct from a contract that becomes void.'

Sharing the same view, our Federal Court case of *Ahmad bin Udoh v. Ng Aik Chong*[19] where Azmi LP observed that it is important to note 'that an agreement discovered to be void for the purpose of section 66 includes an agreement that was void in that sense from its inception'.

Similarly, in another Federal Court case of *Yeep Mooi v. Chu Chin Chua & Ors*[20] which held that:

> 'An agreement 'discovered to be void' does not mean that the contract is void on discovery or void because of discovery of illegality. It means what it says, in that the contract was void *ad initio* without the parties at the time being aware of the true legal position. It is only later that the contract is found to be void and so they became aware of its voidness.'

The word 'advantage' in section 66 of the Contracts Act 1950 was not given a specific definition in the Contracts Act 1950, but reference could probably be made to the Federal Court case of *Nunis v. Public Prosecutor*[21] where Abdul Hamid FJ at p 117 of the judgment remarked that:

> 'As for the other meaning of the word "advantage", it may be useful to examine the meaning given to the expression under the Public Bodies Corrupt Practices Act 1889 as set out in *Words and Phrases* Second Edition Vol. 1 which reads–
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> > "the expression 'advantage' includes any office or dignity, and any forbearance to demand any money or money's worth or valuable thing, and includes any aid, vote, consent, or influence, or pretended aid, vote, consent, or influence, and also includes any promise or procurement of or agreement or endeavour to procure, or the holding out of any expectation of any gift, loan, fee, reward, or advantage, as before defined."'

Money is a universal medium of exchange, and as a general rule, the receipt and use of money will almost always be regarded as a benefit or advantage to a defendant.[22]

The word 'compensation' in section 66 of the Contracts Act 1950 is not to be equated with damages or compensation for breach of contract. In *Govindram Seksaria v. Edward Radbone*,[23] the Privy Council expressly approved the following observations of Stone CJ in the court below on the word 'compensation' contained in section 66 of the Contracts Act:

> 'Compensation for an advantage may appear to be a contradiction in terms, since compensation connotes a measure of loss or damage and not the value of an advantage ... Under section 65 [of the Indian Contract Act] the alternatives are to restore any advantage 'or to make compensation for it to the person from whom he received it.' This mean valuing or quantifying in money the advantage retained, if retained it be'.

RESTITUTION IS MANDATORY RELIEF

Section 66 of the Contracts Act 1950 creates a cause of action whereby a right to restitution arises where the conditions of recovery under section 66 have been satisfied. In other words, when the facts of a case come within the scope of section 66, the court ***MUST*** award restitution and does not have the discretion to refuse relief.

In *Muralidhar Chatterjee v. International Film Company Limited*,[24] the Privy Council observed that 'where a payment has been made under a contract which has for whatever reason become void, the duty of restitution would seem to emerge ...' and 'the Act requires that they give back whatever they received under the contract.' *Muralidhar Chatterjee* was applied in *Yong Mok Hin v. United Malay States Sugar Industries Ltd*,[25] where the Federal Court referred to section 66 of the Contracts Act 1950 as imposing an obligation to restore any benefit received.[26]

In *Menaka v. Lum Kum Chum*,[27] the Privy Council laid down the principle under section 66 of the Contracts Act 1950 that 'a right to restitution may arise out of the failure of a contract though the right be not itself a matter of contractual obligation.'

TREND FOR COURTS TO BE LESS READY TO FIND A CONTRACT ILLEGAL OR UNENFORCEABLE SIMPLY BY REASON OF A STATUTORY PROVISION

One notable result is that Malaysian courts have followed the trend of the courts in common law countries to be slow in striking down commercial

contracts on the grounds of illegality. The Federal Court case of *The Co-Operative Central Bank Limited (In Receivership) v. Feyen Development Sdn Bhd*[28] held that there appears to be a trend for courts to be less ready to find a contract illegal or unenforceable simply by reason of a statutory provision. Edgar Joseph FCJ, in HisLordship's judgment, stated that:

> 'We note that Greig and Davis on the *Law of Contract*, at pp 1117 ff, say that they see a trend in decisions whereby courts are now less ready to find a contract illegal or unenforceable simply by reason of a statutory provision.
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> And, we also note that in *Farrow Mortgage Services Pty Ltd (in liq) v. Edgar & Others* (1993) 114 ALR 1, the following principles of illegality were enunciated by the Court (Lockhart, Gummow and Lee JJ) at pp 9 and 10:
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> > "In his article '*Restitutionary Recovery of Benefits Conferred under Contracts in Conflict with Statutory Policy – The New Golden Rule*' (1987) 25 Osgood Hall LJ 787 at pp 788–9, Prof McCamus describes the 'continued and remarkable growth of regulation in the modern era' as having created an environment which is rather different from that in which the English courts formulated the approach of common law to illegality in contract; the commission of any offence then was perhaps more likely a signal of significantly anti-social conduct than it is today.
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> > The learned author also points out that when agreements have been entered into which create a conflict with the letter or the spirit of a regulatory legislative scheme, two problems emerge for resolution by the law of private obligations. The first concerns the validity of the agreement itself. The second concerns the secondary consequences for the parties, and third parties, if the agreement is indeed held to be unenforceable or void. Statute may render the agreement unenforceable without being void but, if void, it must, of

necessity, be unenforceable: see *Lejo Holdings Pty Ltd v. Deutsche Bank (Asia) AG* [1988] 2 Qd R 30 at 41.

In Australia, the relevant principles, as settled, are largely to be found in the expositions in the judgments in *Yango Patsoral Co Pty Ltd v. First Chicago Australia Ltd* (1978) 139 CLR 410; 21 ALR 585. Counsel for both sides accepted that this was so. We have also been much assisted by the judgment of McPherson J in *JC Scott Constructions v. Mermaid Waters Tavern Pty Ltd* [1984] 2 Qd R 413 cited by the respondents."

And, in *Yango*, Mason J (as he then was) said at p 429:

"There is much to be said for the view that once a statutory penalty has been provided for an offence the rule of the common law in determining the legal consequences of commission of the offence is thereby diminished – see my judgment in *Jackson v. Harrison* (1978) 138 CLR 438 at p 452. See also the suggestions that the principle cannot apply to all statutory offences (*Beresford v. Royal Insurance Co Ltd* in the Court of Appeal [1937] 2 KB 197 at p 220, per Lord Wright*; Marles v. Philip Trant & Sons Ltd* [1954] 1 QB 29 at p 37), per Denning LJ, and that it would be a curious thing if the offender is to be punished twice, civilly as well as criminally (*St John Shipping Corp v. Joseph Rank Ltd* [1957] 1 QB 267 at p 292), per Devlin J. The main considerations from which the principle *ex turpi causa* arose can be seen in the reluctance of the courts to be instrumental in offering an inducement to crime or removing a restraint to crime: *Beresford's Case* [1938] AC 586 at pp 586, 599; *Amicable Society v. Bolland (Fauntleroy's Case* (1830) 4 Bligh (NS) 194 at p 211; 5 ER 70, at p 76).

However, in the present case Parliament has provided a penalty which is a measure of the deterrent which it intends to operate in respect of non-compliance with s 8. In this case it is not for the court to hold that further consequences should flow, consequences which

> in financial terms could well far exceed the prescribed penalty and could even conceivably lead the plaintiff to insolvency with resultant loss to innocent lenders or investors."'[29]

Subsequently, in another Federal Court case of *Lori Malaysia Bhd v. Arab-Malaysian Finance Bhd*,[30] again Edgar Joseph FCJ, delivering the judgment, stated that:

> 'But, having said that, we consider that the trend shown by the courts in Common Law countries to be slow in striking down commercial contracts on the ground of illegality is a sensible one, which we should follow thus incorporating it as part of our Common Law.
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> Indeed, twenty years ago, this is precisely what Raja Azlan Shah, CJ (now H.R.H. the Sultan of Perak) had done in *Central Securities (Holdings) Bhd. v. Haron bin Mohamed Zaid* [1979] 2 MLJ 244. Here is what his Lordship said (at p. 247), when speaking for the old Federal Court:
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> > "We bear in mind the much quoted warning of Devlin J in St. John Shipping Corporation v. Joseph Rank Ltd. [1956] 3 AER 683, 690, 691) against a too ready assumption of illegality or invalidity when dealing with statutes regulating commercial transactions."'[31]

Even in the recent Federal Court case of *Liputan Simfoni Sdn Bhd v. Pembangunan Orkid Desa Sdn Bhd*,[32] in the year of 2019, the Federal Court again emphasised the importance of not striking down commercial contracts easily at [117] of the judgment:

> '[117] ... We agree with the view that the courts should be slow in striking down commercial contracts on the ground of illegality.'

EX TURPI CAUSA NON ORITUR ACTIO (NO ACTION WILL ARISE FROM A WRONG DONE)

The general rule both under English law and under the Contracts Act 1950 is that the courts would not 'enforce' an illegal contract: *ex turpi causa non*

oritur actio (no action will arise from a wrong done). The *locus classicus* in English law on this point is the decision of Lord Mansfield in *Holman v. Johnson*:[33]

> 'No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act. If from the plaintiff's own stating or otherwise, the cause of action appears to arise *ex turpi causa*, or the transgression of a positive law of this country, then the court says he has no right to be assisted. It is upon that ground the court goes, not for the sake of the defendant, because they will not lend their aid to such a plaintiff. So if the plaintiff and defendant were to change sides, and the defendant was to bring his action against the plaintiff, the latter would not then have the advantage of it, for where both are equally at fault, *potior est conditio defenddentis*.'[34]

In this regard, it should be noted that all of the leading and binding authorities of the Privy Council and the Federal Court on the interpretation of section 66 of the Contracts Act 1950 have made it absolutely clear that a plaintiff may not rely on section 66 to obtain restitution where the plaintiff has knowledge of or is party or privy to the illegality.

In the Federal Court case of *Singma Sawmill Co Sdn Bhd v. Asian Holdings (Industrialised Buildings) Sdn Bhd*,[35] Raja Azlan Shah CJ (Malaya) said:

> 'The section therefore enacts in statutory form that a contract that is illegal in itself is void and unenforceable by either party. It is contaminated by *turpis causa* and that rule has long been established that *ex turpis causa oritur non actio* – no person can claim any right or remedy whatsoever under an illegal transaction in which he has participated. The courts do not overlook the fact that they do not assist a person who comes with unclean hands. In the words of Lindley LJ in *Scott v. Brown, Doering, McNab & Co* [1892] 2 QB 724 728:
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> > "No court ought to enforce an illegal contract or allow itself to be made the instrument of enforcing obligations alleged to arise out of

> a contract or transaction which is illegal, if the illegality is duly brought to the notice of the court, and if the person invoking the aid of the court is himself implicated in the illegality."

> That brings us to the real crux of this appeal. Is the tenancy agreement void and unenforceable? Now, in the cases to which we have referred, there was an intention to use the subject-matter of the agreement for an unlawful purpose, and also an intention to make use of the lease or agreement for an unlawful purpose. The principles applicable to both cases are the same. In such cases any party to the agreement who has the unlawful intention is precluded from suing upon it. *Ex turpis causa non oritur actio*. The action does not he; not for the sake of the defendant but because the court will not lend its assistance to such a plaintiff. It will look behind such cosmetic arrangements to see the real intention.'

In another subsequent Federal Court case of *Wong Yoon Chai v. Lee Ah Chin*,[36] Abdul Hamid FCJ, in his judgment, said:

> 'What necessarily emerges from that decision is that it is for the court in each case to determine whether or not the parties to a transaction are aware of the illegality at the time of making the loan transaction.
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> As a licensed moneylender for a period of years he could not have been ignorant of the fact that he had breached the Moneylender's Ordinance. In any event he has not said that he had no knowledge of the illegality.'

WHERE PARTIES ARE *IN PARI DELICTO*

Besides the legal maxim of *ex turpi causa non oritur actio* mentioned above, there is another legal principle disallowing restitution known as *in pari delicto*, which means that the parties were knowingly involved in the illegal transaction. No relief under section 66 of the Contracts Act 1950 would be granted to either party to an illegal agreement if both parties had full knowledge of the illegality at the time when the agreement was entered

into. Indeed, it would be against public policy to allow any party to obtain relief if it knowingly entered into an illegal contract.[37]

In the Court of Appeal judgment of *Mustafa Osman v. Lee Chua (P)*,[38] Gopal Sri Ram JCA, delivering the judgment, observed that:

> 'It cannot be doubted for a moment that the parties in the present case were *in pari delicto* when they entered into the illegal tenancy agreement. After all, the tenancy agreement was prepared by a solicitor. This is, therefore, not a case where the contract may be said to be discovered to be void under section 66 of the Contracts Act 1950. See, *Soh Eng Keng v. Lim Chin Wah* [1979] 2 MLJ 91.'

UNAWARE OF THE ILLEGALITY

The crucial test for the application of section 66 of the Contracts Act 1950 is whether the parties were aware of the illegality at the time the contract was made. The parties may only seek restitution under section 66 if they were unaware of the illegality. In the Federal Court case of *Ng Siew San v. Menaka*,[39] it was stated in the judgment:

> 'In order to invoke section 65 (equivalent to section 66 Malaysian Contract Act 1950), the validity of the contract or agreement should be discovered subsequent to the making of it. This cannot be taken advantage of by parties who knew from the beginning the illegality thereof. It only applies to a case where one of the parties enters into an agreement under the belief that it was a legal agreement, that is, without the knowledge that the agreement is forbidden by law or opposed to public policy and as such illegal. The effect of section 65 is that, in such a situation, it enables a person not *in pari delicto* to claim restoration since it is not based on an illegal contract but disassociated from it. This is permissible by reason of the section because the action is not founded on dealings which are contaminated by illegality. The party is only seeking to be restored to the *status quo ante*.'

EXCEPTION – ILLEGAL PURPOSE NOT ACHIEVED

Despite the general rule of *ex turpi causa non oritur actio* and *in pari delicto* as discussed above, there is one peculiar, unique Federal Court case of *Tan Chee Hoe & Sons Sdn Bhd v. Code Focus Sdn Bhd*[40] having granted restitution under section 66 of the Contracts Act 1950 despite both parties being fully aware of the illegal agreement when they executed the sale and purchase agreement. The Federal Court distinguished it by saying that although the sale and purchase agreement had been signed, it was not completed, concluded, and still in the stage of executory. Therefore, the illegal purpose was not achieved, and as such, the court ordered restitution accordingly. This decision has attracted some controversial comments from academicians.[41]

In this case, the plaintiff had entered into a sale and purchase agreement with the defendant for the purchase of the entire issued and paid-up share capital of one Choo Hoe Sdn Bhd. Pursuant to the sale and purchase agreement, the plaintiff paid the defendant a 10% deposit amounting to RM1.6 million. The completion of the sale was subject to conditions precedent, one of which was the approval of the Foreign Investment Committee and the other, the approval of the sale of shares by the defendant's shareholders in an extraordinary general meeting. The plaintiff failed to pay the balance purchase price before the stipulated date in the sale and purchase agreement, resulting in the defendant forfeiting the 10% deposit. The plaintiff disputed the forfeiture on the grounds that the defendant was in breach of the sale and purchase agreement; that is, the defendant, among others, failed to obtain the required approvals of the Foreign Investment Committee and its shareholders. The defendant's position was that the parties had, by way of a side letter, waived the performance of the condition precedent. The plaintiff commenced proceedings against the defendant seeking, *inter alia*, the return of the 10% deposit as well as damages for breach of contract. The claim failed in the High Court but was allowed by the Court of Appeal.

However, the Federal Court unanimously dismissed the defendant's appeal. The court observed that section 132C of the Companies Act 1965, which provides that a company may not transact for the disposal of a substantial portion of the company's property unless the company has first approved the transaction in a general meeting, was a mandatory statutory requirement which the plaintiff and the defendant could not waive as parties to the sale and purchase agreement. On the facts, the court held that the plaintiff had actual notice of the defendant's non-compliance with section 132C of the Companies Act 1965 but had agreed consciously to waive the performance thereof. The knowing and conscious waiver by the parties of the requirements of section 132C was unlawful pursuant to section 24 of the Contracts Act 1950 and the sale and purchase agreement was accordingly void. The plaintiff had knowingly participated in the contravention of the statutory requirement under section 132C and could not enforce the sale and purchase agreement, which was invalid and void.

Against this background, the Federal Court turned to the question of whether section 66 of the Contracts Act 1950 applied to the facts. After citing the leading authorities, including the decisions of the Privy Council in *Harnath Kuar v. Thakur Indar Bahadur Singh* and *Menaka v. Lum Kum Chum*, the Federal Court observed:

> 'The plaintiff in the present case, expressly based its entire claim on the terms of the SPA. The plaintiff, *inter alia*, alleged that the defendant was in breach of the said SPA in failing to deliver vacant possession of the said land in question to the plaintiff; and to obtain shareholders' approval under s 132C of the Companies Act on or before the completion date, as stipulated in various clauses of the SPA. At the same time, the plaintiff expressly in para 12 of its statement of claim claimed that it was 'at all material times ready, willing and able to honour its obligation under the SPA, subject to the SPA becoming unconditional. Clearly the plaintiff in this case was trying to enforce a void contract.

> The SPA in this case became void when the mandatory statutory requirement of shareholders' approval was not obtained and was consciously waived by the parties at the time when it was executed. Therefore, section 66 of the Contracts Act 1950 came into play i.e. the defendant who had received an advantage (in the form of the 10% deposit of RM1.6 Million) under the void agreement or contract (the SPA) is bound to restore it to the plaintiff from whom he received it ...
>
> Section 66 of the Contracts Act 1950 is clear ... that when a contract becomes void (as in the present case) the party who received any advantage under the contract or agreement is bound to restore it to the person to whom he received it. The advantage to be restored under the section refers to the advantage that he had actually received from the other person. If the advantage received was in the form of 10% deposit of RM1.6 Million, that same advantage must be restored or refunded to the plaintiff. If that cannot be done for whatever reasons, then the defendant is bound to make compensation for it–either one, not both.'

Such departure from the general rule of *ex turpi causa non oritur actio* and *in pari delicto* by the Federal Court case of *Tan Chee Hoe* was acknowledged by the Court of Appeal in the judgment of *Public Bank Bhd v. Ria Realiti Sdn Bhd & Ors*.[42] Ravinthran Paramaguru JCA, in delivering the judgment of the court, said:

> '[62] A notable departure from this trend was the Federal Court decision in *Tan Chee Hoe & Sons Sdn Bhd v. Code Focus Sdn Bhd* [2014] 3 CLJ 141; [2014] 3 MLJ 301. In this case, the Federal Court granted relief under s. 66 although both parties had knowledge of the illegality from the beginning and the contract in question was found to be void and unenforceable. We reproduce the relevant passage below from the judgment of Ramli Ali FCJ:
>
> > "[55] Section 66 of the Contracts Act 1950 is clear on this point, that when a contract becomes void (as in the present case) the party who has received any advantage under the contract or agreement is

> bound to restore it to the person to whom he received it. The advantage to be restored under the section refers to the advantage that he had actually received from the other person. If the advantage received was in the form of 10% deposit of RM1.6m, that same advantage must be restored or refunded to the plaintiff. **If that cannot be done for whatever reason, then the defendant is bound to make compensation for it – either one, not both.** In this regard illustration (d) to s. 66 is instructive:
>
> > (d) A contract to sing for B at a concert for RM1,000, which are paid in advance. A is too ill to sing. A is not bound to make compensation to B for the loss of the profits which B would have made if A had been able to sing, but must refund to B the RM1,000 paid in advance. (emphasis added).”’

His Lordship even went on to hold that even if both parties were aware of the illegality, restitution is still allowable.

> ‘[66] ... And s. 66 does not require absence of knowledge of illegality or lack of intention to contravene the law as a precondition for its invocation.’

TRIO CONSIDERATION – THE UK SUPREME COURT CASE OF *PATEL V. MIRZA*

As expressed by some academicians, the topic of illegality is a complex and complicated area. Over the years, the courts have attempted to state certain principles to determine the illegality or otherwise of a contract, but the current position of the law remains unclear and sometimes even confusing.[43] The highest court in the United Kingdom shared the same sentiment. As stated by Lord Toulson in *Patel v. Mirza*:[44]

> ‘“1. No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act.” So spoke Lord Mansfield in *Holman v. Johnson* (1775) 1 Cowp 341, 343, ushering in two centuries and more

of case law about the extent and effect of this maxim. He stated that the reason was one of public policy: "If, from the plaintiff's own stating or otherwise, the cause of action appears to arise *ex turpi causa*, or the transgression of a positive law of this country, there the court says he has no right to be assisted. It is upon that ground the court goes; not for the sake of the defendant, but because they will not lend their aid to such a plaintiff. So if the plaintiff and defendant were to change sides, and the defendant was to bring his action against the plaintiff, the latter would then have the advantage of it; for where both are equally in fault, *potior est conditio defendentis*."

…

3. Take the law of contract. A contract may be prohibited by a statute; or it may be entered into for an illegal or immoral purpose, which may be that of one or both parties; or performance according to its terms may involve the commission of an offence; or it may be intended by one or both parties to be performed in a way which will involve the commission of an offence; or an unlawful act may be committed in the course of its performance. The application of the doctrine of illegality to each of these different situations has caused a good deal of uncertainty, complexity and sometimes inconsistency.

…

9. In this case the issue is whether Lord Mansfield's maxim precludes a party to a contract tainted by illegality from recovering money paid under the contract from the other party under the law of unjust enrichment (to use the term now generally favoured by scholars for what used previously to be labelled restitution and, before that, quasi-contract). On one side it is argued that the maxim applies as much to such a claim as to a claim in contract, and that the court must give no assistance to a party which has engaged in any form of illegality. On the other side it is argued that such an approach would not advance the public policy which underlies Lord Mansfield's maxim, once the underlying policy is properly understood.'

The UK Supreme Court made recent developments with regard to this area of law in the case of *Patel v. Mirza*, which was decided in 2016. Nine judges were presiding in this case which signifies the importance of this area of law. The brief factual matrix of the case is being reproduced as follows:

> '11. The essential facts can be shortly told. Mr Patel transferred sums totalling £620,000 to Mr Mirza for the purpose of betting on the price of RBS shares, using advance insider information which Mr Mirza expected to obtain from RBS contacts regarding an anticipated government announcement which would affect the price of the shares. Mr Mirza's expectation of a government announcement proved to be mistaken, and so the intended betting did not take place, but Mr Mirza failed to repay the money to Mr Patel despite promises to do so. Mr Patel thereupon brought this claim for the recovery of the sums which he had paid. The claim was put on various bases including contract and unjust enrichment.
>
> 12. The agreement between Mr Patel and Mr Mirza amounted to a conspiracy to commit an offence of insider dealing under section 52 of the Criminal Justice Act 1993.'

The Supreme Court referred to the Law Commission conducting a comprehensive review of the law of illegality and making proposals for addressing what the Commission perceived to be its unsatisfactory features. They also refer to European law and its potential impact on UK domestic law. The Supreme Court also examined the approach adopted in Australia, Canada and the USA. The Law Commission, in its final report, did not recommend any statutory change for a combination of reasons and finally concluded that judicial reform was a better way forward, and the Commission found difficulties in drafting a satisfactory statutory model.

Eventually, the Supreme Court in *Patel v. Mirza* propounded a trio of factors for the courts to consider in determining whether to allow restitution in the area of illegality. Lord Toulson stated:

> 'In answer to that question I would say that one cannot judge whether allowing a claim which is in some way tainted by illegality would be contrary to the public interest, because it would be harmful to the integrity of the legal system, without a) considering the underlying purpose of the prohibition which has been transgressed, b) considering conversely any other relevant public policies which may be rendered ineffective or less effective by denial of the claim, and c) keeping in mind the possibility of overkill unless the law is applied with a due sense of proportionality. We are, after all, in the area of public policy. That trio of necessary considerations can be found in the case law.'

Lord Toulson further emphasises the importance of avoiding overkill and applying the law proportionately to allow restitution despite the transaction being tainted with illegality. In His Lordship's judgement, he said:

> '104. As to the dangers of overkill, Lord Wright gave a salutary warning in *Vita Food Products Inc v. Unus Shipping Co Ltd* [1939] AC 277, 293: "Nor must it be forgotten that the rule by which contracts not expressly forbidden by statute or declared to be void are in proper cases nullified for disobedience to a statute is a rule of public policy only, and public policy understood in a wider sense may at times be better served by refusing to nullify a bargain save on serious and sufficient grounds."
>
> 105. To similar effect Devlin J questioned "whether public policy is well served by driving from the seat of judgment everyone who has been guilty of a minor Page 34 transgression" in *St John Shipping Corpn v. Joseph Rank Ltd* [1957] 1 QB 267, 288 289.
>
> 106. In *Saunders v. Edwards* [1987] 1 WLR 1116, 1134, Bingham LJ said "Where issues of illegality are raised, the courts have (as it seems to me) to steer a middle course between two unacceptable positions. On the one hand it is unacceptable that any court of law should aid or lend its authority to a party seeking to pursue or enforce an object or agreement which the law prohibits. On the other hand, it is unacceptable that the court should, on the first indication of unlawfulness affecting any aspect

of a transaction, draw up its skirts and refuse all assistance to the plaintiff, no matter how serious his loss nor how disproportionate his loss to the unlawfulness of his conduct."

107. In considering whether it would be disproportionate to refuse relief to which the claimant would otherwise be entitled, as a matter of public policy, various factors may be relevant.'

Lord Toulson finally concluded in his judgment by saying:

'120. The essential rationale of the illegality doctrine is that it would be contrary to the public interest to enforce a claim if to do so would be harmful to the integrity of the legal system (or, possibly, certain aspects of public morality, the boundaries of which have never been made entirely clear and which do not arise for consideration in this case). In assessing whether the public interest would be harmed in that way, it is necessary a) to consider the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, b) to consider any other relevant public policy on which the denial of the claim may have an impact and c) to consider whether denial of the claim would be a proportionate response to the illegality, bearing in mind that punishment is a matter for the criminal courts.

121. A claimant, such as Mr Patel, who satisfies the ordinary requirements of a claim for unjust enrichment, should not be debarred from enforcing his claim by reason only of the fact that the money which he seeks to recover was paid for an unlawful purpose. There may be rare cases where for some particular reason the enforcement of such a claim might be regarded as undermining the integrity of the justice system, but there are no such circumstances in this case.'

The trio consideration laid down in the case of *Patel v. Mirza* was adopted by our Federal Court case of *Liputan Simfoni Sdn Bhd v. Pembangunan*

Orkid Desa Sdn Bhd[45] in the year of 2019. The Federal Court judgment at [118] says:

> '… in addition, we find that the test laid down by Lord Toulson in Patel that is to say, **the trio consideration**, is a sensible one which we should follow. Applying the test to the facts of this case, we find that **it is an overkill** for the first defendant to lose the subject land for the infringement of the two Acts which is punishable by a fine upon conviction.'

The factual matrix of the case stated in their judgment is reproduced herein:

> 'Background Facts
>
> [5] The background facts leading to this appeal are these. The plaintiff (Pembangunan Orkid Desa Sdn Bhd) was the registered proprietor of a piece of land held under Grant No 5309, Lot 2788 Mukim Petaling, Wilayah Persekutuan ('subject land').
>
> [6] On or about 15 October 2004, an imposter company claiming to be Pembangunan Orkid Desa Sdn Bhd (but with a different company number, namely 9048-D instead of 31550-U) applied to the third defendant (Pendaftar Tanah dan Galian, Wilayah Persekutuan Kuala Lumpur) for a replacement issue document of title alleging that it had lost the original document of title of the subject land. The original document of title was at all material times in the possession of the plaintiff.
>
> [7] The company number 9048-D in actual fact belonged to a company known as Pembangunan Bersatu Sdn Bhd.
>
> [8] On 19 May 2005, the third defendant issued a replacement issue document of title described as Grant No 9971, Lot No 2788 Mukim of Petaling, Wilayah Persekutuan.
>
> [9] On 23 January 2006, the imposter company entered into a sale and purchase agreement ('first SPA') to sell the subject land to Chai Sit

Trading Sdn Bhd (the second defendant) for a sum of RM680,000. The sale was completed on or around 31 May 2006, after which the second defendant was registered as the owner of the subject land.

[10] On 25 August 2006, the second defendant entered into a sale and purchase agreement with Liputan Simfoni Sdn Bhd (the first defendant) to sell the subject land for a price of RM900,000 ('second SPA'). However, an additional sum of RM870,000 stated to be for the costs of earthworks, was paid by the first defendant to the second defendant.

[11] On 25 September 2006, prior to the completion of the second SPA, the imposter company entered a private caveat, alleging that the second defendant had not settled the balance of the purchase price.

[12] On 28 December 2006, the first defendant presented the memorandum of transfer for the subject land together with Form 19G of the Code, the notice to withdraw the caveat.

[13] On 21 February 2007, the imposter company wrote to the third defendant requesting for a registrar's caveat to be entered against the subject land on the ground that the withdrawal of the private caveat was done without its knowledge. A registrar's caveat was duly entered against the subject land on 27 March 2007, as a result of which the first defendant could not be registered as proprietor of the subject land.

[14] At some point, a director of the plaintiff found out that someone had started to clear the subject land. The plaintiff conducted a land search and discovered that the land was registered in the name of the second defendant and there was another pending transfer submitted on 28 January 2006. The search also disclosed that the registrar's caveat had been entered against the title.

[15] On 24 April 2008, the plaintiff lodged a police report stating that it had never sold the subject land and that its original issue document of

> title was still in its possession. The plaintiff also notified the third defendant.'

The High Court held that the second SPA was void *ab initio* pursuant to section 24(b) of the Contracts Act 1950 because it had the effect of evading the payment of real property gains tax on the undeclared profit and the payment of stamp duty on the additional consideration. As such, the transfer of the title for the subject land from the second defendant to the first defendant was obtained by means of a void instrument, which in turn renders the title of the first defendant defeasible pursuant to section 340(2) of the National Land Code.

The Court of Appeal also agreed with the High Court that the second SPA was void pursuant to section 24(b) of the Contracts Act 1950 because it deprived the government of revenue. The Court of Appeal held that the second SPA was a void instrument as stipulated under section 340(2)(b) of the National Land Code.

However, the Federal Court had a contrary view and held that the second SPA was not void merely because it contravened the statutory provisions. The relevant paragraph of the judgment is being reproduced herein for easy reference:

> '[117] Having carefully considered the authorities cited by the parties, we are inclined to agree with the contention of learned counsel for the first defendant that the second SPA is not void. We agree with the view that the courts should be slow in striking down commercial contracts on the grounds of illegality. The compliance with the Stamp Act 1949 and the Real Property Gains Tax 1976 are not the pre-requisite for the second SPA to be enforceable. There is no prohibition under the two Acts to preclude the first defendant from acquiring rights to the subject land. The Stamp Act 1949 provides a penalty for breach of its provisions. Similarly, under the Real Property Gains Tax Act 1976 there are penalties for breach of its provision. In addition, it is provided that tax due and payable may be recovered by the government by civil proceedings as a debt to the

government. The object of the two Acts is to raise revenue. There is therefore no sufficient nexus such as would satisfy the test laid down in *Curragh Investment Ltd*. The first defendant's infringement of the two Acts therefore did not prevent it from suing on the contract which is legal.

[118] In addition, we find that the test laid down by Lord Toulson in *Patel* that is to say, the trio considerations, is a sensible one, which we should follow. Applying the test to the facts of this case, we find that it is an overkill for the first defendant to lose the subject land for the infringement of the two Acts which is punishable by a fine upon conviction.

[119] The final issue for our determination is whether the second SPA is an instrument for the purpose of s 340(2)(b) of the Code.

[120] The High Court held that as the second SPA is void *ab initio* pursuant to s 24(b) of the Contracts Act 1950, the transfer of the subject land from the second defendant to the first defendant was obtained by means of a void instrument, which in turn renders the title of the first defendant defeasible pursuant to s 340(2)(b) of the Code.

[121] In view of our finding that the second SPA is not void we do not find it necessary to deal with this issue.'

Subsequently, the trio consideration enunciated in the case of *Patel v. Mirza* was also adopted and applied by our Court of Appeal in the case of *Public Bank Bhd v. Ria Realiti Sdn Bhd.* The relevant passage of the judgment is being reproduced herein for reference:

'[63] ... our courts ... have generally held that in order to invoke s 66, a party must not have knowledge of the illegality. This strict approach is no doubt similar to the pre-*Patel v. Mirza* (*supra*) traditional approach in common law where a party that is *in pari delicto* is totally barred from enforcing the terms of a void or illegal contract or otherwise obtaining relief under it. But now, even in respect of enforcement of an

agreement tainted with illegality, the flexible approach introduced by *Patel v. Mirza* (*supra*), affords relief to the less culpable party in certain circumstances.'

FEDERAL COURT CASE OF *TRIPLE ZEST TRADING & SUPPLIES V. APPLIED BUSINESS TECHNOLOGIES SDN BHD*[46]

Subsequent to the Federal Court case of *Liputan Simfoni Sdn Bhd*, the Federal Court was tasked with the responsibility to determine the issue of illegality in the judgment of *Triple Zest Trading & Suppliers v. Applied Business Technologies Sdn Bhd* again, but this time around the Federal Court did not refer and take into account the trio consideration principle laid down by the cases of *Patel v. Mirza* and *Liputan Simfoni Sdn Bhd.* This seems to be a departure from the approach taken by *Liputan Simfoni Sdn Bhd.*

The background facts of the case involved the first appellant ('A1'), a family-owned company whose directors were the second and third appellants ('A2' and 'A3'). A2 was the mother of A3 and one Mumtaz Shafinaz ('Mumtaz'). A2 and Mumtaz were the co-owners of two parcels of land ('the lands'). A1 needed funds for its business and approached the respondent ('R') – a general trading company dealing in petroleum products, construction works and information technology but which was not a licensed moneylender – for an RM800,000 loan. R agreed to lend the said sum provided it was repaid within one month together with a further RM800,000 as an 'agreed profit'. In the loan agreement signed between the parties, A1 agreed to secure the loan by providing R with A2 and A3's personal guarantees that the loan would be repaid as well as depositing the title deeds to the lands with R, along with four undated cheques, each for the sum of RM400,000, issued from A1's current account in favour of R. When A1 defaulted in repaying the loan, R sued the appellants and Mumtaz for, *inter alia*, an order that the lands be transferred to R; alternatively, an order that the lands be auctioned off to pay back the principal sum and 'agreed profit' owed to R. In their defence, the appellants pleaded that they

never consented to the 'agreed profit' of RM800,000, that the entire transaction was an illegal moneylending transaction, that R exercised undue influence on A2 and A3 into signing the personal guarantees and that Mumtaz had nothing to do with the loan agreement and had never pledged the lands as security for the loan.

Among other things, the High Court held that the transaction was not an illegal moneylending transaction as the evidence did not show that R had advertised, announced or held itself out in any way as carrying on the business of moneylending. The appellants appealed to the Court of Appeal ('COA') against the trial court's whole decision, whilst R appealed against part of the decision, which is the refusal to order the transfer or auction of the lands. In the COA, the appellants argued, *inter alia*, that although they had alleged in their pleadings that R was a moneylender – and thereby triggered the rebuttable presumption under s 10OA of the Moneylenders Act 1951 ('the MA') against R that it was a moneylender – R had never rebutted that presumption at trial. The COA, however, found that R had rebutted the presumption and that because R's loan to the appellants was a 'friendly loan' under which no interest ought to be chargeable, R was only entitled to recover the principal loan sum of RM800,000, but not the 'agreed profit' sum, together with interest thereon at 4% from the date of the High Court's judgment until date of realisation. The COA dismissed R's appeal and ordered it to return the title deeds of the lands to A2 and Mumtaz. Arising thereof, the appellants were granted leave to file the instant appeal against the COA's decision.

Abdul Rahman Sebli CJ (Sabah and Sarawak), in delivering the judgment, stated:

> '[34] The precedent that the Court of Appeal set was that an unlicensed moneylender can recover the principal loan sum but not the interest. Although less formidable than the precedent set by the High Court, the precedent set by the Court of Appeal is no less disturbing as it legitimises

> illegal moneylending by allowing illegal moneylenders to recover the principal loan amount in spite of the illegality of the transaction.'

The Federal Court adopted the legal maxim of *ex turpi causa non oritur actio* (no action will arise from a wrong done) and held that the trite principle was that a loss should lie where it fell when an agreement was found to be illegal. The 'agreed profit' in the instant case was caught by paragraphs (a), (b) and (e) of section 24 of the Contracts Act 1950 ('the CA') in that it was a 'consideration' that was forbidden by law, was of such a nature that, if permitted, would defeat any law and was one which the court regarded as immoral or opposed to public policy. The unlawfulness of the 'consideration' thus rendered the loan agreement in the instant case void under section 24 of the CA. The court would not assist those who came before it with unclean hands, and the remedy of restitution under section 66 of the CA would not be available to such litigants. The remedy under section 66 was only available where the contract was discovered to be void or when it became void and not where it was void *ab initio* as was the case with the loan agreement in the instant case.

It is the author's humble opinion for the sake of consistency and uniformity in the judiciary, the Federal Court in *Triple Zest Trading & Suppliers* should have adopted the trio consideration approach propounded by *Liputan Simfoni Sdn Bhd.* Had the Federal Court applied the trio consideration, the outcome would have been different. There is a likelihood the Federal Court would have allowed the respondent to recover the principal loan sum of RM800,000. Disallowing the refund of the principal loan sum to the respondent would be tantamount to '**an overkill**'.

CONCLUSION

As can be observed from the above case laws, there seems to be a lack of consistency and even some confusion in the courts' application of restitution under section 66 of the Contracts Act 1950. This inconsistency could perhaps be due to the complexity of this area of law. Ultimately, what is most important is to strike justice in each peculiar, different cases and

the way forward to achieve this is to adopt the trio consideration enunciated by *Patel v. Mirza*. Whatever the end result, the ultimate judgment to be handed down by the court must be proportionate to the illegality, bearing in mind that punishment is a matter for the criminal courts.

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*Messrs KF Ee & Co.

Endnotes:

[1] Visu Sinnadurai, *Law of Contract* (3rd edn, LexisNexis, 2003) 30.

[2] *Ibid* 33.

[3] *Ibid* 40.

[4] *Arumugan v. Somasundram* (1934) FMSLR 322.

[5] Sinnadurai (n 1) 375.

[6] [1968] CLJU 38; [1969] 1 MLJ 47.

[7] [1990] 1 CLJ Rep 57.

[8] [1999] 2 CLJ 997.

[9] Sinnadurai (n 1) 379.

[10] (1978) 139 CLR 410, 413.

[11] [1991] 2 CLJ Rep 453.

[12] [1982] 2 MLJ 31.

[13] [2020] 1 CLJ 162.

[14] Sinnadurai (n 1) 373.

[15] [1986] CLJ Rep 64.

[16] Low Weng Tchung, *The Law of Restitution and Unjust Enrichment in Malaysia* (LexisNexis, 2015) 244.

[17] (1922) LR 50 IA 69, AIR 1922 PC 403, (1923) 1 Madras LJ 489, PC.

[18] Identical to section 66 of the Malaysian Contracts Act 1950.

[19] [1969] CLJU 5; [1970] 1 MLJ 82.

[20] [1960] CLJU 169; [1981] 1 MLJ 14.

[21] [1982] 2 MLJ 114.

[22] Gareth Jones, *Goff & Jones The Law of Restitution* (Sweet & Maxwell, 4th edn, 1993) 17.

[23] (1947) LR 74 IA 295, AIR 1948 PC 56, (1948) 2 Madras LJ 1, PC.

[24] (1943) LR 70 IA 35, AIR 1943 PC 34, (1943) 2 Madras LJ 369, PC.

[25] [1967] CLJU 220; [1967] 2 MLJ 9.

[26] Low (n 16) 282.

[27] [1976] CLJU 181; [1977] 1 MLJ 91.

[28] [1995] 4 CLJ 300.

[29] *Ibid* at pp 307–308.

[30] [1999] 2 CLJ 997.

[31] *Ibid* at pp 1015–1016.

[32] [2019] 1 CLJ 183.

[33] (1775) 1 Cowp 341.

[34] Sinnadurai (n 1) 492.

[35] [1979] CLJU 96; [1980] 1 MLJ 21.

[36] [1980] CLJU 132; [1981] 1 MLJ 219.

[37] Sinnadurai (n 1) 503.

[38] [1996] 3 CLJ 494.

[39] [1973] CLJU 99; [1973] 2 MLJ 154.

[40] [2014] 3 CLJ 141.

[41] Low (n 16) 378.

[42] [2021] 3 CLJ 772.

[43] Sinnadurai (n 1) 372.

[44] [2016] UKSC 42.

[45] [2019] 1 CLJ 183.

[46] [2023] 10 CLJ 187.