Good faith: Is English law swimming against the international tide?

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The general obligation of good faith in the performance of contractual obligations is widely recognised and accepted overseas both in civil law jurisdictions and also now in most common law jurisdictions. Traditionally, however, the English courts have been reluctant to embrace good faith performance as a general prerequisite in commercial contracts and hence have been perceived as "swimming against the international tide". In possibly the most controversial first instance decision on English contract law for many years, Leggatt J (as he then was) in Yam Seng v International Trade Corp *(2013) underscored that English commercial law is out of step with other major jurisdictions and went on to hold that good faith is a concept that can be used to imply specific duties. This paper presents (1) an overview of the position in civil law jurisdictions and common law jurisdictions (including Canada); (2) a high-level analysis of English case law developments since* Yam Seng*, including* Bates v The Post Office *(2019); and (3) a consideration of the course that English law may plot in the future, particularly following the appointment, effective 2020, of Leggatt LJ to the Supreme Court.*

I. INTRODUCTION

I am greatly honoured to have been asked by Professor Andrew Serdy of The Institute of Maritime law in Southampton to deliver the 2019 Donald O'May Lecture, the 37th in the series since its inauguration. I did not know Mr O'May personally, as he passed away in 1988, when I was still a "baby junior" at the shipping Bar. However, I am aware of his strong reputation within Ince & Co and the shipping industry generally as a brilliant insurance lawyer and also of his close association with and support of the University of Southampton. I am told that he held strong opinions, but no one could predict on which side of the divide he would stand on the issues I would like to discuss in this paper. These issues concern the role of good faith in English law and whether English law should align itself with developments in the rest of the common law world and elsewhere in recognising a general duty of good faith in the performance of contracts.

* QC. International Arbitrator and Joint Head of Chambers of the 36 Group. This is the text (revised and updated to 31 January 2020) of the 37th Donald O'May lecture, delivered on 6 November 2019. I have greatly benefited from discussing the topic with Richard Firth, a retired Senior Consultant with Linklaters LLP Hong Kong and formerly a legal director at Barclays Capital and Citigroup. I also wish to extend my particular thanks to Hasan Tahsin Azizagaoglu, a PhD student with the IML and Southampton Law School, for his excellent research assistance; and also to Asteropi Chatzinikola, a Senior Status law student at Queen Mary University of London, for her valuable editorial input.

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The title of my lecture, "Good faith: is English law swimming against the international tide?", has been inspired by the seminal decision of Leggatt J (as he then was) in *Yam Seng v International Trade Corp*[1] in 2013. In that case, the judge observed that this jurisdiction would appear to be swimming against the tide in refusing explicitly to recognise a general obligation of good faith in the performance of contracts. I would like to examine in this paper the extent to which this remains true and the extent to which such a position is defensible.

II. CONTINENTAL CIVIL LAW

Express duties of good faith are frequently written into civil codes and are to be found, for example, in the civil codes of Belgium, the People's Republic of China,[2] Denmark, France, Germany, Greece, the Netherlands, Turkey and the UAE.[3]

Let us take as an example the newly revised French Civil Code, which came into force on 1 October 2016. Article 1104 states: "Contracts must be negotiated, made and performed in good faith. This is a matter of public policy".[4] You will note that the French doctrine of good faith extends beyond supporting contracts which have already been made and applies also to the negotiation and formation of contracts. That is something which is not a usual feature in common law jurisdictions.

The German model incorporates good faith as a principle governing the interpretation of contracts (under the German Civil Code, the *Bundesgezetsbuch* (BGB), Art.157) as well as performance obligations (under BGB, Art.242).

A huge volume of litigation has been generated by Art.242. An illustration of the width of the practical application of Art.242 is the *Reichsmark* case[5] in 1923, which concerned enforcement of a payment obligation secured by a mortgage incurred before the outbreak of the First World War and before the onset of massive inflation. The court refused to allow the debtor to discharge its obligation by paying the nominal value of the debt in paper marks pursuant to the prevailing currency statute. Relying on Art.242, the court held that the debtor could not in good faith discharge the obligation expressed in nominal value as set out in the currency statute and so the statute had to be disregarded insofar as it conflicted with the good faith principle. In November 1923, one gold mark was equivalent to 522 billion paper marks. The court concluded that it had jurisdiction to determine a new exchange rate.

English lawyers may regard the width of the above application of the good faith principle with a degree of disquiet.

1. [2013] EWHC 111 (QB); [2013] 1 Lloyd's Rep 526.
2. Chinese law draws upon the Dutch, German and Portuguese Civil Codes. See Liang Huixing, *The Draft Code of the People's Republic of China* (Martinus Nijhoff, 2010), xxv–xxvii. The Contract Law of the People's Republic of China promulgated in 1999 requires parties to observe good faith as a general principle, Art.6 providing that "parties should abide by the doctrine of good faith when exercising their rights or fulfilling their obligations". This principle is retained in the new Draft Code.
3. The UAE Civil Code, Art.246(1) provides that "The contract must be performed in accordance with its contents and in a manner consistent with the requirement of good faith".
4. "Les contrats doivent être négociés, formés et exécutés de bonne foi. Cette disposition est d'order public."
5. RGZ 107:78 (28 November 1923).

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EU Directives also make reference to the principles of good faith. Examples of domestic legislation implementing such Directives are collated in the current edition of *Chitty on Contracts*: they include the requirement of good faith in the test for unfair terms in consumer contracts under the Directive of 1993 (now implemented in the Consumer Rights Act 2015) and the principle of good faith in commercial transactions in settling the information which a supplier must provide to a consumer prior to conclusion of a contract under the Financial Services Distance Marketing Directive 2002.[6] In these respects, a limited degree of infusion of the civil law principle of good faith has already taken place.

III. COMMON LAW OUTSIDE ENGLAND AND WALES

Putting to one side civil law traditions, what about the position in the common law jurisdictions other than England and Wales?

United States

In the United States, the *Restatement (2nd) of Contracts* (1981), at s.205, provides that "every contract imposes on each party a duty of good faith and fair dealing in its performance and enforcement". Note that s.205 does not extend to the negotiation of contracts. The editorial comment to s.205 explains the meaning of "good faith" as follows: "Good faith performance or enforcement of a contract emphasises faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a variety of types of conduct characterised as involving 'bad faith' because they violate community standards of decency, fairness or reasonableness." Section 205 was hailed by Professor Robert Summers, an internationally acclaimed academic at Cornell University and joint author of the Uniform Commercial Code, as "one of the truly major advances in contract law during the past 50 years …".[7]

According to this explanation, good faith has two aspects: (a) adherence to reasonable commercial standards of fair dealing and (b) faithfulness to the agreed common purpose of the contract and to the reasonable expectations of the parties arising from it.

The Uniform Commercial Code also provides expressly (in s.1.203) that "every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement".

The doctrine of good faith performance has been recognised in the US for over a century.

An illustration of the doctrine in practice which suffices to give a flavour is a New York case decided in 1938, *Goldberg 168-05 Corp v Levy*.[8] That case involved the lease of business premises where the tenant operated a clothes store. The tenant had a contractual

6. Hugh Beale (ed), *Chitty on Contracts: Volume 1: General Principles*, 33rd edn (Sweet & Maxwell, London, 2018; 1st supplement to 33rd edn (2019).

7. Robert S Summers, "The General Duty of Good Faith—Its Recognition and Conceptualization" (1982) 1195 *Cornell Law Faculty Publications* 810.

8. (1938) 170 Misc 292; 9 NYS 2d 304.

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right to cancel the lease if the total sales from the premises in any calendar year were less than *c.*$100K. The tenant sought to cancel the lease on the basis that the previous year's sales from the premises were less than that figure. The tenant also had another clothes store nearby. The landlord alleged that the tenant had deliberately diverted sales from the leased premises to its other store for the sole purpose of bringing the turnover below the specified figure and thereby laying the basis for a cancellation of the lease. The court held that the tenant's conduct, if proved, would be a violation of the duty of good faith and fair dealing which exists in every contract.

Australia

The doctrine of good faith performance is also recognised in Australia. In 1991, Lord Steyn wrote extrajudicially an article entitled "The role of good faith and fair dealing in contract law: a hair-shirt philosophy?".[9] In the following year, the New South Wales Court of Appeal decided the case of *Renard Constructions (ME) Pty v Minister for Public Works*[10] and concluded that good faith and fair dealing in the performance of contracts is "in these days the expected standard",[11] anything less being contrary to prevailing community expectations.

There is now a body of case law in Australia flowing from that decision. An obligation to negotiate in good faith has also been upheld at the appellate level in Australia in *United Group Rail Services v Rail Corp of NSW*,[12] a decision which strongly influenced Teare J in our jurisdiction to uphold a clause requiring time-limited good faith discussions in *Emirates Trading Agency LLC v Prime Mineral Exports Pte Ltd*.[13]

Scotland

Scottish law also appears to recognise a broad principle of good faith and fair dealing: *Smith v Bank of Scotland.*[14]

IV. A CANADIAN CONTRIBUTION TO ENGLISH LAW?

In his authoritative 2009 Hamlyn Lectures, entitled *Widening Horizons: The Influence of Comparative Law and International Law on Domestic Law*,[15] Lord Bingham of Cornhill commented on the wisdom of considering experiences "from a country as like our own as Canada". It is therefore instructive to turn to the recent ruling of the Supreme Court

9. (1991) 6 Denning LJ 131. It is relevant to recall that Lord Steyn was an outstanding comparative lawyer, having been not only a Lord of Appeal in Ordinary (1995–2005) but also having previously practised Roman-Dutch law in South Africa for some 15 years.
10. (1992) 26 NSWLR 234; 33 Con LR 72 (NSWCA).
11. 33 Con LR 72, 113 (Priestley JA).
12. [2009] NSWCA 177; 127 Con LR 202.
13. [2014] EWHC 2104 (Comm); [2014] 2 Lloyd's Rep 457; [2015] 1 WLR 1145.
14. 1997 SC (HL) 111, 121.
15. Thomas H Bingham, *Widening Horizons: The Influence of Comparative Law and International Law on Domestic Law: The Hamlyn Lectures* (CUP, Cambridge, 2010), 12.

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of Canada in *Bhasin v Hrynew.*[16] In that case, the Supreme Court held that there is a general organising principle of good faith in the performance of contracts and that there is a common law duty which applies to all contracts to act honestly in the performance of contractual obligations. The Supreme Court acknowledged that the principle of good faith must be applied in a manner that is consistent with the commitments of the common law of contract, which is generally to place considerable weight on the freedom of the contracting parties to pursue their individual self-interest.

It is of interest that the Court[17] and academics in Canada who have commented upon this decision, have expressed the view that recognition of such a general organising principle will promote certainty and give coherence to the law. As one commentator has expressed it, "The effect of the new organising principle is that a number of disparate 'heads of recovery' are now brought within a powerful and useful analytical framework. In such a framework, similarities (and differences) can be explored and the development of the law made more fruitful."[18]

Let me tell you a little more about the facts in *Bhasin*. Mr Bhasin ("B") was an "enrolment director" who worked for a company called Can-Am, selling savings plans under a commercial dealership agreement. Mr Hrynew ("H") was another director, who also worked for Can-Am on the same basis. H coveted B's business. Can-Am was required by the Alberta Securities Commission to appoint a compliance officer. Can-Am, working with H and against B, appointed H as its compliance officer, falsely telling B, who had objected strenuously to the appointment, that H's appointment was required by the Commission. B's objections were based on his fear that, with the information H would now have about his business, H could take over B's business. It was B's refusal to allow H access to his confidential information that led to Can-Am refusing to renew B's contract. In the result, H substantially took over B's business.

Cromwell J, giving the unanimous judgment of the Supreme Court, held that Can-Am's breach of contract consisted of its failure to be honest with B in its contractual performance throughout the period leading up to the exercise of the non-renewal clause, both with respect to its own intentions and with respect to H's role, and that it was therefore liable in damages calculated on the basis of what B's economic position would have been had Can-Am fulfilled that duty.

The Court conducted a survey of the current position in relation to good faith in the common law world and noted, in relation to England, that the piecemeal approach adopted by English judges to demonstrated problems of unfairness (as noted by Bingham LJ in *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd*[19]) "often fails to take a consistent or principled approach to similar problems";[20] further, that "foreclosing some incremental development of the law at the level of principle"

16. 2014 SCC 71; [2014] 3 SCR 495. I am most grateful to Professor Stephen Smith, James McGill Professor of Law at McGill University, Montreal, Quebec for highlighting the importance of this case in the present context. Professor Smith has published extensively on contract law, including on this topic. See: www.mcgill.ca Stephen Smith.

17. 2014 SCC 71; [2014] 3 SCR 495, [60].

18. "The Obligation to Perform in Good Faith: Comment on *Bhasin v Hrynew*" (2015) 56 Can Bus LJ 395, 404.

19. [1989] 1 QB 433.

20. *Bhasin* 2014 SCC 71; [2014] 3 SCR 495, [42].

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goes beyond what prudent caution requires and demonstrates "an almost 'perverted pride'" in the law's failings.[21]

Key to the ruling of the Canadian Supreme Court leading to the recognition of the general organising principle of good faith in contractual performance were the following considerations, none of which you may think are alien to English lawyers or at odds with principles which we recognise:

"Commercial parties reasonably expect a basic level of honesty and good faith in contractual dealings. While they remain at arm's length and not subject to the duties of a fiduciary, a basic level of honest conduct is necessary to the proper functioning of commerce. The growth of longer term, relational contracts that depend upon an element of trust and co-operation clearly calls for a basic level of honesty in performance, but even in transactional exchanges, misleading or deceitful conduct will fly in the face of the expectations of the parties.[22]

… enunciating a general organising principle of good faith and recognising a duty to perform contracts honestly will help bring certainty and coherence to an area of the law in a way that is consistent with reasonable commercial expectations.[23]

An organising principle is not a free standing rule but rather a standard that underpins and is manifested in more specific legal doctrines and may be given different weight in different situations … It is a standard that helps to understand and develop the law in a coherent and principled way.[24]

The organising principle of good faith exemplifies the notion that, in carrying out his or her own performance of the contract, a contracting party should have appropriate regard to the legitimate commercial interests of the contracting partner. While 'appropriate regard' for the other party's interest will vary depending on the context of the contractual relationship, it does not require acting to serve those interests in all cases. *It merely requires that a party not seek to undermine those interests in bad faith*. This general principle has strong conceptual differences from the much higher obligations of a fiduciary. Unlike fiduciary duties, good faith performance does not engage duties of loyalty to the other contracting party or a duty to put the interests of the other contracting party first.[25]

This organising principle of good faith manifests itself through the existing doctrines … Generally, claims of good faith will not succeed if they do not fall within these existing doctrines. But we should also recognise that the list is not closed. The application of the organising principle of good faith to particular situations should be developed where the existing law is found to be wanting and where the development may occur incrementally in a way that is consistent with the structure of the common law and gives due weight to the importance of private ordering and certainty in commercial affairs.[26]

The approach of recognising an overarching organising principle but accepting the existing law as the primary guide to future development is appropriate in the development of the doctrine of good faith. Good faith may be invoked in widely varying contexts and this calls for a highly context-specific understanding of what honesty and reasonableness in performance require so as to give appropriate consideration to the legitimate interests of both contracting parties. For example, the general organising principle of good faith would likely have different implications in the context of a long-term contract of mutual co-operation than it would in a more transactional exchange.[27]

21. *Ibid*, [59].
22. *Ibid*, [60].
23. *Ibid*, [62].
24. *Ibid*, [64].
25. *Ibid*, [65] (emphasis added).
26. *Ibid*, [66]. Interestingly a piecemeal approach is being advocated.
27. *Ibid*, [69]. This draws attention to a justification for difference in treatment of relational contracts. Such a distinction also features and has developed in English law.

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The principle of good faith must be applied in a manner that is consistent with the fundamental commitments of the common law of contract which generally places greater weight on the freedom of contracting parties to pursue their individual self-interest. In commerce, a party may sometimes cause loss to another—even intentionally—in the legitimate pursuit of economic self-interest. … The development of the principle of good faith must be clear not to veer into a form of *ad hoc* judicial moralism or "palm tree" justice. In particular, the organising principle of good faith should not be used as a pretext for scrutinising the motives of contracting parties.[28]"

Tying the organising principle to the existing law aims to mitigate the concern that any general notion of good faith in contract law may undermine certainty in commercial contracts. In my view this approach strikes the correct balance between predictability and flexibility:

"The new duty of honest performance (which is a manifestation of the general organising principle) should not be thought of as an implied term but a general doctrine of contract law that imposes as a contractual duty a minimum standard of honest contractual performance. The parties are not free to exclude it.[29]

The duty of honest performance has similarities with the existing law in relation to civil fraud and estoppel, but it is not subsumed by them. Unlike promissory estoppel and estoppel by representation, the contractual duty of honest performance does not require that the defendant intend that his or her representation be relied on and is not subject to the uncertainty of whether estoppel can be used to find an independent cause of action.[30]"

In the period of nearly five years since *Bhasin* was decided, there has been no sign that a floodgate has been opened to the recognition of new types of claim, and Canadian academic commentators have received the decision positively. One commentator, writing in 2016,[31] has observed that the case law post-*Bhasin* reveals that Canadian courts have upheld the view that a duty of honest contractual performance represents only a modest change to the law of contract; and that, while lawyers have made efforts to expand the scope of the doctrine, these arguments have largely been rejected by the courts. An example of the current approach is to be found in the recent decision of the Ontario Court of Appeal in *Bank of Montreal v Javed*.[32]

Javed involved an action by the Bank of Montreal on a guarantee provided by the defendants. One of the defendants, Mr Shah, together with his co-defendant, provided a guarantee to the bank to secure a business loan for their company. Ultimately, Shah resigned from the company and the company defaulted on the loan. The bank demanded payment and commenced an action against Shah to enforce its guarantee. The court granted judgment against Shah. On appeal, Shah argued (amongst other things) that the bank's conduct following the execution of his guarantee was unconscionable. He relied on the fact that the Bank had refused his post-resignation request to provide details of the company's business account information as unconscionable performance of its contract.

28. *Ibid*, [70–71].
29. *Ibid*, [74–75].
30. *Ibid*, [88].
31. Marco P Falco, "Good Faith and Reasonableness: Two Limits on Canadian Freedom of Contract" (2016) *Business Law Today* 1.
32. 2016 ONCA 49.

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Some paragraphs of the decision in *Bhasin* had drawn an analogy between honest contractual performance and the doctrine of unconscionability. In *Javed*, Mr Shah argued that *Bhasin* extended the test for unconscionability so as to include an assessment of a party's performance of its obligations under the agreement. The Court of Appeal had no difficulty in rejecting that argument, and there is no sign that the floodgates have been opened as a result of confirmation of the existence of an organising principle of good faith in the performance of contracts.

V. THE INTERNATIONAL POSITION

Finally, and before turning to a review of English law, we should not overlook the fact that at an international level there are various soft law instruments (such as the UNIDROIT Principles of International Commercial Contracts, Art.1.7 of which provides for a mandatory non-excludable duty of good faith and fair dealing) as well as Conventions (including the Vienna Convention on the International Sale of Goods 1980, Art.7), which recognise a duty of good faith and fair dealing on the parties.

Further, many of the same litigants that come before the Commercial Court may and do choose to arbitrate their disputes under Rules which give express recognition to duties of good faith. The London Court of International Arbitration (LCIA) Rules (Arts 14.5 and 32.2) and Lloyd's Standard Salvage and Arbitration Clauses (cl 2(b)) contain an express obligation on the parties and the Tribunal to operate the provisions of the arbitration agreement in good faith. Likewise, the Swiss Rules and those of the Belgian Centre for Arbitration and Mediation (CEPANI).

One of the key principles of the International Bar Association (IBA) Rules on the Taking of Evidence in International Arbitration is that "each party shall act in good faith" in the taking and presentation of evidence. That provision is not merely aspirational, because there is a sanction for breach of that duty in Art.9.7 of the IBA Rules (including in costs).

If English law is to continue to serve the international marketplace, it cannot remain impervious to ideas of good faith that have gained wide acceptance internationally.

VI. ENGLISH LAW[33]

Outside the sphere of insurance contracts and contracts between fiduciaries, the general approach of the English judiciary has been one of scepticism, if not hostility to the recognition of a general principle of good faith in the performance of commercial contracts. Lord Steyn, writing extra-judicially in 1997, has observed that this hostility is not bred from any great familiarity with the way the principle works but is nonetheless profound.[34]

33. See generally Richard Cumbley and Peter Church, *Practical Law Practice Note: Contracts: Good Faith*, uk.practicallaw.thomsonreuters.com/w-003-1201.

34. Lord Steyn, "Contract Law: Fulfilling the Reasonable Expectations of Honest Men" (1997) 113 LQR 433.

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Lord Steyn said that his impression was that the basis of the hostility was suspicion about what good faith means. He added this:[35]

"If it were a wholly subjective notion, one could understand the scepticism. If it were an impractical and open-ended way of fastening contractual liability onto parties, it would deserve no place in international trade. But it is none of these things. While I accept that good faith is sometimes used in different senses, I have in mind what I regard as the core meaning. Undoubtedly good faith has a subjective requirement: the threshold requirement is that the party must act honestly. This is an unsurprising requirement and poses no difficulty for the English legal system. But good faith additionally sets an objective standard, viz the observance of reasonable commercial standards of fair dealing in the conclusion and performance of the transaction concerned. Used in this sense judges in the greater part of the industrialised world usually have no great difficulty in identifying a case of bad faith. It is not clear why it should perplex judges brought up in the English tradition."

The first modern case to consider in depth the issue of whether English law should recognise a general duty to perform contracts in good faith is Leggatt J's decision in *Yam Seng*.[36]

The facts can be stated simply. The claimant had agreed to distribute "Manchester United" fragrances produced by the defendants in territories in the Far East. Although the football team was very popular in those territories, the fragrances were unfortunately not, and the parties fell out, accusing each other of breaches of the Distribution Agreement, some of which the claimant relied upon to justify terminating the contract.

After a masterly review of the international landscape in relation to good faith, the judge concluded that English law had not yet reached the stage where it was ready to recognise a requirement of good faith as a duty implied by law into all commercial contracts.[37] Nevertheless, he considered that there was no difficulty, following the established methodology of English law for the implication of terms in fact, in implying such a duty based on the presumed intention of the parties. He said:[38]

"The modern case law on the construction of contracts emphasised that contracts … are made against a background of unstated shared understandings which informed their meaning. …

A paradigm example of a general norm which underlies almost all contractual relationships was an expectation of honesty. …

Another aspect of good faith … is … fidelity to the parties' bargain. …

Although [the requirements of good faith] are sensitive to context, the test of good faith is objective in the sense that it depends not on either party's perception of whether particular conduct is improper but on whether in the particular context the conduct would be regarded as commercially unacceptable by reasonable and honest people. The standard is thus similar to that described by Lord Nicholls in … *Royal Brunei Airlines Sdn Bhd v Tan*.[39]

Understood in the way I have described, there is … nothing novel or foreign to English law in recognising an implied duty of good faith in the performance of contracts."

35. *Ibid*, 438.
36. [2013] EWHC 111 (QB); [2013] 1 Lloyd's Rep 526.
37. *Ibid*, [131].
38. *Ibid*, [133], [135], [139], [144], [145].
39. [1995] 2 AC 378, 389–390.

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He concluded that the traditional English hostility to a doctrine of good faith in the performance of contracts, to the extent it still exists, is misplaced.[40]

The judge was prepared to uphold two implied terms on the facts and to find that they had been broken: (a) an implied term that D would not knowingly give false information to C on a matter of commercial importance to C during the performance of the contract, because such conduct would infringe the core expectation of honesty, and (b) an implied term not to approve a retail price for a product for a domestic market which was lower than the duty-free retail price for the product agreed with C (ie, a duty not to undercut duty-free prices).

Yam Seng has met with mixed reactions which have tended to polarise opinion as to the desirability of embracing good faith as a principle governing the performance of contracts. It has been cited with approval by the Court of Appeal in *Globe Motors Inc v TRW Lucas Varity Electrical Steering Ltd*,[41] as well as by the Singapore Court of Appeal in *The One Suites Pte Ltd v Pacific Motor Credit (Pte) Ltd*.[42] However, there have been many negative comments on the adoption of a good faith standard as a matter of routine into commercial contracts. In the Court of Appeal in *MSC Mediterranean Shipping SA v Cottonex Anstalt*,[43] Moore-Bick LJ has observed that "There is a real danger that if a general principle of good faith were established it would be invoked as often to undermine as to support the terms in which the parties have reached an agreement".[44] This was a decision on appeal from Leggatt J at first instance. In his recent Hirst lecture, Sir Christopher Clarke cited as an example of why English law remains good for business the fact that English courts have rejected a general duty of good faith in the performance of contracts, save in well-established circumstances such as insurance and partnership, coupled with a guarded but developmental approach to implying a duty of good faith in particular cases.[45] Leggatt LJ has also recently reiterated his stance from *Yam Seng* in *Sheikh Tahnoon Bin Saeed Bin Shakhboot Al Nehayan v Kent*.[46] We have a veritable clash of philosophical approaches amongst Titans.

One thing that cannot be doubted is that express clauses requiring good faith are encountered frequently in practice.

Express terms requiring good faith

In *Berkeley Community Villages Ltd v Pullen*,[47] the claimant was a property developer who agreed to assist the owners of some farmland to promote the land and try to obtain planning consent for residential development. It contained a clause which said "In all

40. [2013] EWHC 111 (QB); [2013] 1 Lloyd's Rep 526, [153].
41. [2016] EWCA Civ 396, [67].
42. [2015] SGCA 21.
43. [2016] EWCA Civ 789; 2016] 2 Lloyd's Rep 494.
44. *Ibid*, [45].
45. Sir Christopher Clarke, "London: the venue of choice for international disputes in the year ahead?", the Third Jonathan Hirst Memorial Lecture (20 May 2019), [56].
46. [2018] EWHC 333 (Comm).
47. [2007] EWHC 1330 (Ch).

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matters relating to this agreement the parties will act with the utmost good faith towards one another …". The developer spent a lot of time and effort in promoting the land and the land became more valuable as a result. However, the landowners decided to sell the land before planning consent had been obtained and before the developer became entitled to be paid a fee for his work. The developer applied to the court for an injunction to prevent the sale, arguing that the sale would be a breach of the clause requiring the parties to act with utmost good faith towards each other. Morgan J accepted that argument and granted the injunction. He construed the good faith clause as "imposing on the Defendants a contractual obligation to observe reasonable commercial standards of fair dealing in accordance with their actions which related to the Agreement and also requiring faithfulness to the agreed common purpose and consistency with the justified expectations of the claimant".[48] The judge was influenced by Australian and American sources in formulating the content of what good faith requires.

A case on the other side of the line was *Gold Group Properties Ltd v BDW Trading Ltd.*[49] It was an express term of the contract between the property developer and the owner that each of the parties should "at all times act in good faith towards the other and use all reasonable endeavours to ensure the observance of the terms of the agreement". The property developer failed to develop the land and was sued by the owner for damages for repudiatory breach. The developer argued that it was the owner that was in repudiatory breach of the express term of good faith by refusing to agree to any revision of the parties' agreement to take account of the fall in the property market. The judge (Stephen Furst QC, sitting as Deputy Judge of the High Court) found for the landowners, concluding that "good faith, whilst requiring the parties to act in a way that will allow both parties to enjoy the anticipated benefits of the contract, does not require either party to give up a freely negotiated financial advantage clearly embedded in the contract",[50] and he found for the landowners, holding that there had been no breach of the obligation to act in good faith by refusing to accept or negotiate on the basis of the developer's offer to delay development for two years or revise the revenue sharing agreement.

The approach of Morgan J in *Berkeley* was followed by Vos J in *CPC Group Ltd v Qatari Diar Real Estate Investment Co*[51] and that case was in turn cited with approval by Jackson LJ in *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust.*[52] In *Medirest*, the Court of Appeal had to consider the significance of an express term in a detailed contract for the supply of catering and cleaning services for a seven-year period by a contractor to an NHS Trust at one of its hospitals. The express term provided that "The Trust and the Contractor will co-operate with each other in good faith and will take all reasonable action as is necessary for the efficient transmission of information and instructions to enable the Trust … to derive the full benefit of the Contract". The Court of Appeal held that there had been no breach on the facts. As Beatson LJ observed, "care must be taken not to construe a general and potentially open ended obligation such as the obligation to co-operate or 'to act in good faith' as covering

48. *Ibid*, [97].
49. [2010] EWHC 1632 (TCC).
50. *Ibid*, [91].
51. [2010] EWHC 1535 (Ch).
52. [2013] EWCA Civ 200.

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the same ground as other, more specific provisions, lest it cut across those more specific provisions and any limitations in them".[53] Further, as the duty of good faith is heavily dependent on context, and in context the relevant term required the parties to act together honestly to achieve the two stated purposes, there had been no breach as there was no evidence of dishonesty.

An express duty of good faith in contractual performance was found to have been broken in a case decided in 2018, *Health & Case Management Ltd v Physiotherapy Network Ltd*.[54] The court reviewed the earlier cases that had considered express terms requiring good faith, and gave content to the express good faith term in the contract before it as requiring the claimant to "adhere to the spirit of the contract, to observe reasonable commercial standards of fair dealing and to be faithful to the agreed common purpose and act consistently with the justified expectations of the parties".

It can now be said that English law generally does recognise and will enforce express contractual duties of good faith in relational contracts, and that the court will give specific content to what good faith requires by reference to the context in which those contracts were concluded.

So far, so good.

VII. NEGOTIATION IN GOOD FAITH

What about promises to negotiate in good faith? Are such clauses enforceable?

In *Walford v Miles*,[55] Lord Ackner stated that:

> "the concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations. To advance that interest he must be entitled, if he thinks it appropriate, to threaten to withdraw from further negotiations or to withdraw in fact in the hope that the opposite party may seek to re-open negotiations by offering him improved terms. … How is the court to police such an agreement? A duty to negotiate in good faith is an unworkable in practice as it is inherently inconsistent with the position of a negotiating party."

That decision has been the subject of some trenchant criticism from legal scholars, including by Lord Steyn writing extra-judicially in 1997 in an article entitled "Contract Law: Fulfilling the Reasonable Expectations of Honest Men".[56] The Court of Appeal in *Petromec Inc v Petroleo Brasileiro SA Petrobras (No 3)*[57] distinguished *Walford v Miles* on the ground that there was no concluded contract in that case and held that a clause requiring parties to negotiate in good faith the reasonable extra costs of upgrading an oil rig was enforceable. Longmore LJ said that:[58]

53. *Ibid*, [154].
54. [2018] EWHC 869 (QB).
55. [1992] 2 AC 128, 138.
56. (1997) 113 LQR 433.
57. [2005] EWCA Civ 891; [2006] 1 Lloyd's Rep 121.
58. *Ibid*, [121].

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"It is not irrelevant that it is an express obligation which is part of a complex agreement drafted by City of London solicitors … It would be a strong thing to declare unenforceable a clause into which the parties have deliberately and expressly entered. … To decide that it has 'no legal content' … would be for the law deliberately to defeat the reasonable expectations of honest men …"

Agreements to negotiate in good faith have long been held enforceable in the US. They are also enforceable in Singapore (*HSBC v Toshin*[59]) and Australia.

In *United Group Rail Services Ltd v Rail Corp of NSW*,[60] the NSW Court of Appeal, after an extensive review of the English and Australian authorities, held that an obligation to negotiate in good faith was enforceable. The Court accepted that an agreement to agree was unenforceable, but this has to be contrasted with an agreement to undertake negotiations in good faith to settle a dispute under a contract, which was not incomplete, and which was sufficiently certain to be enforceable. The judge stressed that the difficulty of proving breach did not mean that the obligation lacked real content.

This reasoning was followed by Teare J in a case in which I was involved, *Emirates Trading Agency LLC v Prime Mineral Exports Pte Ltd*.[61] The judge concluded that the obligation to seek to resolve disputes by friendly discussions necessarily imported an obligation to seek to do so in good faith and that the obligation was enforceable. It was not uncertain, as it had an identifiable standard, namely fair, honest and genuine discussions aimed at resolving the dispute. Further, the judge held that enforcement of such an agreement was in the public interest. That case also has its supporters and detractors, depending upon which side of the good faith divide one stands.

Rosalina Investments Ltd v New Balance Athletic Shoes (UK) Ltd[62] is the latest case dealing the enforceability of an obligation to negotiate a renewal of a contract in good faith. On the facts it was held there was no viable claim for breach of an obligation to negotiate a renewal in good faith. One of the grounds for rejection of the claim was the statement of Lord Ackner in *Walford v Miles* that a duty to negotiate in good faith is inherently inconsistent with the position of a negotiating party.

VIII. NO EXPRESS TERM

What about the English law approach in cases where there is no express obligation to act in good faith? Would or should it have made a difference to the outcome of those cases already discussed (*Berkeley* etc) if there had been no express term to act in good faith? The view expressed by Leggatt J in a lecture delivered to the Commercial Bar Association in 2016 is that there would not necessarily have been a difference.[63] This is because an express clause requiring good faith does no more than express the normal expectation of the contracting parties. Leggatt J stated that:[64]

59. *HSBC Institutional Trust Services (Singapore) Ltd (trustee of Starhill Global Real Estate Investment Trust) v Toshin Development Singapore Pte Ltd* [2012] SGCA 48; [2012] 4 SLR 378.
60. [2009] NSWCA 177; 74 NSWLR 618.
61. [2014] EWHC 2104 (Comm); [2014] 2 Lloyd's Rep 457; [2015] 1 WLR 1145.
62. [2018] EWHC 1014 (QB).
63. Mr Justice Leggatt, "Contractual duties of good faith", Lecture to the Commercial Bar Association (18 October 2016).
64. *Ibid*, [24–27].

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"This is where I come to what I see as the real significance of the concept of good faith: why it matters. It involves what I think is quite a deep point about the nature of commerce and commercial law.

… There is something of a tendency of English commercial lawyers to view commerce as if it were a kind of Darwinian struggle in which everyone is trying to gain at the expense of those with whom they do business and where, even when parties have made a contract, that does no more than set limits on the pursuit of profit at the other party's expense. This view of contracting parties as adversaries may be encouraged by the experience we all have as lawyers dealing with litigation. By the time the parties have resorted to litigation, their relationship has often become decidedly adversarial and the adversarial nature of our legal process may also reinforce this perception.

This model of commerce and of contract … does not in my view correspond to commercial reality. My belief about this is based on my experience when I was a barrister in advising commercial clients and trying to understand the point of view of people who actually negotiate and perform commercial contracts … I believe it is a mistake to see contracting as an essentially adversarial activity. … The essence of trade and commerce is reciprocity which benefits both parties and makes each party better off. To achieve such mutual gain, the parties agree to co-operate with each other in various ways. Contract law facilitates such co-operation by giving it legal backing.

If contract law is to perform that function effectively, it is necessary to recognise that not all the shared understandings and expectations which contracting parties have and which are necessary to realise their joint aims are ever spelt out, or are capable of being spelt out, in their contractual document. For example, very few, if any, contracts, contain a clause by which the parties promise not to lie to one another: that is just something which is naturally taken for granted …"

He concludes in a manner which may reflect the approach that will be taken to good faith when Leggatt LJ (as he now is) has taken his seat in the Supreme Court, in 2020:[65]

"There is, I suggest, a case to be made for recognising an obligation of good faith in the performance of contracts as a default rule. Faithfulness to the agreed common purpose of the contract, adherence to reasonable commercial standards of fair dealing—these are values which protect the integrity of the process of contracting and promote its effectiveness. … such a default rule is likely to have the greatest value when applied to relational contracts, because it is the hallmark of such contracts that they involve expectations of co-operation and loyalty which are not, and in practice cannot fully be, articulated in the express terms of the contractual document."

At this stage, it is important to dispel a myth which is often seized upon by good faith sceptics as a reason for rejecting the idea that there should be an obligation of good faith in commercial contracts—good faith is not altruism and does not require a party to subordinate its own commercial interests to those of the other party to the contract. Good faith simply requires loyalty to the agreement—to the bargain.

Relational contracts

It is in the context of relational contracts that there have been significant developments on the highway of good faith since the decision in *Yam Seng*. A relational contract is one between parties whose relationship involves expectations of cooperation and loyalty and which are not (and perhaps cannot be) completely expressed in a formal document. Paradigm examples are contracts of employment. In *Yam Seng* it was suggested that some

65. *Ibid*, [30–31].

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Joint Venture agreements, Franchise Agreements and long-term distributorship agreements might also come into this category.

The Joint Venture agreement in *Bristol Groundschool Ltd v Intelligent Data Capture Ltd*[66] was characterised as a relational contract and the judge found that there was an implied term requiring good faith in its performance. That implied term was found to have been broken by C in secretly accessing D's database in anticipation of the termination of the JV and downloading material which D then continued to use to sell its training manuals.

In *D&G Cars Ltd v Essex Police Authority*[67] in 2015, the Essex Police authority used a private contractor to dispose of cars which had come into possession of the police. Under the terms of the agreement, the contractor was required to dispose of cars in accordance with instructions given by the police authority. The police gave instructions for one particular Land Rover Discovery to be completely crushed, but instead of doing that the contractor rebuilt it and began using it as a recovery vehicle in its own fleet. When the police found out, they terminated the contract. The issue was whether the termination was justified. The judge described the contract as a relational contract and held that it was an implied term that the contractor would perform it with honesty and integrity. He held that, even if the contractor had not been deliberately fraudulent, there had been a breach of the implied term which amounted to a repudiatory breach of contract.[68]

The most important recent decision to consider implied terms of good faith in the context of relational contracts is that of Fraser J in the *Bates v Post Office* litigation.[69]

The proceedings related to alleged defects in an electronic accounting system introduced across Post Office branches since the turn of the century. The claimants, including Mr Bates, were a group of around 550 individuals and companies, mainly sub-postmasters, responsible for running PO branches. They alleged that the accounting system caused unexplained shortfalls and discrepancies. The PO denied that the accounting system was at fault and pursued the sub-postmasters for the shortfalls, in some cases securing criminal convictions. The claimants sought damages for financial loss and other remedies based (inter alia) on the fact that the contracts with the PO were relational contracts and contained an implied duty of good faith.

Having reviewed the authorities, the court concluded that the concept of a relational contract is established in English law and that a duty of good faith is implied into those contracts. Transparency, cooperation, trust, and confidence are implicit in the implied duty of good faith.[70] In the judge's view, the duty goes beyond an obligation to act honestly and requires the parties to refrain from conduct which would be regarded as commercially unacceptable by reasonable and honest people.[71]

66. [2014] EWHC 2145 (Ch).
67. [2015] EWHC 226 (QB).
68. *Ibid*, [217].
69. *Bates v Post Office Ltd: Judgment (No.3) "Common Issues"* [2019] EWHC 606 (QB). Permission to appeal has been refused.
70. *Ibid*, [738].
71. *Ibid*, [711].

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The court gave a non-exhaustive list of factors relevant to whether a contract is a relational contract.[72] Key is whether there is an express term in the contract preventing a duty of good faith being implied. Other factors include whether there is a mutual intention for there to be a long-term relationship; whether there is a commitment to collaboration; whether there is a significant investment or substantial financial commitment by the parties and the exclusivity of the relationship. The judge found that the contracts before him were relational contracts and that this meant the contracts included an implied obligation of good faith.[73] He defined good faith as meaning that both parties must refrain from conduct which in the relevant context would be regarded as commercially unacceptable by reasonable and honest people. Transparency, cooperation, and trust and confidence are implicit within the implied obligation of good faith. The judge made clear why he considered the implied obligation of good faith went further than a duty to cooperate and a duty not to prevent performance (which terms were agreed would be implied into the contracts): "First, … simply because it is agreed by the parties that they would not inhibit or prevent one another does not amount to coming even close to the type of relationship considered to exist in a relational contract. Secondly, there is more to an obligation of good faith than necessary co-operation. Co-operation is part of it but it is not limited to co-operation."[74]

Of the 21 implied terms that the claimants had pleaded, the court agreed that most gave specific content to the duty of good faith, including an obligation to keep accurate records, to conduct a proper, full and fair investigation into any alleged shortfalls, not to conceal from the sub-postmasters any known problems in the accounting system and not to claim payment of losses without first establishing the fact of loss and investigating the cause.

The judge also made clear that his finding that the contracts were relational does not open the floodgates to an automatic and widespread application of an implied duty of good faith in all commercial relationships and that very specific characteristics are necessary before a commercial contract is categorised as a relational one.[75]

IX. CONCLUSION

Turning to the question posed at the beginning of this paper—Good faith: is English law swimming against the international tide?—my suggested answer is that English law is taking tentative steps towards changing its course and starting to flow with the international tide. If my surmise is correct, how should we view such a development?

The traditional approach of English law was described by Bingham LJ (as he then was) in *Interfoto v Stiletto*[76] as being one which committed to no overriding principle, but which develops piecemeal solutions in response to demonstrated problems of unfairness.

It is true that many of the doctrines with which we as English lawyers are familiar are directed to addressing perceived unfairness. Outside of the insurance and fiduciary

72. *Ibid*, [725].
73. *Ibid*, [738].
74. *Ibid*, [740].
75. *Ibid*, [721].
76. [1989] 1 QB 433.

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context where duties of good faith have long been part of the established fabric, the following principles have been developed over time in order to address demonstrated problems of unfairness.

First, it is now well established that, where a contract confers a discretion on one party and the exercise of that discretion may adversely affect the interest of the other party, the discretion must be exercised honestly and in good faith for the purpose for which it was conferred. You may recall the case of *The Product Star (No 2)*,[77] in which the Court of Appeal held that charterers had to exercise their discretion to divert the vessel in good faith. (Sir Andrew) Leggatt LJ (father of the present Leggatt LJ) said that,

"where A and B contract with each other to confer a discretion on A, that does not render B subject to A's uninhibited whim. … Not only must the discretion be exercised honestly and in good faith but having regard to the provisions of the contract by which it is conferred, it must not be exercised arbitrarily, capriciously or unreasonably".[78]

That principle is now very well established, finding expression in the decision of the Supreme Court in *Braganza v BP Shipping Ltd*[79] in which the Court approved the application of both limbs of the well-known reasonableness test in *Wednesbury*.[80]

However, the common law has retained its flexibility by carving out exceptions to a good faith principle which are thought not to be consistent with the interests of commerce. Thus, in a recent decision of Blair J in *Lehman Bros International Europe v Exxonmobil Financial Services BV*,[81] concerning a contractual discretion in the context of a financial instrument, the judge declined to apply the *Wednesbury* test. He said:[82]

"The contractual discretion in the present case is given to a commercial party to a contract with another commercial party on the wholesale financial markets where the decision is as to the valuation of securities in the case of default. The decision is one which can be (and may need to be) taken without delay and in which the non-defaulting party is entitled to have regard to its own commercial interests. In this kind of situation Braganza does not require the kind of analysis of the decision-making process that would be appropriate in the public law context."

The decision of the English courts to categorise termination clauses as something different from contractual discretions, and thus not subject to any requirement that they be exercised in good faith, is another example of the pragmatic approach by English law which in that instance limits any overarching principle of good faith.[83,84] A similar approach

77. *Abu Dhabi National Tanker Co v Product Star Shipping Ltd (The Product Star) (No 2)* [1993] 1 Lloyd's Rep 397.

78. *Ibid*, 404.

79. [2015] UKSC 17; [2015] 2 Lloyd's Rep 240; [2015] ICR 449; [2015] 1 WLR 1661.

80. *Associated Provincial Picture Houses Ltd v Wednesbury Corp* [1948] 1 KB 223.

81. [2016] EWHC 2699 (Comm).

82. *Ibid*, [287].

83. Depending on which side of the divide one is on, exercise of a termination right can be characterised in certain circumstances as "opportunistic" or stigmatised as "bad faith". See further: Jonathan Morgan, *Contract Law*, 2nd edn (Palgrave, 2015) and Philip Wood, *The Fall of the Priests and the Rise of the Lawyers* (Hart, Oxford, 2016).

84. See *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200; *Greenclose Ltd v National Westminster Bank Plc* [2014] EWHC 1156 (Ch); [2014] 2 Lloyd's Rep 169; and *Lomas v JFB Firth Rixson Inc* [2012] EWCA Civ 419; David Foxton QC, "A Good Faith Goodbye?

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to termination rights was taken by the Supreme Court of Canada in *Bhasin*,[85] where the right to terminate was not treated as a discretion and thus not subject to the principles applicable to discretions. However, the position should not to be taken as immutable under English law, because Leggatt J at first instance in *MSC v Cottonex*[86] suggested that the option to terminate a contract was not analytically different in principle from any other contractual discretion, and the same reason exists to imply a constraint on the decision maker's freedom to act purely in its own self-interest.

A second illustration of the piecemeal adoption by the English law of solutions to address unfairness is the principle of construction that prevents a party from taking advantage of its own wrong.[87]

Similarly, and although less far-reaching than good faith, for the reasons explained in *Bates v PO*, implied terms as to necessary cooperation and non-prevention of performance are among the armoury of terms that are commonly implied into contracts to prevent bad behaviour that does not conform with good faith.

In the same vein, there is also the well-established principle in the shipping context that notices of readiness (NORs) have to be given in good faith.[88]

And, of course, there is the terrain covered by the law on misrepresentation and deceit, as well as estoppel, which address many cases of injustice which a broader good faith principle might also address. You will no doubt be able to think of other examples, such as the principles relating to fraud on a power.[89]

There is much to be said for proceeding incrementally by fashioning particular solutions in response to particular problems, as has recently been done in connection with relational contracts, building where relevant upon experience in other jurisdictions.

Lord Bingham's 2009 Hamlyn lectures, *Widening Horizons: The Influence of Comparative Law and International Law on Domestic Law*,[90] were widely regarded to be of outstanding interest and quality. One of his key points was that "sometimes in seeking to resolve a problem in domestic law, a judge gains assistance or inspiration from considering the law of another country in which an apparently satisfactory solution to the same or a similar problem has been found".[91] The approach taken in Canada in *Bhasin* may in due course commend itself as the right direction for English law to take.

My personal view is that, as long as courts and judges continue to respect the reasonable expectations of the parties (informed and even inspired by international developments and experience), our contract law can be satisfactorily left to develop in accordance with its own pragmatic traditions.[92] Earlier in 2019, the appointment of

Good Faith Obligations and Contractual Termination Rights" [2017] LMCLQ 360; *Taqa Bratani Ltd v Rockrose UKCS8 LLC* [2020] EWHC 58 (Comm).

85. *Supra*, fn.15.
86. *Supra*, fn.42.
87. *Alghussein v Eton College* [1988] 1 WLR 587.
88. *Cobelfret NV v Cyclades Shipping Co Ltd (The Linardos)* [1994] 1 Lloyd's Rep 28.
89. *Eclairs Group Ltd v JKX Oil & Gas Plc* [2015] UKSC 71; [2015] Bus LR 1395.
90. *Supra*, fn.14.
91. *Ibid*, 3.
92. The remarks of Sir David Hughes Parry (the first director of the University of London's Institute of Advanced Legal Studies) with which he chose to conclude his 1959 Hamlyn Lectures still resonate sixty years on: "One never appreciates more fully the truth of a profound observation by the great American judge Mr Justice Holmes than when studying developments and trends in the law of contracts over the past three

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three new Justices of the Supreme Court, to take effect in 2020, was announced.[93] Two of those appointees have a particular interest in the topic of good faith—Sir George Leggatt LJ and Professor Andrew Burrows. We can only hope that a case will arise which will give the Supreme Court an opportunity to give principled guidance as to the future role of good faith in English law.

or four hundred years 'The law', he observed, 'is always approaching, and never reaching, consistency. It is forever adopting new principles from life at one end, and it always retains old ones from history at the other … It will become entirely consistent only when it ceases to grow'": Sir D Hughes Parry, *The Sanctity of Contracts in English Law* (Stevens, London, 1959), 76–77.

93. The Supreme Court, "Lord Reed Appointed Next President of Supreme Court, Alongside Three New Justices—The Supreme Court" (*Supremecourt.uk*, 2019): www.supremecourt.uk/news/lord-reed-appointed-next-president-of-supreme-court-alongside-three-new-justices.html.

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