The Principle of Good Faith in the Performance of Commercial Contracts in England and Wales

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ABSTRACT

This thesis explores the necessity of a principle of good faith in the performance of commercial contracts in England and Wales and suggests that commercial law would benefit from explicitly recognising such a concept. While the law can provide protection for certain cases of unfair conduct, such protection is insufficient, particularly where the parties have unequal bargaining power. Small or inexperienced businesses may find themselves legally obliged to perform agreements with implications they did not fully understand at the time of contracting. This may not always be due to their inexperience or oversight but can also result from a change in circumstances. The main criticism for introducing good faith into contract performance remains the uncertainty in contract enforcement. For too long the debate has been restricted to theoretical and judicial confines. The self-imposed rules of the market's institutions clearly indicate that such fears are misplaced. In particular, Australia provides a concrete example showcasing the usefulness of the concept in franchising contracts. Indeed, this thesis argues that the current judicial stance is significantly delaying the recognition of good faith in contractual performance, not only by failing to provide an overarching standard of good faith in commercial contract performance but also by fixating on a traditional antagonistic view of contractual parties detached from contextual influences in contractual dealings. Legislation is needed to resolve the conundrum faced by the judiciary in what is perceived to be a colossal task, and recent legislative endeavours have failed to fully bridge the gap in regulating opportunistic conduct between businesses where consumer or competition laws are not triggered. This thesis proposes a pragmatic way forward with a statutory good faith standard for commercial contracts, with full awareness that this would inevitably necessitate a rehaul of the entire commercial contract law landscape.

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DECLARATION OF ORIGINAL AUTHORSHIP

I confirm that this is my own work and the use of all material from other sources has been properly and fully acknowledged.

Dimag Feridun

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TABLE OF ABBREVIATIONS

ACCC: Australian Competition and Consumer Commission

B2B: Business-to-business

B2C: Business-to-customer

BFA: British Franchise Association

C2C: Customer-to-customer

CA: Court of Appeal

CESL: Common European Sales Law

Chp/chps: chapter/chapters

Ch: Chancery Division

CISG: United Nations Convention on Contracts for the International Sale of Goods 1980

CLC: Construction Leadership Council

CLP: Current Legal Problems

CMA: Competition and Markets Authority

Costs LR: Costs Law Reports

Cth: Commonwealth of Australia

DCFR: European Draft Common Frame of Reference

FAA: Franchise Association of Australia

FCOC: Franchising Code of Conduct (Australian)

EWCA Civ: England and Wales Court of Appeal, Civil Division

EWHC: England and Wales High Court

ed/eds: editor/editors

edn: edition

eg: for example

EU: European Union

Fn/fns: footnote/footnotes (external to the thesis)

GCA: Groceries Code Adjudicator

HC: High Court

HL: House of Lords

IBA: International Bar Association

ICC: International Chamber of Commerce

ICGL: International Comparative Legal Guides

i.e.: that is

J: Justice

JCT: Joint Contracts Tribunal

LJ: Lord Justice

LMCLQ: Lloyd's Maritime and Commercial Law Quarterly

LQR: Law Quarterly Review

MLR: Modern Law Review

MR: Master of the Rolls

n: footnote (internal to the thesis)

no: number

NZBLQ: New Zealand Business Law Quarterly

OJLS: Oxford Journal of Legal Studies

p/pp: page/pages

para/paras: paragraph/paragraphs

PC: Privy Council

PECL: Principles of European Contract Law

pt: part

QB: Queen’s Bench Division

RGSC: Revenue Generating and Sharing Contract

RIBA: Royal Institute of British Architects

SBC: Small Business Commissioner

SCJ/SCCJ: Supreme Court Justice/Supreme Court Justices

UCC: Uniform Commercial Code

UCCB: Unconscionable Conduct in Commerce Bill HL (2019-2021) [37]

UK: United Kingdom

UKHL: United Kingdom House of Lords

UKSC: United Kingdom Supreme Court

UN: United Nations

UPICC: UNIDROIT Principles of International Commercial Contracts 2016

US/USA: United States of America

UTCCR: Unfair Terms in Consumer Contracts Regulations

Vol/vols: volume/volumes

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INTRODUCTION

Soon after law students are introduced to the vast world of contract law, they encounter a curious term: good faith.[1] Not only does this term quickly greet newcomers to the study of contract law, but it also continues to appear in other subjects such as insurance law or employment law.[2] The term avails itself of various nomenclature, such as the 'principle of good faith', 'the doctrine of good faith', 'the duty of good faith', or can be found hiding behind synonyms such as 'honest and fair dealings' or 'regard given to the interests of the other party.'[3]

The concept of good faith is intrinsically linked to our understanding of the purpose of contract law.[4] While the aims of contract law may be numerous, an understanding that it seeks to facilitate exchange is the most adequate premise for this research.[5] This necessitates that contract law upholds contracts.[6] This can be achieved either by (i) regulating commercial behaviour, for instance by applying extensive substantive rules that dictate what the contractors can or cannot do, or (ii) facilitating commerce, by simply relying on freedom of contract which is delineated by minimal rules and standards on permissible behaviour.[7] In any event, certainty of legal rules requires that cases brought before the courts be decided based on the doctrine of

[1] A quick glance at the most popular contract law student textbooks shows explicit references to the topic, see for instance, Ewan McKendrick, *Contract Law* (14th edn, Red Globe Press 2021) chp 12.6 and chp 12.10; Richard Stone, James Devenney, *The Modern Law of Contract* (Routledge 2022) chp 7.8.

[2] In the context of insurance law, the contract of insurance is deemed to be an uberrimae fidei contract which imposes upon the insured a pre-contractual duty of disclosure which is now enacted into the Insurance Act 2015, the implication of which is further discussed in chp 2.5 below. In the context of employment law, the duty corresponds to that of 'obedience and performance in good faith on one side, and the duty of care and not to destroy mutual trust and confidence on the other' see Hugh Collins, 'Implied Terms in the Contract of Employment' in M Freedland and others (eds) *The Contract of Employment* (Oxford University Press 2016) 480.

[3] See eg *Carewatch Care Services Limited v Focus Caring Services Limited* [2014] EWHC 2313 (Ch) [11] (Henderson J) ('duty of good faith'); Richard Brooks, 'Good Faith in Contractual Exchanges', in A. S. Gold and others (eds), *The Oxford Handbook of the New Private Law* (Oxford University Press 2020) 497 ('doctrine of good faith'); *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB), [2013] 1 CLC 662 [151] (Leggatt J) ('good faith and fair dealing'); Anthony F Mason, 'Contract, Good Faith and Equitable Standards in Fair Dealing' (2000) 116 LQR 66, 72 ('take account of the interests of others').

[4] See eg Johan Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 441, who argues that in the context of dispute adjudication, interpretation of contracts proceeds on the assumption that 'a fair construction best matches the reasonable expectations of the parties,' thereby equating the purpose of contract law to ascertaining such expectations.

[5] Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 8, 12; other purposes may be to (i) 'enforce promises' or to (ii) 'regulate the market in the provision of goods and services' However these are problematic as in the case of the former, promise can be a weak basis upon which to mount liability, and in the latter, it is arguable that the court's function is regulating the market through adjudication, rather they give effect to agreements even where these can be deemed unfair.

[6] ibid 10-11. Upholding contracts indeed gives effect to the promises which were exchanged, including those that are presumed; therefore, the courts can adjudicate disputes on the basis of an approach which is based on ascertaining the intentions of the parties.

[7] Catherine Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (2012) 65 CLP 455, 472.

precedent.[8] This is an essential characteristic of the common law. Without certainty regarding the legal consequences bestowed upon each act, a healthy environment for legal relationships to form, continue, or end cannot exist.[9] In the context of commercial law, this would mean no favourable conditions for commerce to develop and thrive between commercial actors, both within the country and with those abroad.[10] Indeed, contract law is crucial to the operation of commercial law, as it is the main way in which the facilitation of exchange is implemented.[11] It follows that the purpose of commercial law must reflect that of contract law and facilitate commercial activity.[12] Commercial law can also be viewed more neutrally as a 'response' to business disputes, encompassing 'all those principles, rules and statutory provisions, of whatever kind and from whatever source, which bear on the private law rights and obligations of parties to commercial transactions.'[13] A more regulatory role could also be recognised for commercial law, such as in the context of unfair contract terms for consumers or businesses acting on standard terms.[14] Regardless of its ultimate purpose, certainty is viewed as a crucial 'desideratum' in commercial law, akin to its importance in contract law.[15]

Consequently, 'certainty is not an end in itself. Rather, it is an instrumental goal.'[16] As such, 'personal autonomy, (...) and economic efficiency' are the ultimate goals which certainty seeks to achieve.[17] The first goal is reflected in the parties' willingness to enter into enforceable binding contracts where the object of the contract requires the involvement of the other party.

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[8] David H Parry, *The Sanctity of Contracts in English Law* (Stevens & Sons Limited 1959) 72 recognises that certainty provided by the doctrine of precedent cannot be 'unsettled overnight' but notes that the 'static machinery of law' tends to lag behind social and economic change, which inevitably hinders the adjustment of the rights and obligations of the parties.

[9] Rex Ahdar, 'Contract Doctrine, Predictability and the Nebulous Exception' (2014) 73(1) Cambridge Law Journal 39, 41, 52-53. The author posits that predictability of the law is more valued by lawyers than contracting business parties, who are rather concerned with the 'successful performance of the deal, the other party doing its bit, its own potential liability if things go awry, and so on.'

[10] Steyn (n 4) 433 notes that '[t]he commercial advantage of the English approach is that it promotes certainty and predictability in the resolution of contractual disputes.'

[11] Reza Beheshti, Séverine Saintier, and Sean Thomas, *Bradgate's Commercial Law* (4th edn, Oxford University Press 2024) 6, other mechanisms being implemented through tort law, property law, equity and trusts, and criminal law.

[12] ibid. A recent survey into the economic value of English law posits that the role of the law is to operate as an 'infrastructure' which supports economic activity and generates economic value, see Oxera for LegalUK, 'Economic Value of English Law' (*Oxera*, 5 October 2021) <https://legaluk.org/wp-content/uploads/2021/09/The-value-of-English-law-to-the-UK-economy.pdf> accessed 3 April 2025, para 2.4. Also see, Gonzalo Villalta Puig, 'The Misalignment of Commercial Law and Commercial Practice' (2012) 2 LMCLQ 317.

[13] Roy Goode, Herbert Kronke and Ewan McKendrick, *Transnational Commercial Law: Texts, Cases and Material* (Oxford University Press 2015) 1.02.

[14] See eg. Consumer Rights Act 2015 or Unfair Contract Terms Act 1977.

[15] Beheshti, Saintier, Thomas (n 11) 8 citing Lord Scott SCJ in *Golden Strait Corp v Nippon Yusen Kubishika Kaisha (The Golden Victory)* [2007] UKHL 12, [2007] 2 AC 353, [38].

[16] Ahdar (n 9) 40.

[17] ibid 41.

The second goal is embodied in the necessity to predict with 'some confidence whether and when and to what extent (...) contracting parties, are legally bound.'[18] The more the law of contracts allows for a clear prediction, the more economic efficiency can be fostered. Therefore, upholding contracts for the sole purpose of upholding them can lead to decisions that undermine such goals of autonomy and economic efficiency. In other words, such decisions can be deemed to be substantively unfair as they threaten the 'collective welfare of society' by causing an inefficient allocation of resources in a market economy.'[19] Absolute certainty in contract law is an unattainable goal, and such a pursuit can be 'unresponsive to the practical, dynamic needs and reasonable expectations of the commercial community.'[20] Rather, any consideration regarding certainty should be to seek the avoidance of unnecessary uncertainty.[21] Such an approach would also make space for the much-needed flexibility in commercial contract law.[22]

Commercial law's desire to achieve certainty is tempered by the need to recognise the ever-changing and evolving commercial practices. Therefore, commercial law is doomed by its very nature to struggle with the tension between certainty and flexibility of rules or principles depending on the circumstances of each case.[23] The way it chooses to strike 'the right balance between the competing principles' reflects how the law ultimately determines commercial law's purpose to be, whether in adjudication or through legislation.[24] Where the rules are certain, their application may result in unfair outcomes, whereas where they are

[18] ibid.
[19] ibid, 41, 53. The author accepts that 'fairness and justice must be balanced against the need for certainty, with the relative weight given each dependent upon the precise legal, social and economic context, one's philosophical outlook and so on.' Fairness is discussed below in chp 1.3.1.1.
[20] Ahdar (n 9) 58, 60. The author cites the examples of lawful duress and the courts' attempt to reformulate established rules such as remoteness as examples of uncertainty but he posits that the preference of commercial actors and their advisers for clear predictable rules should prevail in contract law over arguments that rigid rules which do not allow for exceptions 'make achieving justice a hostage to certainty.'
[21] ibid.
[22] For instance, the Supreme Court in *Rock Advertising Ltd v MWB Business Exchange Centres Ltd* [2018] UKSC 24, [2019] AC 119 preferred an approach which favoured certainty over flexibility by upholding the validity of a no oral modification clause and effectively upholding the parties' self-imposed limit as to future conduct, despite accepting that in some circumstances there may be a limit on its enforceability, notably when criteria for estoppel could be fulfilled. However, the commercial reality requires that flexibility also be a component of the parties' relationship, in particular where the nature of the contract requires a more informal approach to contractual amendments. See for example, Richard Binns, '*Rock v MWB*: Legal Certainty or Hinderance of Commercial Endeavours?' (2019) 41(2) European Intellectual Property Review 119, 122, who argues that the decision might 'stifle the commercial reality of many IP (intellectual property) licensing relationships and may leave current business practices exposed where they are not reflected in writing.' Therefore, the parties, at drafting stage, have to carefully provide for the exceptions to a no oral modification clause if needed.
[23] Beheshti, Saintier, Thomas (n 11) 6.
[24] ibid 7.

flexible, they may lead to fair outcomes but their future application may be unpredictable.[25] Such modern view of commercial law is problematic because it necessarily leads to a process which distinguishes between various types of commercial contracts that are worthy of upholding certainty or flexibility and those that are not, which necessarily implies a value judgment on which commercial contracts are more conducive to fulfilling the purpose of commercial law which the decision maker seeks to achieve. Indeed, commercial contracts involving larger or multinational businesses, sometimes referred to as 'pure commercial transactions,' are considered to better serve commercial law's facilitative purpose when certainty is favoured over flexibility.[26] Conversely, in the case of a significant imbalance between the parties, flexibility is favoured over certainty.[27]

The underlying reasoning for the above distinction can be explained by a protectionist approach seeking to protect vulnerable parties, where such vulnerability is understood as inexperience, lack of access to resources to obtain insurance or legal advice. However, parties with higher bargaining power are also vulnerable to legal disputes, even though their vulnerability may not stem from a lack of access to such resources. A financially crippling legal dispute may ultimately lead to the contracting parties laying off employees or cutting down costs which creates a market in which commerce is not facilitated but curtailed. This thesis argues that all commercial parties are deserving of the same level of certainty and flexibility, without distinguishing between the types of commercial contract or contracting party. Further support to this argument can be generated by challenging the role of companies as simple profit maximisers. Rather, a public interest goal could be recognised for companies, as the main vehicles for economic activity.[28] This would not necessarily contradict the profit maximisation goal of the companies, as those acting in the public interest would in turn increase the company's profits by increasing employee and customer satisfaction and the goodwill of the company.[29] Indeed, this approach would recognise the existence of companies within a market, and more importantly, within a local, national or international community of other

[25] ibid.
[26] ibid.
[27] ibid.
[28] George Shepherd, 'Not Just Profits: The Duty of Corporate Leaders to the Public, Not Just Shareholders' (2021) 23(3) University of Pennsylvania Journal of Business Law 823, 826, advocates that in the context of US corporate law, '[i]n exchange for enjoying limited liability, corporations, and their officers and directors, should have a duty to serve the public purpose.' The author posits profit maximisation as being flawed because it allows companies to exploit vulnerable individuals and communities, and ignores the original purpose of corporations which was to serve some public purpose, such as building a canal or railroad.
[29] ibid, (fns 11-21).

commercial actors, of which each corporation is a part, as they do not exist in a vacuum and must engage in economic activity to further their profit-making purposes.[30]

This is where the term of good faith can bring flexibility to all areas of commercial contract law. It is submitted that good faith plays an essential role in contracts, one that goes beyond the prevention of opportunistic behaviour.[31] It is difficult to explain good faith simply from a contract law point of view, in particular where it is to be understood as a principle of contract law.[32] Legal discourse has always been separated from other non-legal topics, however, it would not be correct to state that such non-legal topics, such as economics, sociology or ethics, have not had any influence on its study and development, including its principles.[33] The encouragement of good faith, along with other considerations, such as avoidance of unjust enrichment or facilitation of commerce, have all been 'internalized by the rules of contract law itself.'[34] Moreover, a principle is itself grounded in policy, as the resolution of private disputes would be in the public interest where they can be settled according to clear and predictable standards.[35] Consequently, 'public policy and the concept of justice between individual parties cannot be entirely dissociated.'[36] The role of the courts is thus important in setting down principles, as they are not only adjudicating the dispute between the parties before them, but they also ensure the continuation of existing principles and the rules derived from them, or at the appellate level, establish new principles and rules for future cases.[37] In doing so, they give force to 'social, economic and political considerations.'[38] Indeed, the 'rules of contract law shape the distribution of wealth and power in modern societies.'[39] As such, contract law is closely concerned with fairness.[40] Where the structure of society, including contract law, is fair, this creates fair social cooperation that 'creates mutual advantage.'[41] Such mutual advantage is understood as 'primary goods' that 'every rational

[30] ibid 853-855, the author discusses the power that a corporation may hold over its workers and surrounding community which it can 'destroy at its whim' by shifting its investment elsewhere.
[31] For instance, it can also provide a justificatory basis for shifting risk allocation in long-term contracts, see chp 4.6.2 for discussion on frustration and good faith.
[32] See discussion on principle and open norms in chp 1.3.2.
[33] Stephen M Waddams, *Principle and Policy in Contract Law – Competing or Complementary Concepts?* (Cambridge University Press 2011) 221.
[34] ibid 222.
[35] ibid 225.
[36] ibid.
[37] ibid 217.
[38] ibid.
[39] Study Group on Social Justice in European Private Law, 'Social Justice in European Contract Law: A Manifesto' (2004) 10(6) European Law Journal 653, 665.
[40] Understanding contract law requires positing justice as fairness, see Josse Klijnsma, 'Contract Law as Fairness' (2015) 28(1) Ratio Juris 68, 69, 75.
[41] ibid 70.

person would want, irrespective of their particular conception of the good, like wealth but also rights, liberties (...).'[42] Therefore, the rules and principles provided by contract law should seek to allow 'people to engage in exchange and production and thus pursue their conception of the good as free and equal moral persons.'[43] In the context of specific contracts, this would mean that principles or rules, such as that of good faith, target 'various forms of opportunistic abuses (...).'[44]

The concept is not new by any means.[45] Notwithstanding its civil law origins, good faith has managed to find widespread application in English consumer, insurance or employment law.[46] Therefore, the question arises as to whether commercial law should welcome good faith with open arms. The doctrine is rich in academic research on the topic, and the interest is not recent.[47] However, it seems to have garnered more attention than ever before, in particular since Leggatt J's decision in *Yam Seng*.[48] Although some later decisions

[42] ibid.

[43] ibid 76. This view is also supported by Hanoch Dagan and Avihay Dorfman, 'Justice in Contracts' (2022) 67(1) The American Journal of Jurisprudence 1, 2.

[44] Dagan and Dorfman (n 43) 3, 25-26. In the context of US law, the authors identify three categories of application for good faith. First, to specific contract categories which are at risk of opportunistic behaviour, such as insurance contracts. Second, specific moments in the life of contracts in general where one party is vulnerable to the other's opportunism, such as use of contractual discretion, termination or renegotiation. Third, a residual '"freestanding" bad faith behaviour,' a list of examples being provided by the Restatement (Second) of Contracts, s 205.

[45] Simon Whittaker and Reinhard Zimmermann, 'Good Faith in European Contract Law: Surveying the Legal Landscape' in Simon Whittaker and Reinhard Zimmermann (eds), *Good Faith in European Contract Law* (Cambridge University Press 2000) 16-17, explain that the principle of good faith ('*bona fides*') was first recognised as a legal principle by Roman law in seeking to bring a just solution in dispute adjudications. It was initially inserted into dispute adjudication procedure at the request of the defendant as '*exceptio doli*,' essentially giving the judge an equitable discretion to resolve the case on fairness and reasonableness (fn 45). In time, it led to the development of other doctrines such as that of mistake and duress.

[46] Notably, Consumer Rights Act 2015 in the context of consumer law, Insurance Act 2015 in the context of insurance law, or *Attorney General v Blake Jonathan Cape Ltd* [1998] Ch. 439 (CA) 454 in the context of employment law where Lord Woolf MR described the employee's duty of good faith as a duty not to make a profit out of the employer's trust, or not to put himself in a position where his duty and interest may conflict, or not act for his own benefit or the benefit of a third party without the informed consent of his employer. The duty of mutual respect and trust was also sanctioned by the House of Lords in *Malik v Bank of Credit and Commerce International SA* [1998] AC 20 (HL) 45-46 (Lord Nicholls) where the court established that it imposes reciprocal duties on the employer and employee and strives to strike a balance between "an employer's interest in managing his business as he sees fit and the employee's interest in not being unfairly and improperly exploited."

[47] See John N Adams, 'The Economics of Good Faith in Contract' (1995) 8(2) Journal of Contract Law 126; Daniel Friedmann and Jack Beatson (eds), *Good Faith and Fault in Contract Law* (Oxford University Press 1997); Roger Brownsword, 'Two Concepts of Good Faith' (1994) 7(3) Journal of Contract Law 197; Ewan McKendrick, 'English Contract Law: A Rich Past, an Uncertain Future?' (1997) 50(1) CLP 25; Reziya Harrison, *Good Faith in Sales* (Sweet & Maxwell 1997); Jane Stapleton, 'Good Faith in Private Law' (1999) 52(1) CLP 1; Whittaker and Zimmermann (n 45).

[48] *Yam Seng* (n 3), where the duty was implied in fact, as it was in a later case decided by Leggatt J in *Sheikh Tahnoon Bin Saeed Bin Shakhboot Al Nehayan v Kent* [2018] EWHC 333 (Comm) (*Al Nehayan*) [2018] 1 CLC 216. The basis of implication was expanded in *Bates v Post Office Ltd* (No.3) [2019] EWHC 606 (QB) to an implication in law.

gave support to Leggatt's reasoning, others have refused to follow in his footsteps.[49] While some consider that good faith is needed in English law,[50] others consider it would cause significant issues within the operation of commercial law itself, akin to an 'infecting virus', 'irritating British law.'[51] However, a view of contract law as one which encompasses various types of contracts, rather than one which imposes a strict separation between each, is more apt to welcome good faith into commercial law. Indeed, 'the development of principles in one area should be seen as enlightening and informing their application in other areas, so that there is a continuing dialogue between the demands of special contracts and the development of general principles.'[52] The recognition of good faith in other areas of law undoubtedly allows for the debate to seep into commercial law too.[53] Moreover, the separation between various contracts can be justified on the basis of different power dynamics rather than typology.[54] Therefore the debate on good faith in commercial law is becoming increasingly difficult to dismiss solely on the grounds of concerns about undermining legal certainty.

The United Kingdom (UK)'s departure from the European Union (EU) brings about a new and interesting dilemma for the future direction of English commercial law. The lawmaker is no longer required to submit to the requirements of EU laws and regulations. Any past integrations of the good faith concept into English law, such as those made into consumer regulations, may continue to remain valid until further notice, with no guarantee that they will

[49] For case law favourable to good faith, see eg *Yam Seng* (n 3); *Bristol Groundschool Ltd v Intelligent Data Capture Ltd* [2014] EWHC 2145 (Ch), [2014] All ER (D) 117 (Jul); *D&G Cars Ltd v Essex Police Authority* [2015] EWHC 226 (QB). For opponents of good faith, see eg *Greenclose Limited v National Westminster Bank Plc* [2014] EWHC 1156, [2014] All ER (D) 127 (Apr); *Carewatch Care Services Ltd* (n 3), *MSC Mediterranean Shipping Company S.A. v Cottonex Anstalt* [2016] EWCA Civ 789, [2016] 2 CLC 272, *Re Compound Photonics Group Ltd; Faulkner v Vollin Holdings Ltd* [2022] EWCA Civ 1371, *Mackie Motors (Brechin) Ltd v RCI Financial Services Ltd* [2023] EWCA Civ 476, *Quantum Advisory Ltd v Quantum Actuarial LLP* [2023] EWCA Civ 12.

[50] See eg Roger Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' in Geraint Howells and Reiner Schulze (eds), *Modernising and Harmonising Consumer Contract Law* (Otto Schmidt/De Gruyter European law Publishers 2009), Michael Levenstein, 'Where Angels Fear to Tread: The Limits of Good Faith in Commercial Contracts' (2017) 32 (9) Journal of International Banking & Financial Law 569.

[51] Gunther Teubner, 'Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences' (1998) 61 MLR 11. Also see David Campbell, 'Good Faith and The Ubiquity of the 'Relational' Contract' (2014) 77 MLR 482, 490, even though the author accepts that good faith may play a role in contracts, he considers that 'good faith articulated through specific duties will be far more likely to respect the intentions of the parties than a general doctrine.'

[52] Richard Stone and James Devenney, *The Modern Law of Contract* (Taylor and Francis Group 2024) 19-20.

[53] For instance, see chp 2.5 for the discussion on the export of good faith duties from insurance into commercial law.

[54] Stone and Devenney, *The Modern Law of Contract* (2024) (n 52) 20-21, the authors argue for instance that consumer contracts and business contracts need not be subject to separate sets of contractual principles, but that a single law of contract can apply to both whilst catering to each type's power dynamics by providing sufficient flexibility within that same general law of contract.

continue to exist in the future.[55] Moreover, critical legal developments were taking place in other countries with close historical and economic ties to the UK.[56] Notably, Canada had recognised a general principle of good faith applicable in contract law in *Bhasin v Hrynew*.[57] Such developments inevitably bring the fate of good faith in English law back into the spotlight.

Amidst the academic debate, the legal practice and commerce press ahead with their work. The lack of empirical data in the application of good faith in business relations prevents a tangible assessment of the needs and wants of the commercial actors in this area. Although practice of the law and the academic debate over good faith influence each other, how they do so exactly is yet to be determined.[58] The argument underlying this thesis is that good faith should explicitly be recognised in English law. Although relational contract theory helps move away from an understanding of parties as antagonistic in nature,[59] it is not suggested that English law should recognise a separate category of relational contracts.[60] Whilst Leggatt J's reference to relational contracts in *Yam Seng* has fuelled the debate on relational theory in contract law, the shortcomings of the theory itself would be a hindrance to the recognition of a general principle of good faith in contracts, rather than an aid. It is suggested that a revenue generating and sharing contract (RGSC) classification would be better suited for the task in the commercial context.[61] Where an inequality of bargaining power argument is preferred to justify an intervention by the Parliament or by the courts, this assumes that parties with equal bargaining power do not contract on the basis of good faith, therefore, their freedom of contract should not be delimited by such superfluous concepts.[62] As such, the recognition of good faith

[55] For a list of EU Directives and Regulations implemented though the Consumer Rights Act 2015, see Explanatory Notes to the Consumer Rights Act 2015, paras 9-11.
[56] From a comparative perspective, a failure to recognise an underlying principle of good faith is 'unusual': see Paul S Davies, *JC Smith's the Law of Contract* (3rd edn, Oxford University Press 2021) 299.
[57] [2014] SCC 71, [2014] 3 SCR 494. Recently, the Supreme Court of Canada in *C.M. Callow Inc v. Zollinger and others* [2020] SCC 45, [2020] 3 SCR 908 relied on *Bhasin v Hrynew* [2014] SCC 71, [2014] 3 SCR 494 and expanded the duty of good faith in the performance of contracts, by broadening the types of conduct that can lead to a finding of a breach of that duty.
[58] For an example of the limitations of such studies, see Maud Piers, 'Good Faith in English Law - Could a Rule Become a Principle?' (2011) 26 Tulane European and Civil Law Forum 123, 165-166. The author has carried out empirical research in academic work of references to good faith, confirming the substantial increase in interest over the years to the subject. However, she accepts that the data 'does not necessarily reflect or influence the way *practicing lawyers* go about employing the concept of good faith in their work' and that 'correlations between legal practice and academic output exist and are important' (emphasis in text).
[59] For discussion on relational contracts, see below text to n 79.
[60] Ewan McKendrick, 'Long-term Contracts in English Law' in Daniel Friedmann and Jack Beatson (eds), *Good Faith and Fault in Contract Law* (Oxford University Press 1997) 332; Haward C Soper, 'What is a Relational Contract? Does Coherence Lurk Amongst Shapeshifting Incidents and Grandiloquent Language?' Singapore Journal of Legal Studies (2023) 52, 78.
[61] Chp 3.2.3.1.2.
[62] McKendrick, 'Long-term Contracts in English Law' (n 60) 332 argues that relational contracts should not be recognised as a separate category because Parliamentary or judicial intervention is based on inequality of

in all commercial contracts prevents distinguishing of contracts based on the type, the size, the experience, or the bargaining power and market influence of the parties. It puts all parties on equal footing in terms of how their agreements are viewed by the courts in the context of dispute adjudication.

Franchising serves as an ideal example to illustrate the operation of a duty of good faith beyond the confines of bargaining power, relational or lengthy contract dynamics. Indeed, beyond such characteristics, it is a method of distribution of goods and/or services and/or technologies where the success of the parties' cooperation determines the success of the enterprise.[63] As such, team effort will be more prevalent than in spontaneous commercial transactions such as sales agreements, where the cooperation of the parties will be less demanding than in longer-term contracts. The lengthy duration of the agreement and the parties' more elaborate tasks to achieve the purpose of the contract inevitably increase the risk of conflict. Indeed, the parties' expectations from each other and the contract take a central role in remedying potential breaches of contractual performance. An explicit recognition of good faith in commercial contracts would level the playing field amongst all commercial actors independently from their individual characteristics and be conducive to an environment where commerce is more likely to flourish sustainably.[64] Importantly, the lack of a principle of good faith in English commercial contracts has generated self-regulating market tools such as the British Franchise Association (BFA)'s Code of Ethical Conduct in an attempt to fill the legal vacuum.[65] English contract law is at a crossroads; modern contract law has affected many aspects of classical contract law.[66] Indeed, while the classical contract approach long favoured by the courts insists on rigid rules, modern contract law has slowly pushed back against

bargaining where certain categories of contracts are systematically characterised by such inequality, such as employment or consumer credit contracts. The burden is therefore on the parties themselves in allocating the risk wisely, in particular in the context of long-term contracts.

[63] Gillian K Hadfield, 'Problematic Relations: Franchising the Law of Incomplete Contracts' (1989) 42 Stanford Law Review 927, 931.

[64] See eg the analysis of the Australian example of a mandatory code of conduct imposing a legal duty of good faith in franchising contracts in chp 5.4.

[65] British Franchise Association, 'The Code of Ethics for Franchising' (*BFA*, 2024) <https://www.thebfa.org/wp-content/uploads/The-Code-of-Ethics-for-Franchising-2024.pdf> accessed on 3 April 2025.

[66] Melvin A Eisenberg 'The Transformation of Contract Law from Classical to Modern' in MA Eisenberg (ed), *Foundational Principles of Contract Law* (Oxford University Press 2018) 25, the author identifies four spectrums to evaluate a shift from classical to modern contract law doctrine, being (i) objectivity vs subjectivity (for instance in the context of interpretation of contracts), (ii) standardisation vs individualisation (depending on whether variables are used, such as the taking into account of circumstances to determine intentions of the parties) (iii) static vs dynamic (depending on whether interpretation is influenced only by events at the time of entry into contract or by those occurring prior to the contract formation) (iv) binary vs multifaceted (such as in the context of damages, where the choice is between damages or not, the choice is binary, but it is multifaceted where the choice is amongst different types of damages such as expectation, reliance, restitutionary).

classical contract law.[67] The demands of a globalised commercial market require that English law does not fall behind other jurisdictions and, more importantly, that it does not impede commercial bargains.

In sum, this thesis argues for an explicit recognition of good faith in commercial performance. This proposal offers multiple benefits. First, it eliminates distinctions based on contract type, party size, experience or bargaining power and levels the playing field across all commercial disputes involving B2B contracts. Second, it recognises that lengthier or cooperative agreements require that their expectations be protected in the long run to reduce conflicts and promote mutual success. Third, it encourages fair dealings and creates an environment where commercial activity can sustainably flourish by balancing the needs of all parties, regardless of their bargaining power. Fourth, it allows English law to adapt to the requirements of a globalised market to avoid falling behind other common law jurisdictions, which have embraced good faith as a general principle in contracts. Lastly, it avoids over-reliance on self-regulation. Indeed, the lack of a principle of good faith has led to self-regulators' efforts highlighting the need for a clear legal framework rather than relying on market tools to address gaps. Consequently, recognising good faith in English commercial law would align it with evolving global practices, enhance fairness, and promote effective and sustainable commercial relationships.

1. Mapping the Debate on Good Faith in English Commercial Law

In the landmark case of *Carter v Boehm*, Lord Mansfield stated that good faith was the 'governing principle (...) to all contracts and dealings.'[68] The case established the duty of utmost good faith on each party to a contract of insurance, specifically in regards to disclosure of material information. This 18th-century case was decided against the backdrop of the insurance market in which the insurers were at a significant disadvantage compared to the insured as the risk assessments could mainly be based on the declarations of the latter. Without such a principle, the insurance business could not have developed as a viable business. However, Lord Mansfield's statement remained confined to the practice of insurance law. A classical view of contract law did not permit the import of good faith into commercial contract law. The courts have repeatedly refused to recognise good faith as capable of application per

[67] ibid.
[68] (1766) 3 Burr 1905, 97 ER 1162, 1909.

se.[69] So far, good faith seemed to be reserved for certain types of contracts, such as those involving fiduciary duties or those classified as uberrimae fidei (such as insurance contracts). Consumer legislation, sourced through EU regulations, also enshrined a duty of good faith in an attempt to correct the significant imbalance that occurs in the parties' rights and obligations.[70]

Meanwhile some judges remained open to good faith in the context of commercial law. Leggatt J famously found in *Yam Seng Pte Ltd v International Trade Corporation Ltd* that a duty of good faith could be implied into contracts as a matter of English law.[71] He dismissed concerns that 'recognising a duty of good faith would generate excessive uncertainty' and considered that 'hostility' towards such doctrine was 'misplaced.'[72] He posited that many norms governed the contractual relationship, honesty being one of them. Good faith goes beyond what is dishonest conduct, and includes conduct that is 'improper,' 'commercially unacceptable' or 'unconscionable.'[73] The novel approach that was taken in this case was that the court borrowed the concept of a 'relational contract.'[74] This paved the way for subsequent cases to refer to relational contracts as a legal concept and fuelled the debate in the legal doctrine.[75]

Understanding the relational view of contracts first requires an understanding of the classical view. The classical view of contract law is dedicated to party autonomy and freedom of contract, where the parties are presumed to be self-interested and motivated by antagonistic 'hard economic rationality.'[76] It is characterised by a formalistic understanding of the functioning of the law, where dispute adjudication should operate on the basis of precise rules as opposed to general principles, informed by precedent and obeying a notion of justice which was procedural rather than substantive.[77] However, the increasing use of the standard form

[69] See eg *Walford v Miles* [1992] 2 AC 128 (HL) in the context of contract negotiations.
[70] See n 14.
[71] *Yam Seng* (n 3) [166].
[72] ibid [154].
[73] ibid [139].
[74] ibid [143].
[75] See eg *Bristol Groundschool* (n 49); *D&G Cars Ltd* (n 49). In the legal literature, see eg Hugh Collins, 'Is a Relational Contract a Legal Concept?' in S Degeling, J Edelman, and J Goudkamp (eds), *Contract in Commercial Law* (Thomson Reuters 2016) <https://core.ac.uk/download/pdf/237399685.pdf> accessed 3 April 2025.
[76] Catherine Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (Cambridge University Press 2022) 30. The author further explains that the demands of a market economy, in particular of commodity markets, contributed to shaping of understanding contracts as 'instruments of future planning (...), with legal significance being attached to the creation of liability at the point of agreement rather than the point of action.'
[77] ibid 31. Also see Patrick S Atiyah, *Rise and Fall of Freedom of Contract* (Oxford University Press 1979) 400, who identifies the era of classic contract law to be between 1770–1870. However, John H Baker, 'The Rise and Fall of Freedom of Contract by P.S. Atiyah' (1980) 43 Modern Law Review 467, 469, warns that it should not be

contract, the problematic of free choice and intention as the basis of contractual liability, and the emergence of the consumer as a significant contracting power have all contributed to its decline.[78] In the 1960s, Ian Macneil challenged the premise of the theory of contract by arguing for a relational one.[79] The novelty of this modern view was that it presented trust and cooperation to be the foundation of contracts, capable of impacting the formation of the contract, its performance and its enforcement.[80] Indeed, Macneil contended that the parties, in particular where a long-term relationship is contemplated or in course, depend on flexible norms to allocate contractual risk to administer the agreement.[81] He used the word 'relational' in two interconnected ways; first, to mean that all contracts are embedded in a 'social matrix', thereby making even the most discrete of relations subject to the operation of the same norms that affect all other ones.[82] The second meaning is to understand contracts as a reflection of ongoing relationships, not fixed in time exclusively at the point of contracting.[83] Any modifications throughout the performance of the contract, more likely for long-term contracts than discrete ones, would be reflected in the application of the contract, thereby underlining the importance of cooperation between the parties to fulfil the contractual aim. The norms that inform contractual behaviour, such as flexibility, are understood as internally underlying the contract, rather than imposed upon it externally.[84] This prompted some commentators to criticise this view of law as 'overinclusive' or 'underinclusive,' in any event, unsatisfactory.[85] This criticism stems from the difficulty of defining when a contract is discrete and when it is relational, leading to difficulty in 'operationalizing' the approach in legal terms.[86] However,

assumed that classical law had 'replaced a previous body of law which reflected a golden age of fairness and equity.' Prior, he contends that there was little contract law at all because 'there was not machinery for producing it and most of the questions were left to juries as questions of fact.'

[78] Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 34 referring to Atiyah's work in Stephen A Smith, *Atiyah's Introduction to the Law of Contract* (6th edn, Oxford University Press 2005), 15–19.

[79] Relational contract theory has its origins in sociological and economic theory, see Jonathan Ainslie, 'Good Faith and Relational Contracts: A Scots-Roman Perspective' (2022) 26 Edinburgh Law Review 29, 34.

[80] David Campbell, *The Relational Theory of Contract: Selected Works of Ian Macneil* (Sweet and Maxwell 2001), 3, 5. Also see Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 33.

[81] Ian R Macneil, 'Contracts: Adjustment of Long-term Economic Relations Under Classical, Neoclassical and Relational Contract Law' (1978) 72 Northwestern University Law Review 854, 901.

[82] Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 13.

[83] ibid, 14; Macneil poses the problem as one of 'presentiation' of the classical view of contracts, which requires that regardless of the subsequent performance of the contract or modifications of the relationship, the contract is to be determined by reference to the time when it was concluded, as opposed to when the performance was undertaken, or modifications happened.

[84] ibid.

[85] Melvin A Eisenberg, 'Relational Contracts' in J Beatson, D Friedmann (eds) Good Faith and Fault in Contract (Oxford Clarendon Press 1995) 292.

[86] ibid 293, 296 for instance Eisenberg posits that length of the contract is not a valid way in which to determine whether a contract is relational or discrete. Rather, he posits that relational contract should be understood to mean a contract (a legally enforceable promise, a bargain) where there is also a relationship.

even where a relational contract is found to exist, it should not be made subject to special rules, but 'to general rules of a properly formulated body of contract law,' specific exceptions being allowed for some subcategories of discrete or relational contracts.[87] For instance, an obligation to perform contracts in good faith would apply to all contracts, whether discrete or relational.[88] In contrast, a special rule that allows for termination on fair terms in the context of long-term contracts will only apply to long-term contracts, but not to relational contracts as a class, the length of the contract being a distinguishing feature to which the special rule can apply.[89] In sum, general legal principles should be devised to apply to both discrete and relational contracts.

A relational understanding of contract law offered an alternative to the inability of the classical view's anchoring of freedom of contract in addressing challenges prompted by market developments. Such an alternative emphasised 'the importance of preventing domination, ensuring equivalence in exchange and upholding co-operation in contractual dealings.'[90] The use of judicial discretion increasingly became informed by such concerns, which was likely helped by legislative measures such as the Consumer Credit Act 1974 or Unfair Contract Terms Act 1977 (UCTA 1977).[91] These legislative measures themselves were explained by a 'welfarist' approach to law, influential between the 1940s and 1970s, which recognised the state's role in a post-war era, as having to provide its citizens with public goods and services as necessities.[92] In the relational lens, the contract was no longer viewed as a discrete abstraction but was an entity embedded in the social norms within which the parties operated.[93] The effects of a relational view of contracts on judicial reasoning were further evidenced by increasing references to the parties' reasonable expectations, which was proposed as an alternative to the traditional contract law's organising principle of freedom of contract.[94] Indeed, not only did the concept of reasonable expectations appear in legislation, such as in UCTA 1977 as a control on standard form exclusion or limitation of liability clauses, but also it allowed judicial reasoning to depart from the strictness of the classical theory, such as by

[87] ibid 298.
[88] ibid 299.
[89] ibid 304.
[90] Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 35.
[91] ibid, prior to such legislation, the courts had already started to address the shortcomings of the classical theory, for instance by creating the innominate terms categorisation of contractual terms in *Hong Kong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 1 All ER 474.
[92] ibid 40, the author gives the examples of the use of the principle of proportionality, the protection from exploitation by a stronger party, prevention of bad faith reliance on formal contract rules to obtain unbargained advantages, as examples of the welfare mindset in judicial reasoning.
[93] ibid 38.
[94] Steyn (n 4) 433.

limiting the use of contractual discretion, allowing the use of a good faith restriction, or adopting contextualist contractual interpretation as an alternative to the literal one.[95]

With a relational view of contracts, an increasing number of references were made to the concept of good faith. Campbell argued that good faith is fundamental to all contracts and that the relational contract theory recognises the essence of commercial contracts as being a 'fundamentally co-operative contractual relationship.'[96] Consequently, both express and implied duties of good faith have also garnered attention in the last decade.[97] Bell and McCunn observed that such attention in the case law will undoubtedly result in the recognition of implied duties of good faith but that determining the content of it necessitates further judicial intervention.[98] Collins suggested that context and purpose of the transaction would determine the content of a good faith duty in each case but that 'expectations of cooperation and loyalty' and 'the avoidance of actions likely to destroy mutual trust and confidence between the parties' will usually help draw out the limits of the implicit expectations of the parties.[99]

Nevertheless, the lack of an overarching principle or duty of good faith in commercial contracts in general means that the courts must continue to find 'piecemeal solutions' to unfair outcomes.[100] Consequently, condemnable conduct will be considered under well-established doctrines such as misrepresentation, duress or unconscionable conduct.[101] Bridge and Whittaker voice the concern of many legal practitioners when they argue that good faith introduces uncertainty and places too much power in the hands of courts, taking away from the freedom of the parties to contract as they see fit.[102] In other words, good faith would permit judges to be 'trespassing too far into the legislative domain.'[103] The influence of the classical theory, after having encountered the influences of the relational one, has led to what MacNeil called 'neo-classical' law, which accepts contract as a discrete instrument but subjects it to

[95] Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 42.
[96] Campbell, 'Good Faith and The Ubiquity of the 'Relational' Contract' (n 51) 475.
[97] For express terms, see eg *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200; *CPC Group Ltd v Qatari Diar Real Estate Investment Co* [2010] EWHC 1535 (Ch), [2010] All ER (D) 222 (Jun). For implied terms, see eg *Al Nehayan* (n 48); *Essex County Council v UBB Waste (Essex) Ltd* [2020] EWHC 1581 (TCC), 191 ConLR 77.
[98] Andrew J Bell and Joanna McCunn, 'Professional Negligence in 2020: The Year in Review 2021' (2021) 37 Journal of Professional Negligence 5, 16-18.
[99] Collins, 'Is a Relational Contract a Legal Concept?' (n 75) 7.
[100] As famously stated by Bingham LJ in *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] 1 QB 433 (CA) 439.
[101] See eg McKendrick, *Contract La*w (n 1) 251, 252.
[102] Michael Bridge, 'Good Faith, the Common Law and the CISG' (2017) 22 Uniform Law Review 98, 100-101; Simon Whittaker, 'Good Faith, Implied Terms and Commercial Contracts' (2013) 129(3) LQR 451, 468.
[103] Hugh Beale (ed), *Chitty on Contracts* (33rd edn, Sweet and Maxwell 2020), 1-047.

occasional exceptions.[104] This ultimately provides an incohesive framework for understanding contracts, and is also reflected in the approach to good faith in judicial reasoning.[105]

The amorphous characteristic of good faith has led to many methodologies in literature in an attempt to better understand and possibly characterise the concept to implement it into English law. Notably, Teubner comes to mind with its criticism of legal transplants and the risks created by the implementation of foreign concepts into a certain system of law.[106] Nonetheless, comparative studies remain important and relevant for eliciting a concept that has already been tried and tested in other systems of law.[107] Conclusions drawn from an economic analysis of law also inform the debate on good faith from alternative angles that go beyond the confines of legal literature. Burton's analysis of good faith has often been in the realm of an economic one, in which he defined good faith against parties' economic interests.[108] Indeed, his approach takes into account the prevention of any forgone opportunities to the detriment of the other party. He gauged these opportunities in reference to the parties' reasonable expectations at the time of contracting.[109] As mentioned above, social sciences also play a crucial role as the role of contract law is put into question through the ethical aspects that good faith should play in commercial transactions.[110] Another approach that is relevant and builds upon both social and economic constructs of good faith mentioned above is one adopted by Collins and Brownsword in re-imagining contract law within the regulatory sphere of law in general.[111] By adopting a wider lens on contract law, the purpose of good faith is put into question within the general purpose of contract law. Indeed, Campbell was correct in claiming that 'determining a correct policy towards good faith is only in the first instance a question of

[104] Macneil, 'Contracts: Adjustment of Long-term Economic Relations Under Classical, Neo-classical and Relational Contract Law' (n 81) argues that the legal reasoning of the courts and the law as envisaged by commentators is 'neo-classical' rather than classical.
[105] David Campbell and Hugh Collins, 'Discovering the Implicit Dimensions of Contracts' in D Campbell, H Collins and John Wightman (eds.), *Implicit Dimensions of Contract* (Hart Publishing, 2003) 25–27.
[106] Teubner (n 51). See further discussion below at text to n 246 on the concept of legal irritants.
[107] See for eg Simon Whittaker, 'Unfair Terms in Commercial Contracts and the Two Laws of Competition: French Law and English Law Contrasted' (2019) 39(2) OJLS 404; Severine Saintier, 'The Elusive Notion of Good Faith in the Performance of a Contract, Why Still a Bête Noire for the Civil and the Common Law?' (2017) 6 Journal of Business Law 441; Edward A Farnsworth, 'Comparative Contract Law' in *The Oxford Handbook of Comparative Law*, M Reimann, and Zimmermann (eds), (1st edn, Oxford University Press 2006).
[108] Steven J Burton, 'Breach of Contract and the Common Law Duty to Perform in Good Faith' (1980) 94(2) HLR 369.
[109] For more on the economic analysis of law, see eg Timothy J Muris, 'Opportunistic Behavior and the Law of Contract' (1981) 65 Minnesota Law Review 521 (defining opportunism as the transfer of wealth from one party to the other contrary to the parties' understanding); Richard A Posner, *Economic Analysis of Law* 81 (3rd edn, Little, Brown and Company 1986) (defining opportunism as taking advantage of the other party's vulnerability).
[110] See for eg David Campbell, *Relational Theory of Contract: Selected Works of Ian Macneil* (Sweet & Maxwell 2001) 3-58.
[111] Hugh Collins, *Regulating Contracts* (Oxford University Press 1999); Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 87-114.

legal doctrine. Ultimately, it is a question of values.'[112] This is the reason why the shift from the classical theory of contract law to a modern one was necessary.

Importantly, an understanding of contracts as simply a tool of exchange for self-interested parties denies the co-operative norms which underlie all contracts.[113] Thus '[t]he fundamental unit for the analysis of contract therefore is not the subjective will of the contracting party, but the subjective will in the objective form of the persuasion of the other party; that is to say, in a form constitutive of the contractual relation of co-operation.'[114] Where the neo-classical theory imposes a 'static market-individualis[t]' understanding of the parties' reasonable expectations, a modern theory embraces a 'dynamic market-individualis[t]' one.[115] This research lends support to the latter analysis by reviewing not only the case law and legislation but also the voluntary regulations adopted by market actors for their commercial dealings.

2. Research Question and Originality

This research questions whether there is a need to recognise good faith in the performance of English commercial contracts. Given English law's current hostility towards good faith in the performance of contracts, it is proposed that the debate must necessarily move away from a traditional understanding of contract law to a modern one. English courts' compulsive devotion to certainty can be seen as an obstacle to furthering the advancement of other principles, such as good faith. Moreover, the lack of legislative impetus on enacting good faith into commercial contracts is noticeable.[116] However, the debate on good faith in

[112] Campbell, 'Good Faith and The Ubiquity of the 'Relational' Contract' (n 51) 491.
[113] Prince Saprai, *Contract Law Without Foundations: Toward a Republican Theory of Contract Law* (Oxford University Press 2019) chp 7 argues that the purpose of contract is to structure relationships of cooperation based on trust, equality and respect.
[114] Campbell, 'Good Faith and The Ubiquity of the 'Relational' Contract' (n 51) 485.
[115] Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 103-104. The author posits that 'static market-individualism' relies on a classical understanding of contracts, where the principal function of contract law is seen as being to 'establish a clear set of ground rules within which a market can operate.' In contrast, 'dynamic market-individualism' relies on modern contract theory which is more flexible and is 'guided by the practices and expectations of the contracting community (particularly the commercial community).' John N Adams and Roger Brownsword, 'The Ideologies of Contract' (1987) 7(2) Legal Studies 205, 206 a 'market-individualism' theory posits the law's function as to encourage market participation by facilitating the creation and enforcement of contractual obligations. To curb the harshness of the 'market-individualism' model, a 'consumer-welfarist' model is proposed in which the consumer is to be protected from the other party's exploitative conduct (210). The 'market-individualism' model applies to commercial contracts, whereas the 'consumer-welfarist' one applies to consumer contracts, see John Wightman, 'Reviewed Works: Contract and Economic Organisation by David Campbell, Peter Vincent Jones; Exploring the Boundaries of Contract by Roger Halson' (1997) 24(3) Journal of Law and Society 450, 456.
[116] Chp 6.4.1.

commercial law is an important one as it seeks to determine the extent to which the law should concern itself with fairness in freely negotiated business contracts. Indeed, the 'enforcement of basic norms of commerce and of fair and honest dealing is an essential function of a system of commercial law.'[117] Some 'piecemeal solutions' to address problems of fairness do exist.[118] However, their adequacy or sufficiency to alleviate the unfairness in a given context is open to debate.[119]

Outside of some specific areas of law, English courts have been reluctant to recognise good faith in the performance of contracts. Issues regarding its definition and the alleged risk of uncertainty it would be introducing to contract law have regularly formed the basis of the opposition towards its recognition.[120] Therefore, the shock waves created by Leggatt J's decision in *Yam Seng* are understandable in such a hostile context.[121] Although the decision was not to imply a duty of good faith in law, it was held that such an implication could be made in fact, based on the presumed intention of the parties.[122] The parties can also choose to draft express good faith clauses in their contracts, but these also come with their own sets of issues relating to interpretation and application.[123] The available legislation also presents limited solutions as they only apply to pre-determined contexts and do not lend themselves to a general application over all commercial contracts.[124]

This research's particular focus on franchising contracts is fuelled by the explicit reference made by Leggatt J in *Yam Seng* to such contracts as being 'relational,' thereby explicitly embracing the modern contract law theory in the context of contractual performance.[125] In contrast to the other types of 'relational' contracts he enumerated, franchising is also an industry in itself.[126] A recent survey has shown that not only does it contribute £17.2 billion per annum to the UK's gross domestic product, but that it is growing

[117] *Al Nehayan (*n 48**)** [187] (Leggatt LJ).
[118] As famously stated by Bingham LJ in *Interfoto* (n 100) 439 in the context of pre-contractual negotiations. Similarly, in a later case on the termination of a contract, Moore-Bick LJ in *MSC Mediterranean Shipping Company S.A.* (n 49) [45] also stated that 'the better course is for the law to develop along established lines rather than to encourage judges to look for what the judge in this case called some 'general organising principle' drawn from cases of disparate kinds.'
[119] Chp 2.
[120] Steyn (n 4) 433.
[121] For an opposite view, see Moore-Bick LJ's decision in *MSC Mediterranean Shipping Company S.A.* (n 49).
[122] Yam Seng (n 3) [161].
[123] Chp 4.4.
[124] For example, Unfair Contract Terms Act 1977, or Consumer Rights Act 2015. See chp 6.4.
[125] *Yam Seng* (n 3) [143].
[126] ibid [143], joint venture and long-term distribution agreements were the other two examples provided by Leggatt J.

more than ever before.[127] Therefore, franchising has the benefit of an organised industry body which provides for self-imposed voluntary rules that reflect the needs and the demands of the industry in the context of their commercial dealings.[128] They are long-term agreements in the sense that the performance of the contract extends over a certain or indeterminate period with an emphasis on team effort by both parties. Therefore, they are particularly suited for an evaluation of good faith considerations in the performance of contracts.

While the debate is ongoing in English law, on a global scale, it seems that English law is swimming against the tide with its unwelcoming attitude.[129] The United States (US) enshrined good faith in article 1 of the Uniform Commercial Code (UCC), uniformly adopted by all states from the 1950s onwards.[130] It provides that 'every contract or duty within this code imposes an obligation of good faith in its performance or enforcement.'[131] In Canada, the Supreme Court in *Bhasin v Hrynew* held in 2014 that there is a general organising principle of good faith in the performance of contracts.[132] In Australia, back in 1992, the New South Wales Court of Appeal in *Renard Constructions (ME) Pty v Minister for Public Works* (*Renard Constructions*) also concluded that there were strong arguments for the recognition of a duty of good faith and fair dealing in contractual performance.[133] While developments on good faith in common law countries have been recent, civil law countries have already recognised good faith in contracts many years ago. Germany's *Treu und Glauben*, France and Switzerland's *bonne foi* have over 100 years of judicial and academic literature dissecting and analysing the concept from various angles. In many cases, both the civil and common law traditions, which expressly recognise good faith address issues that are also encountered in English law.

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[127] BFA, '2018 BFA NatWest Franchise Survey' (BFA, 2018) <https://www.thebfa.org/about-us/industry-research/> accessed 3 April 2025.

[128] BFA, 'The Code of Ethics for Franchising' (*BFA*, 2024) <https://www.thebfa.org/wp-content/uploads/The-Code-of-Ethics-for-Franchising-2024.pdf> accessed on 3 April 2025.

[129] Vasanti Selvaratnam, 'Good Faith: Is English Law Swimming Against the International Tide?' (2020) 2 LMCLQ 232; Baris Soyer and Andrew Tettenborn, 'Mapping (Utmost) Good Faith in Insurance Law- Future Conditional?' (2016) 132 LQR 618, 629, 632-633. Good faith is also recognised in many international instruments such as the United Nations Convention on Contracts for the International Sale of Goods (CISG) s7(1), the UNIDROIT Principles of International Commercial Contracts (PICC) s 1.7(1), the Principles of European Contract Law (PECL) s 1.06(1), s 1.201, the European Draft Common Frame of Reference (DCFR) s I-I:103(2), and the Common European Sales Law (CESL) s 2.

[130] Uniform Law Commission, 'Uniform Commercial Code' (*Uniform Laws*, 2024) <https://www.uniformlaws.org/acts/ucc> accessed 3 April 2025. However the remainder of the articles of the UCC were not uniformly adopted by all states, see Uniform Law Commission, 'UCC Article 1, General Provisions' (Uniform Laws, 2001) <https://www.uniformlaws.org/acts/ucc> accessed 1 December 2025. See also the Restatement (Second) of Contracts, s 205 which provides that '[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.'

[131] UCC, s 1-203.

[132] *Bhasin* (n 57).

[133] (1992) 26 NSWLR 234.

Consequently, the arguments advanced to oppose good faith in English contract law appear increasingly elusive or unfounded.[134]

It follows from the above context that English law should strive to align itself with other common law countries. Any such endeavour will depend on the number of cases which reach the courts dealing with the issue, the progressive or conservative stance of the judges deciding such cases, and whether legislation is introduced by the Parliament.[135] However, there is also another force which is influential in shaping the law, and that is the market. In the commercial realm, commercial actors are, of course, vital. They abide by certain legal rules to carry out their transactions, but they also abide by a set of market rules. These market rules are set down by the market itself, and more specifically by its actors. Although much empirical evidence is needed to establish how good faith is viewed and used by the market itself, any such data would likely be able to influence the judiciary and legislative powers. In the meantime, the best indicator for the choices of the market is the self-imposed rules or guidelines published by the institutions of the market itself.[136]

The opposite is, however, not true. Hence, the current state of the law might not reflect the desires of the market itself. The judiciary is not part of the market forces, nor is the legislative, they shape the present of market dealings but not their future direction. Therefore, their stance may be a mere reflection of what the market forces want, although such assumptions can be misplaced and subject to substantial corrections over the years. Rather than assuming the wishes of the market, this thesis proposes that self-regulating rules of the commercial actors should also be taken into account in gauging the readiness of the law to recognise new rules. Codes of conduct or practice are, in that respect, important indicators. A wider view of contract law must be embraced to avoid restricting the debate to the confines of a contractual instrument. The research question, therefore, seeks to adopt a panoramic view of the regulation of transactions, and in particular of the regulation of fairness in commercial dealings.

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[134] Chp 1.2.

[135] Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 199, 200 further highlights the obstacles in the face of highly significant cases making it to the upper courts and thereby giving a direction to the law, such as the cost of litigation. Another reason is because for appeals to proceed into higher courts, there usually has to be an important point of principle or practice (for the Court of Appeal) and a point of law of general public importance (for the Supreme Court), thereby preventing many cases on contract law from proceeding, which contributes to the 'lack of diversity' of contract cases.

[136] Chp 6.3.

The originality of the research is twofold; first, it proposes a concrete legislative solution. It provides for a clearly drafted statutory good faith duty to be applied in contractual performance, thereby removing the ambiguity about whether and when good faith applies in commercial settings. This ensures that opportunistic or bad faith behaviour is curtailed in all commercial dealings, not just specific contract types. Indeed, a good faith duty provides a clear baseline for businesses and reduces reliance on piecemeal common law developments; avoids the unpredictability of diverging judicial interpretations, thereby providing consistent application of the standard; and proactively encourages parties to act in good faith, rather than serve as a reactionary tool.

Second, it submits good faith as a unifying concept of contract law by challenging the way in which English law deals with opportunism in commercial contractual performance. The currently available legislative framework for commercial contracts deals with consumer contracts on the one side, and the commercial practices of companies in the context of competition laws on the other side.[137] However, there exists a gap for regulating commercial contractual behaviour where the opportunistic behaviour is not caught by either. This research identifies such a gap and proposes good faith as a solution, based on a novel analysis of extra-judicial sources from the market actors themselves, thereby also providing an original contribution to modern contract law theory. Further, the juxtaposition with the Australian experience, and in particular with the regulation of its franchising contracts, further amplifies the gap that English law should strive to fill to have a more cohesive commercial contract law.

3. Methodology

This thesis uses several methodologies to answer the research question. The doctrinal method is crucial in most legal research, as it is in the present thesis. Doctrinal work requires that 'arguments are derived from authoritative sources, such as existing rules, principles, precedents, and scholarly publications.'[138] It allows the researcher to 'describe a body of law and how it applies. In doing so, the researcher may also provide an analysis of the law to demonstrate how it has developed in terms of judicial reasoning and legislative enactment.'[139]

[137] For instance, by prohibiting anti-competitive agreements between businesses, or conduct that amounts to an abuse of a dominant position in a market regulated under the Competition Act 1998.
[138] Rob Van Gestel, and Hans W Micklitz, *Revitalizing Doctrinal Legal Research in Europe: What about Methodology?* (2011) European University Institute Working Papers Law, <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1824237> accessed 3 April 2025, 26.
[139] Ian Dobinson and Francis Johns, 'Legal Research as Qualitative Research' in Mike McConville and Wing Hong Chui (eds), *Research Methods for Law* (2nd edn, Edinburgh University Press 2018) 21.

The topic of good faith has proved to be fertile ground for a large number of academic researchers in the UK and abroad. The previously published body of work on the topic by academics and legal professionals is vast and requires rigorous scrutiny to filter a workable amount for this research. The thesis seeks to achieve a balance between the most prolific and cited researchers on the topic and those who brought fresh perspectives through an alternative approach.

Pluralist methodology is also prevalent in this work. Although good faith is not enacted into any relevant legislation in English commercial law for this thesis, it does exist in the common law.[140] Non-legal sources of law, sometimes referred to as 'soft law,'[141] such as codes of conduct in the franchising context, also help construct and review the normative arguments advanced in this work. The flexibility that the businesses require can only be translated into legal reforms by adopting an adaptable view of the law, through the use of multiple methodologies available to a legal researcher. Therefore, a sole doctrinal approach is not suitable to tackle the research question. A pluralist view of law allows an insight into market practices and can illuminate the inadequacy of existing legal rules. Business practices that circumvent applicable rules by incorporating an express duty of good faith, such as in the franchising context, may reflect broader inadequacies within contractual frameworks.

This work seeks to go beyond a descriptive or explanatory exercise. The literature is already rife with such endeavours. Therefore, the thesis does not dwell extensively on the meaning of the concept, nor its historical origins. Whether there is a need or not for an overarching principle of good faith in English commercial law cannot be determined through a mere overview of the state of the law as it stands. Even the comparative methodology, incorporated through the analysis of the Australian laws and soft law, serves to illuminate the primary target, which is English law.[142] It is not intended to be an extensive comparative legal analysis of both systems of law, as this will surpass the parameters imposed by the task at hand. Yet, a comparative outlook offers valuable insights into alternative or contrasting approaches to the law as applied in England. More importantly, the proposal of a statutory duty is only possible by employing a normative methodology. Indeed, legal scholarship often requires a

[140] The scope of the thesis is restricted to business contracts excluding consumer ones as set out in section 4 of the introduction. The only explicit reference can be found in the Commercial Agents (Council Directive) Regulations 1993, SI 1993/3053, ss 3, 4. However agency contracts are also excluded from the scope of this work as set out in the introduction.

[141] Stephen Daly, 'The Rule of (Soft) Law' (2021) 32(1) King's Law Journal 3.

[142] Ishwara P Bhat, Idea and Methods of Legal Research (Oxford Academic Press 2020) 279 explains that comparative legal research notably aims to 'promote critical understanding of one's own legal system.'

blend of both descriptive and normative analysis, recognising the interplay between existing practices and normative ideals.[143]

The methodologies employed herein aim to identify and address any gaps or uncertainties which need to be eliminated if commercial law is to exist as a coherent system of law. Legal reform can be prompted at any time by evolving economic and technological factors or new judicial decisions. Consequently, a critical approach is essential, as it facilitates an examination of both the practice and theory of law. While the practice of law is central to this thesis, a normative perspective also demands a critical lens, particularly in assessing the effectiveness of current legal constraints on opportunism. Furthermore, the use of multiple methodologies in this work is required by the task at hand as it enables a deeper understanding of how current legal practices function and where they may fall short in addressing opportunism in commercial transactions. In this regard, the integration of various methodologies not only evaluates the moral dimensions of legal obligations but also critiques prevailing practices to advocate for meaningful reform. Ultimately, this thesis aspires to contribute to the ongoing debate about English law's role in promoting fair conduct in commercial relationships.

4. Scope

The thesis will explore how good faith is already regulating the contractual process and argue that such regulation is deserving of an independent doctrine in its own right, similar to the existing contractual principles. The research is focused on the laws within the jurisdiction of England and Wales; however, the text of the thesis only refers to English law for the purposes of brevity. It is important to set out the parameters of this research due to its extensive and fluctuating nature.

Firstly, the focus is limited to the contracts of commercial law. Commercial law itself is not easy to define as an area of law.[144] Roy Goode's definition, which was given in the context of encouraging codification of commercial law, suits the purpose of this thesis.[145] He

[143] Sanne Taekema, 'Theoretical and Normative Frameworks for Legal Research: Putting Theory into Practice' (February 2018) Law and Method 1, 10, 15.
[144] For an overview of the debate, see Gerard McMeel, 'Are There Any General Principles of Commercial Law?' in C Mitchell and S Watterson (eds), *The World of Maritime and Commercial Law: Essays in Honour of Francis Rose* (Hart Publishing 2020) 182-184.
[145] An alternative definition is provided by Harold C Gutteridge, 'Contract and Commercial Law' (1935) 51 LQR 91, 91 who defines commercial law as 'special rules which apply to contracts or the sale of goods and to such contracts as are ancillary thereto, namely contracts for the carriage and insurance of goods and contracts the main purpose of which is to finance the carrying out of contracts of sale.'

defines it as a '(…) body of law which governs commercial transactions, that is, agreements and arrangements between professionals for the provision and acquisition of goods, services and facilities in the way of trade.'[146] Indeed, this research is concerned only with transactions in which goods and services are exchanged for consideration, in addition to dealings where the parties collaborate to bring about the provision of such goods and services to third parties.[147] As such, laws applicable to institutions of trade, such as companies and partnerships, are excluded from this definition. The most relevant types would be contracts of sale and purchase, distribution, franchising, transportation or joint-ventures. Contracts which are, in essence, secondary to the transaction itself and operate in support of the main agreement, such as insurance or financing agreements, or commercial lease agreements, are also excluded from the scope of this thesis.[148]

Furthermore, transactions with customers, whether business-to-customer (B2C) or customer-to-customer (C2C), are also outside the scope of this definition.[149] It is the transactions between professionals which are relevant for present purposes. The breadth of consumer law is too extensive to be included in this research.[150] Although the transactions between non-professionals could also be relevant in terms of commercial practice, for present purposes, it would operate as a sub-category of consumer law rather than commercial law as defined above. Similarly, there is an area of digital law fast developing, which is concerned with online intermediation platforms, and the line between B2C and C2C contracts is starting to blur. Again, the number of laws applicable to online trading takes it out of the scope of this research.[151]

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[146] Roy Goode, 'The Codification of Commercial Law' (1998) 14 Monash University Law Review 141. Such a definition is also suitable because it does not import 'relational' contracts into the definition, a concept which he equates to 'long-term' contracts that build up a pattern of practices, co-operation and expectations [...],' Roy Goode, 'International Restatements of Contract and English Contract Law' (1997) 2(2) Uniform Law Review 231, 244.

[147] The term of revenue generating and sharing contracts (RGSC) is proposed for the latter type of transactions in chp 3.2.3.1.2.

[148] Such secondary type contracts usually obey more specific rules, such as insurance contracts' statutory provisions and a well-established notion of utmost good faith in that context, see Insurance Act 2015, ss 3, 14. See further chp 2.5 below.

[149] B2C means transactions between a business and consumers who are the end-users of its products or services. C2C means transactions between members of the public without recourse to businesses.

[150] Moreover, there is an unsettled debate as to whether the application of good faith in consumer law (notably as a test of fairness under the Consumer Rights Act 2015) is restricted to procedural concerns, such as the formation of contract and defective consent due to a 'significant imbalance' in the parties' relationship, or whether good faith encompasses a substantive duty in contract performance, see Davies, *JC Smith's The Law of Contract* (n 56) 229.

[151] For more on the subject, see Paola Iamiceli, 'Online Platforms and the Digital Turn in EU Contract Law: Unfair Practices, Transparency and the (Pierced) Veil of Digital Immunity' (2019) 15 European Review of Contract Law 392, 419-420.

Second, this research is only interested in 'objective' good faith. The doctrine sometimes refers to 'subjective' good faith or 'objective' good faith.[152] Subjectivity relates to the state of mind of a party, as in the case of a bona fide purchaser. The law presumes the good faith of the purchaser based on the purchaser's advertence to the relevant matter. It operates as a defence to instances of the transferor's defective title.[153] However, despite at common law the defence being synonymous with a subjective test of honesty, it includes an objective test of constructive notice in equity by reference to the conduct of a reasonable person in the defendant's position.[154] However, even in the context of the common law, the presumption of honesty can be rebutted if the seller can bring evidence to the contrary. Consequently, such rebuttal effectively discards any subjective assessment of honesty by reference to an objective one, which is based on the assessment of the external manifestation of the bona fide purchaser's state of mind.[155] Indeed, it is not a possible task, or a very difficult one, to attempt an investigation into the psyche of the party. Especially when analysing individual doctrines or guiding principles, the court's assessment of the parties' conduct must be carried out against an objective norm. This objectivity can only be measured by a material manifestation of the parties' intent. Therefore, the analysis of good faith in the context of this research has to be limited to the external, discernible and verifiable demonstrations of the intent upon which an assessment can be made.

Third, the thesis excludes considerations of good faith relating to negotiations which do not finalise in a concluded contract, including re-negotiation cases. This is usually referred to within the context of breaking off negotiations and confusingly as 'pre-contractual good faith.' A better description would be 'non-contractual good faith' or 'negotiation good faith'. However, it is different from considerations of good faith in the formation of the contract, arising in the 'pre-contractual' phase. These are better served by a 'pre-contractual good faith' designation, as this presupposes that a contract has been concluded but that the factors arising before the formation have affected the validity of the contract. For our purposes, both non-contractual and pre-contractual phases will be excluded. Moreover, termination and remedies

[152] Stapleton (n 47) 17.
[153] Graham Virgo, 'The Defence of *Bona Fide* Purchase' in G Virgo (ed), *The Principles of the Law of Restitution* (3rd edn, Oxford University Press 2015) 656.
[154] ibid 658.
[155] Also see Nick Sage, 'Reconciling Contract Law's Objective and Subjective Standards' (2023) 86 MLR 1422, 1445, who argues that both the subjective and the objective assessment embody an ethical ideal to guarantee a minimal requirement of decency in business dealings, thereby being complementary to each other and not mutually exclusive. The author defines commercial decency as 'uphold[ing] contractual seriousness and fair play and disapprov[ing] of unscrupulous advantage-taking.'

are also excluded, and the thesis focuses solely on the performance of contracts. Although some consideration is given to termination, this is only where it relates to the contractual performance issues, and not to the exercise of the contractual right of termination.[156] Furthermore, the thesis is concerned with the regulation of substantive fairness of primary obligations of the parties, as opposed to secondary ones, such as agreed damages clauses. Therefore, topics such as penalty clauses, which are classified as secondary obligations that deal with the consequences of the breach of primary obligations, fall outside of the scope.[157]

Fourth, the purpose of this research is to analyse good faith in English law. However, the experiences of other jurisdictions can inform the progress of English law. The laws of Australia are particularly relevant for the UK and especially will serve to illustrate the shortcomings of English law in tackling unfairness in contractual performance disputes in the context of franchising contracts in particular. It is not intended to be an exhaustive comparative study between two countries on the topic of good faith in general. The choice of Australian jurisdiction is based on a pragmatic approach. It is, like the UK, one of the biggest economies in the world, based on gross domestic product.[158] It is one of the trading partners of the UK with a common law system, and presumably, many of the contracts facilitating the trading are subject to the laws of either of the concerned trading countries.[159] Moreover, due to historical ties, Australia's legal system was developed from the English common law, which was inherited from the time of the European settlement in the eighteenth century.[160] Australian case law is relevant in English decisions.[161] In addition, the Australian franchise industry and the

[156] Such as *Socimer International Bank Ltd (in liq) v Standard Bank London Ltd* [2008] EWCA Civ 116, [2008] Bus LR 1304.

[157] Other agreed damages clauses are 'forfeiture clauses for deposits, clauses that require the party in breach to transfer property for a stipulated sum and clauses that entitle the innocent party to withhold money that she would otherwise have to pay under the contract,' see Prince Saprai, 'Rationalising the Penalties Rule' in Mindy Chen-Wishart and Prince Saprai (eds) *Research Handbook on the Philosophy of Contract Law* (Edward Elgar Cheltenham Forthcoming 2023), Faculty of Laws University College London Law Research Paper No. 16/2023, <https://ssrn.com/abstract=4551681> accessed 3 April 2025, 1, 5. In regards to a penalty clause, in *Cavendish Square Holding BV v Talal El Makdessi* and *ParkingEye Ltd v Beavis* [2015] UKSC 67, the court said that the clause must also be 'unconscionable' or 'extravagant' in light of any legitimate interest that the innocent party had in obtaining performance (3).

[158] Caleb Silver, 'The Top 25 Economies in the World' (Investopedia, 29 January 2025) <https://www.investopedia.com/insights/worlds-top-economies/#toc-measuring-gdp> accessed 3 April 2025. In 2025, UK is the sixth and Australia is the 13th largest economy in the world.

[159] Trading Economics, 'United Kingdom Exports By Country' (Trading Economics, 2024) <https://tradingeconomics.com/united-kingdom/exports-by-country> accessed 3 April 2025.

[160] Anthony M Gleeson, *The Rule of Law and the Constitution* (ABC Books 2000) 6.

[161] In *Al Nehayan* (n 48) [175], in discussing the content of the obligation of good faith, Leggatt LJ referred to the 'considerable body of Australian authority on the subject which has informed the interpretation by English courts of express contractual duties of good faith.'

enactment of good faith duties into law are supported by extensive parliamentary consultations, which showcase the transformative powers of the law for the market actors.

5. Meaning

Good faith is not a new concept. It has existed independently of any legal precepts for a long time. Its origin is usually traced back to the Roman times, and interestingly it even presumably predates such times. Indeed, it is argued by some authors that the concept was already present in the Bible.[162] The ingenuity of the Romans has been to convert the concept into a cause of legal action.[163]

Literature is full of attempts at defining the notion of good faith.[164] The most common one is to reference the idea in connection with moral norms such as honesty and integrity.[165] This approach involves an assumption as to the moral qualities of an actor in a given cultural and commercial setting. However, such parameters can and do change depending on the time and location of the commercial realities of the economic actors. When parameters change, the notion can evolve to take into account the cultural and economic realities of the times. It is the elusiveness and the flexibility of the concept that weaken its comprehensibility and draw much criticism.[166]

Another difficulty with the notion is that it does not easily lend itself to a systematic classification of the types of behaviour that could be categorised as good faith behaviour. An argument can be made that the flexibility of the notion caters for a fair assessment of the facts, as the circumstances of the parties can be taken into consideration, and the analysis can be made against the backdrop of the particularities of their agreement. When the notion itself is vague and each case requires an objective yet flexible assessment, the question arises as to what extent the objective, pre-determined rules of law can give way to vague, flexible legal concepts. In *Yam Seng*, Leggatt J stated that the test is an 'objective [one] in the sense that it

[162] Russell A Eisenberg, 'Commercial Law: Good Faith Under the Uniform Commercial Code - A New Look at an Old Problem' (1971) 54 Marquette Law Review 1, 9; Edward A Farnsworth, 'Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code' (1963) 30 University of Chicago Law Review 666; Edward Imwinkelreid, 'The Implied Obligation of Good Faith in Contract Law: Is it Time to Write Its Obituary' (2009) 42(1) Texas Tech Law Review 1.
[163] James J Stankiewicz, 'Good Faith Obligation in the Uniform Commercial Code: Problems in Determining Its Meaning and Evaluating Its Effect' (1972) 7 Valparaiso University Law Review 389, 407, citing Raphael Powell 'Good Faith in Contracts' (1956) 9 CLP 16, 22-28.
[164] See chp 1.3.3 below.
[165] Melvin A Eisenberg, 'The Principle of Good Faith in Contract Law' in MA Eisenberg (ed), *Foundational Principles of Contract Law* (Oxford University Press 2018) 707.
[166] For the main criticisms against its recognition in commercial law, see chp 1.2.

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.'[167] He even paired 'good faith' with 'fair dealing' to draw 'attention to the fact that the standard is objective and distinguished the relevant concept of good faith from other senses in which the expression 'good faith' is used.'[168] The assessment of whether the act is in good faith or not, therefore, quite often gives the impression that it is being made intuitively rather than by any pre-determined objective criteria. Indeed, the particularities of the context, albeit assessed objectively, still require an *ad hoc* evaluation on a case-by-case basis. This vagueness triggers and feeds the judiciary's fear towards good faith as a general principle applicable to commercial contracts. It is the main worry raised by the judges that such an indefinable and amorphous concept would put at risk legal certainty.[169]

Another approach taken in the literature is to define good faith as the opposite of bad faith. Law dictionaries define bad faith (*mala fide* in Latin) as an act performed fraudulently or dishonestly.[170] For example, bad faith conduct could be a dishonest use of a contractual discretion. The terms however are not always interchangeable and raise issues as to the definition of bad faith itself. For instance, although any act performed fraudulently will be carried out in bad faith, not all acts of bad faith will be classified as being made fraudulently. Indeed, in a fraudulent misrepresentation, the element of intent, namely to influence the other party to its detriment, might be lacking in some acts of bad faith. It could simply be a disloyal act that does not take into account the interests of the other party to a degree that it can be considered as carried out in bad faith, but short of any fraudulent intent. It could also be that the act is disloyal, but it does not breach any of the contractual obligations. In other words, a party to a contract might abide by the terms of the contract, but the act of compliance is not carried out in good faith. For instance, in *D&G Cars Ltd v Essex Police Authority*, Dove J preferred a reference to integrity rather than good faith to 'capture the requirements of fair dealing and transparency' in a long-term contract. He stated that an act which was not clearly dishonest but which 'compromise[d] the mutual trust and confidence between the parties (...)

[167] *Yam Seng* (n 3) [145]. Davies, *JC Smith's Law of Contracts* (n 56) 309 '[a]lthough the test is objective, it must take into account what the party actually knew.' The context-dependent nature of good faith requires that its assessment cannot be dissociated from the parties' knowledge however the yardstick against which the knowledge is assessed is an objective one.
[168] ibid [151].
[169] See chp 1.2.
[170] Jonathan Law, A Dictionary of Law (Oxford University Press 2018) <https://www.oxfordreference.com/view/10.1093/acref/9780198802525.001.0001/acref-9780198802525> accessed 3 April 2025.

without necessarily amounting to the telling of lies, stealing or other definitive examples of dishonest behaviour' would still be contrary to a requirement of dealing in good faith.'[171]

How is good faith understood in this thesis? In the context of contractual performance, it can be defined as a commitment to uphold the reasonable expectations of the parties involved, characterised by honesty, integrity, and fair dealing. This definition acknowledges that good faith is not a fixed notion but rather a flexible concept that must adapt to the cultural and economic realities of the time and context in which a contract operates. Good faith is primarily evaluated through an objective lens, centred around whether a party's conduct would be perceived as commercially unacceptable by reasonable and honest individuals within the relevant context. This objective assessment emphasises fairness and moral considerations while allowing for an *ad hoc* evaluation of each specific case. It recognises that an act may comply with contractual terms yet still fall short of the standard of good faith if it undermines mutual trust and confidence, even in the absence of dishonesty or fraudulent intent. Furthermore, while good faith is often contrasted with bad faith, it is important to note that not all actions that may be deemed as falling short of good faith involve dishonesty. Rather, good faith encapsulates a broader standard that promotes cooperative dealings and discourages opportunistic behaviour. Therefore, the essence of good faith in contractual performance lies in the balance between legal certainty and the adaptability of the notion to enhance fairness and integrity in contractual relationships.

Good faith does not have a widely accepted and precise definition in academia nor in case law. However, a precise definition is not necessary for it to be effectively applied in contract law. Indeed, concepts such as reasonableness in negligence or foreseeability in the assessment of damages, among others, also lack strict definitions.[172] The courts have simply addressed their vagueness and clarified them along the way. Therefore, instead of a strict definition, a clear framework is needed to advance the role of good faith in the performance of commercial contracts.

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[171] *D&G Cars* (n 49) 175.

[172] Richard Mullender, 'The Reasonable Person, the Pursuit of Justice, and Negligence Law' (2005) 68 MLR 681 683, expressing that ''reasonableness' creates a 'space' for judges to give authoritative expression to their understanding of 'ordinary moral reasoning' citing Herbert LA Hart, *The Concept of Law* (2nd edn, Clarendon Press 1994) 132-133. Moreover, foreseeability in the context of negligence is another vague term which has required judicial development over the years, see Helen Scott, 'The History of Foreseeability' (2019) 72(1) Current Legal Problems 287, 314, who examines it in its historical context to provide an insight 'into the variety of purposes which it is capable of serving.'

6. Outline of the Thesis

This thesis explores the role of good faith in English contract law, addressing its conceptual foundations, judicial treatment, and potential for reform. At its core, the analysis questions whether contract law, in its current form, adequately curbs opportunism and promotes fairness in commercial relationships. Through a multi-faceted approach, this study examines existing doctrines, judicial reasoning, legislative developments, and industry-led initiatives, ultimately arguing for a more coherent and structured role for good faith in contractual performance.

The discussion begins in chapter one, which explores the concept of good faith and investigates its contents and boundaries. It addresses the common objections raised against a general principle of good faith in contractual performance and challenges these concerns by arguing that fears of uncertainty or excessive judicial discretion are largely misplaced. It advocates for a balanced approach in which considerations of fairness should carry at least as much weight as freedom of contract. The chapter posits good faith as a normative standard that requires a deeper inquiry into the purpose of contract law itself, specifically, the reasonable expectations of contracting parties as honest actors. Additionally, it highlights the institutional role of contract law in preventing opportunistic behaviour during contractual performance. Despite its various definitions, the chapter ultimately emphasises that the core function of the concept remains the same, which is to ensure fair dealing in contractual performance by protecting the parties' reasonable expectations.

Building on this theoretical foundation, chapter two shifts focus to existing English legal doctrines that address unfairness in contracts, albeit in a fragmented manner. It critically examines the mechanisms currently used to regulate opportunistic behaviour, revealing their shortcomings and lack of coherence. A key focus is placed on the reform of insurance law, which has separated the duty of fair presentation from the utmost good faith in contract performance. This reform provides a lens through which to assess whether similar structural changes might be appropriate in general contract law. The chapter ultimately argues that the current piecemeal approach fails to provide a sufficiently robust safeguard against opportunism in commercial contractual performance and that a more systematic integration of good faith into commercial law is necessary.

While chapter two exposes the limitations of existing statutory and doctrinal responses, chapter three turns to judicial efforts to address opportunism through the implication of terms.

It first examines the general principles governing the implication of terms in contracts before narrowing the discussion to the specific judicial treatment of good faith. This chapter shows the limitations of restricting good faith to instances of implication in fact and highlights the difficulties of implying it in law, in particular based on a relational classification of contracts. Instead, it proposes an alternative classification, namely the revenue generating and share contracts. However, the chapter cautions against rigidly categorising contracts to imply good faith, warning that such an approach risks perpetuating the fragmented treatment of opportunism in contract law.

Chapter four moves toward a broader theoretical re-evaluation of good faith. It advocates for a more comprehensive approach to tackle unfairness by adopting good faith as an interpretative tool in contract law. It underlines the importance of a relational view of contracts, rather than a classical view which focuses on the adversarial nature of the relationship. The chapter draws inspiration from the evolution of the doctrine of frustration, which initially developed through implied terms before becoming a recognised legal principle in its own right. This historical parallel suggests that good faith could follow a similar trajectory. The chapter further contends that contracting out of good faith should not be possible, as this would be inherently contradictory to an understanding of good faith as the essence of the reasonable expectations of the parties.

To give a practical grounding to these theoretical arguments, chapter five turns to the specific context of franchising agreements. These contracts provide a compelling case study for the development of a good faith duty due to their long-term nature and inherent need for cooperation between the parties. The chapter examines the lessons that can be drawn from industrial codes of conduct and the Australian experience with statutory good faith obligations, both of which offer valuable insights for potential reforms in English law. A key challenge, however, is the lack of transparency and empirical data on how unfairness in the performance of franchising contracts is currently addressed. To remedy this, the chapter advocates for a regulatory approach similar to that adopted in Australia, one that invites stakeholder input, establishes oversight mechanisms, and ensures periodic evaluations of the effectiveness of good faith obligations. This is particularly relevant in contractual relationships where power imbalances persist throughout the agreement, not merely at its formation.

Finally, chapter six looks beyond the academic debate and case law. It explores various market initiatives to tackle the good faith gap in contracts. It explores various industry-led

initiatives aimed at addressing fairness in contractual performance, as well as the possibility of incorporating a statutory good faith duty within the framework of the UCTA 1977. However, this chapter also examines why a legal reform is necessary, but why recent and proposed reforms, including that of the UCTA 1977 and Digital Markets, Competition and Consumers Act 2024, fall short of providing a comprehensive solution. Industry codes serve as insightful initiatives into the reasonable expectations of certain groups of commercial actors in a specific industry. Indeed, the presence of good faith standards in such codes hints at a minimum level of ethical behaviour that needs to be present for that industry to continue to flourish. The chapter highlights that without a clearly defined standard in law, both judicial and market-based efforts to promote fairness will remain fragmented and inconsistent.

Taken together, these chapters build a case for a more structured and principled approach to good faith in English contractual performance. Rather than leaving good faith to develop in an *ad hoc* and inconsistent manner, this thesis advocates for its recognition as a foundational principle that underpins contractual performance. By integrating insights from theory, judicial reasoning, statutory reform, and industry practice, it aims to make an original contribution to the ongoing debate on the role of good faith in the performance of contracts in English law.

CHAPTER 1: THE CONCEPT OF GOOD FAITH

1.1. Introduction

Conceptualising a new principle requires investigating both its *raison d'être* and its practical elements. References to 'honest' dealings in the parties' contract, or 'reasonable' conduct when the court attempts to construe a contract, are not unusual in commercial disputes. Such norms are inherently difficult to define as they refer to mutable social norms. This confuses the plethora of vocabulary potentially available to the parties and the court in picking the right concept to cater to their specific needs. Another potential issue is determining whether they are interchangeable or whether their use should be exclusively restricted to certain scenarios. For instance, can a person's honest conduct be automatically classified as a reasonable act, or does reasonable conduct in the circumstances also equate to an honest performance? The inquiry of an overarching principle of good faith necessarily demands whether such norms should be grouped under it. As such,

> [t]hese duties are increasingly seen as expressing the core content of any general obligation of good faith that might be recognised in the common law of contract by holding the parties to fundamental values of loyalty and fidelity essential to the integrity of the contractual relationship.[173]

The extent of these good faith derived duties is inevitably constrained by the applicable contract. An overarching principle potentially aims to lift such restrictions in the pursuit of achieving the parties' expectations.

This chapter sets out to investigate the intricate nature of good faith within commercial contracts. It will explore the rationale behind the recognition or lack thereof of good faith as a guiding principle in contract law. By dissecting the complexities of commonly associated norms with good faith, such as 'honesty' and 'reasonableness,' it will highlight the difficulties faced by the courts and the parties in defining and applying these concepts.

Additionally, the chapter will analyse the ongoing debate between proponents and opponents of good faith duties, focusing on the key arguments against the acknowledgement of such a principle in commercial law, particularly concerns regarding legal certainty and the potential imposition of positive duties on contracting parties. The chapter will also consider

[173] Jeannie M Paterson, 'Good Faith Duties in Contract Performance' (2014) 14 Oxford University Commonwealth Law Journal 283, 284.

how good faith may enhance the fundamental norms of loyalty and fidelity that underpin contractual relationships, ultimately advocating for a more coherent understanding of good faith as a necessary element for achieving fairness in contractual dealings. By the end, the chapter aims to lay the groundwork for the subsequent exploration of how good faith obligations can be effectively integrated into contract law.

1.2. Arguments Against Recognising Good Faith in Commercial Law

The literature and case law are rife with opponents and proponents of good faith. While some reject the idea in its entirety, others recognise the need to mitigate the consequences of unfair outcomes in the contractual context. This part will explore some of the main arguments against recognising good faith in commercial law.

1.2.1. Threat to Legal Certainty

What is Certainty in Law?

Certainty and predictability in law are terms which are used interchangeably, with some authors preferring one over the other. Notably, Professor Roy Goode is one to prefer 'predictability', as he dislikes the term 'certainty', having stated that 'nothing in life is certain except uncertainty (…).'[174] A better view is to view predictability as a component of certainty rather than an alternative nomenclature. Certainty is much broader than the law's predictability. Predictability is an important factor why the courts treat similar cases consistently because '[t]he content of any particular law can only be understood in a meaningful way if its application to particular circumstances can be predicted.'[175] The nature of doing business requires a reasonable amount of predictability. Predictability means that parties can foresee with some degree of confidence whether a proposed course of action is likely to be lawful or not. Whether for repetitive or individually negotiated deals, the commercial actors will take into account the stance of the courts when it comes to taking calculated risks. All commercial activity will come with a risk, but businesses will attempt to minimise or avoid it by assessing and allocating it in various ways.

Legal uncertainty itself may comprise different components. For instance, the legal risk of litigation is different from legal uncertainty. Legal risk relates to the possibility of being sued

[174] Goode, 'The Codification of Commercial Law' (n 146) 150 (fn 36).
[175] Ian R MacNeil, 'Uncertainty in Commercial Law' (2009) 13 Edinburgh Law Review 68, 69.

or a technical defect in a transaction resulting in a loss.[176] The ambiguity of language is clearly prevalent and unavoidable even in the most meticulously drafted contracts. Where a word needs to be interpreted, it does not make its application uncertain. It simply means that the relevant context must be determined to ascertain its meaning. A classical view of contract law assumes that all commercial contracts operate in a context where the parties' interests are antagonistic.[177] It can be argued that this ultimately stems from the judiciary's distorted view of contract law, whereby many of the contractual parties would have become adversaries during the dispute resolution process, despite the majority of the contractual disputes being resolved outside of courtrooms.[178]

Legal risk is therefore broader than legal uncertainty because it can arise even where the law is clear. Legal uncertainty is where the drafting or application of the law itself creates a risk itself.[179] In commercial law, legal uncertainty is deemed to be twofold.[180] First is where litigation does not clear up all of the doubts underlying the uncertainty, either because the uncertainty was not the subject of the litigation, or because a court decision seems to affect the reliability of the established law, casting doubt on the reliability of that decision for future cases. The second type of uncertainty is where the courts change their stance on already established law. A well-established rule may not stand the test of time when it does not cater to the modalities of a new situation which could not have been anticipated when it was first set out. However, it is important that arbitrary judicial making is curtailed by the commercial actors' understanding and exercise of their rights. As such, legal certainty is also relevant to the parties' ability to make informed decisions and consequently, in creating efficient markets.[181] If the parties do not understand the possible legal consequences of their actions, they increase their legal risk and potentially may withdraw from the market altogether. Even when the parties are well-informed on their legal rights, any uncertainty in the law affects their ability to predict their judicial cost, and that in itself is reason enough for courts to remove legal

[176] ibid 70.
[177] *Walford v Miles* (n 69) 138, Lord Ackner's remarks in the pre-contractual context are a reflection of such an understanding. He had stated that 'a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations.'
[178] Scott C Styles, 'Good faith: A principled matter' in Forte ADM (ed), *Good Faith in Contract and Property Law* (Hart Publishing 1999) 171.
[179] ibid, legal uncertainty is seen as a subset of legal risk.
[180] ibid 70-71.
[181] ibid 71-72.

uncertainties as much and as soon as possible, to preserve or not to hamper the growth of the markets.[182]

Accordingly, while absolute certainty in law may be impossible, a reasonable degree of predictability remains essential for commercial parties to assess and manage legal risk. Where legal uncertainty persists, whether through unresolved litigation, ambiguity in drafting, or shifts in judicial interpretation, it increases legal risk and undermines confidence in the exercise of legal rights. It is therefore important that courts address legal uncertainty wherever possible, to enable commercial actors to operate with confidence and to support stability in commercial relationships, with an understanding that addressing legal uncertainty does not automatically eliminate the potential for legal risk.

Choice of Law in International Commercial Contracts

English law has been and continues to be one of the preferred choices of law, and London one of the preferred choices of forum, for resolving international commercial disputes. About 73% of the Commercial Court's caseload in England and Wales is made up of international disputes, and that has been the case for the past two decades.[183] Similarly, according to the information published by the International Court of Arbitration which is run under the auspices of the International Chamber of Commerce (ICC) in Paris, in 2023 the most frequently selected substantive law was English law with 131 cases (15% of all cases), followed by Swiss law (83 cases) followed by the laws of a US state (81 cases), then by German law (62 cases), by Mexican law (35 cases), French and Spanish law (33 cases each), Brazilian law (29 cases) and Italian law (25 cases).[184] Given that 2,389 parties were involved in cases filed in 2023, 31% of cases were multiparty cases, with most frequent nationalities among parties being USA (10.84%), Germany (4.65%), Mexico (4.65%), Spain (4.35%) and United Arab Emirates

[182] ibid 72. Also see Oxera for LegalUK (n 12) para 3.2, which posits that '[w]hen there is uncertainty surrounding a potential transaction, parties will price in the risk of that uncertainty, leading to higher transaction costs.'
[183] Courts and Tribunals Judiciary, 'Business and Property Courts, The Commercial Court Report 2022-2023 (Including the Admiralty Court Report)' (*Courts and Tribunals Judiciary*, 2024) <https://www.judiciary.uk/wp-content/uploads/2024/03/14.448_JO_Commercial_Court_Report_2223_WEB.pdf> accessed 3 April 2025, 18-19.
[184] International Chamber of Commerce, 'ICC Dispute Resolution 2023 Statistics' (*International Chamber of Commerce*, 2023) <https://iccwbo.org/wp-content/uploads/sites/3/2024/06/2023-Statistics_ICC_Dispute-Resolution_991.pdf> accessed 3 April 2025, 12.

(3.52%). Swiss parties represented 2.76% and United Kingdom represented 1.97%.[185] Despite leaving the EU, English law remains an attractive option.[186]

In line with the previous years' publications,[187] the Law Society of England and Wales continues to sing the praises of English law to commercial actors, and the English forum for dispute resolution, whether through public courts or arbitral institutions. It attributes such a strong preference for English law and courts to the strength of the law, the jurisdiction, and the legal professionals of England and Wales, as well as to London's attraction as a seat of arbitration.[188] In particular, it ascribes English law's predictability to two factors: first, to the principle of precedent; and second, to the judiciary's non-interventionist approach.[189] Concerning the latter factor, it states that

> [c]ommercially oriented judges assess disputes based on the terms of the written contract between the parties and do not enforce a general duty of good faith unlike judges in many other jurisdictions.[190]

Clearly there is an understanding amongst practitioners of English law that the lack of an overarching principle of good faith contributes to the predictability of the law. It would be useful to compare such an understanding to empirical data. For instance, a recent study has reviewed recent empirical studies on the choice of laws and forum of commercial parties and identified ten important factors.[191] Unsurprisingly, amongst these factors is one which relates to the content of the substantive law.[192] However, the lack of empirical data as to the precise reason behind each category makes it impossible to determine the weight given by commercial actors to whether the principle of good faith is given any consideration. The available data also does not indicate whether the parties consider that the predictability of English law cases would be jeopardised if an overarching principle of good faith existed. Other factors indicated in the abovementioned study are familiarity with a legal system, arbitration friendliness (if arbitration

[185] ibid 4, 21.
[186] See eg Peter Gross, 'A Good Forum to Shop in: London and English Law Post-Brexit' (2018) 2 Lloyd's Maritime and Commercial Law Quarterly 222, 222-233; Louise Merrett, Antonia Sommerfeld, 'Incentives for Choice of Law and Forum in Commercial Contracts: Predicting the Impact of Brexit' (2020) 28(3) European Review of Private Law 627.
[187] Hein. Kötz, 'The Jurisdiction of Choice: England and Wales or Germany?' (2010) 18 European Review of Private Law 1243.
[188] Law Society of England and Wales, 'Global Legal Centre' (*The Law Society of England and Wales*, 2025) <https://www.lawsociety.org.uk/campaigns/england-and-wales-global-legal-centre> accessed 3 April 2025.
[189] ibid.
[190] ibid.
[191] Merrett, Sommerfeld (n 186).
[192] ibid 638.

is envisaged as a form of dispute resolution), the legal tradition (whether common or civil law), the language used, the neutrality of the law as perceived by the parties, the stability of the legal system as perceived by the parties, the predictability of the outcome as perceived by the parties, the forum, and the presence of a large financial, insurance and re-insurance sector.[193] Other authors include similar factors such as familiarity with a legal system, the quality of the law which cater to the specific needs of the parties, the predictability of decisions, laws and stability of the laws as perceived by the parties, the neutrality of the laws as perceived by the parties, and the location of internationally active law firms as the lawyers would advise their clients to choose the law which they are the most familiar with.[194]

The substance of the law, or the tradition of common law or civil law is particularly relevant to the topic of good faith. Indeed, a long-standing debate of legal origins has attempted to determine whether an argument of 'superiority' of common law compared to civil law in the commercial world has any reasonable standing. Voigt has relied on empirical evidence to dispel such myth.[195] In reviewing the evolution of the doctrine, he noted that in the second half of the 20th century, the doctrine relied on a sharp divide between the two systems, common law being described as more stable (i.e. certain) compared to civil law as the latter could 'radically be changed overnight,' and the former being more efficient because the common law process tends to favour efficient rules.[196] Efficient rules being less likely to be litigated, this presumably adds to the predictability of the law.[197] However he agrees with other authors from the late 20th century that the difference between the two systems is overstated in particular with respect to substance.[198] This is further supported by the fact that many common law countries have embraced a principle of good faith in commercial contracts. Indeed, USA, Australia, New Zealand, Canada have all recognised it in different formats.

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[193] ibid 638, 642, 643, 661.
[194] Stefan Voigt, 'Are International Merchants Stupid? Their Choice of Law Sheds Doubt on the Legal Origin Theory' (2008) 5 Journal of Empirical Legal Studies 1, 10-12. For an overview of the debate on choice of law, see Jonathan Morgan, C*ontract Law Minimalism: A Formalist Restatement of Commercial Contract Law* (Cambridge University Press 2013) 184-189.
[195] Voigt (n 194) 1.
[196] ibid 4, citing (1) Friedrich A Hayek, *The Constitution of Liberty* (University of Chicago Press 1960), (2) Bruno Leoni, *Freedom and the Law* (3rd edn, Indianapolis: Liberty Fund 1991), (3) George L Priest, 'The Common Law Process and the Selection of Efficient Rules' (1977) 6 Journal of Legal Studies 65, and (4) Paul H Rubin, 'Why is the Common Law Efficient?' (1977) 6 Journal of Legal Studies 51.
[197] Priest (n 196) 72.
[198] Voigt (n 194) 4, citing (1) Richard A Posner, 'Formal Versus Substantive Economic Theories of Law' in Richard A Posner (ed), *Law, Economics, and Democracy: Three Lectures in Greece* (Sakkoulas Publishers 2002), and (2) Konrad Zweigert, Hein Kötz, *An Introduction to Comparative Law* (Tony Weir tr, 3rd edn, Oxford University Press 1998).

In international transactions, commercial actors, who have the freedom of choice of applicable substantive law, are not bound by their home countries' laws. They can opt for the laws of an entirely different system. And they do. As the numbers set out in the ICC's arbitration statistical report show, the nationality of the parties and the choice of the substantive law do not always correlate.[199] If common law were far superior to civil law, all commercial actors, regardless of their nationalities, would prefer the common law. Of course, this is not the case. Indeed, recent empirical surveys confirm that although businesses do tend to prefer the laws of their home jurisdiction in some cases, for the most part, English law is the prevailing choice in international commercial contracts.[200] The same is true for the choice of forum in favour of English courts. Even English businesses, who presumably could prefer the laws and forum of other jurisdictions, almost exclusively opt to subject their contracts to English law and courts. Despite the lack of empirical data on the role of good faith in these statistics, a reasonable assumption can be made that the presence of good faith obligations in civil law countries does not act as a strong enough deterrent to shy commercial actors away from the civil law. To the contrary, the presence of good faith duties in common law countries, such as the US, does not impede the laws of these countries from being chosen by international commercial actors.

Collins' approach also supports the above argument. He refutes the assumptions that by policing the fairness of contracts, the law is rendered uncertain, and stops being a 'predictable source of support for their exchange' which 'may draw them towards less optimal transactions or prevent them from reaching a deal at all.'[201] The potential invalidity of terms in contracts does not weigh on the parties' decision-making process in entering into that contract. The parties' priority is to get on with the deal, and not sour the relationship with legal talk. Indeed, '[w]hen contracts are primarily sustained by trust and non-legal sanctions, which they usually are, uncertainty about legal enforceability is unlikely to make any difference to the calculations of the parties whether or not to run the risks of betrayal and disappointment.'[202] Moreover, some uncertainty is to be welcomed, not shunned. Flexible 'open-textured standards' are what businesspeople seek in the law, as these can accommodate the variety of market customs and the particularities of each transaction.[203] However, viewing the law as a

[199] ICC (n 193).
[200] For an overview of the results in respect of recent empirical studies on choice of law and forum, see Merrett, Sommerfeld (n 186) 635-636.
[201] Collins, *Regulating Contracts* (1999) (n 111) 268, 269.
[202] ibid 270.
[203] ibid 271.

commodity to be exported is also problematic.[204] Indeed, the law is a 'public and social good which should reflect, as far as possible, the value to which society aspires.'[205] Consequently, the recognition of good faith in contractual performance should not be driven by the interests of those in a stronger bargaining or market position.

Empty Threats of Uncertainty

If many international businesspeople do not shy away from other jurisdictions with good faith duties, how credible is the legal community's issue with certainty when it comes to embracing a good faith doctrine? McKendrick is inclined to accept good faith's organisational capacity in contract law, but draws a limit where it imposes on contracting parties a more onerous obligation than that contained in the contract.[206] Andrews argues that introducing a general good faith duty to cover all aspects of contractual performance would provoke a good faith 'big bang' which would require re-examination of the established doctrine.[207] Similarly, Cartwright also prefers to give effect to the intentions of the parties and avoid recognising an overarching good faith which would impose positive duties in all contracts.[208] Such an introduction would not be welcomed as the courts would have to deal with uncertainty until good faith acquires more certainty in its application. This is a circular argument; if the uncertainty is not removed, then the notion stays uncertain, but to gain more clarity, it must be dealt with by the courts and its meaning and application elucidated. Andrews argues that the benefit to be obtained by adopting an overarching principle would be curtailed by the anxiety and uncertainty experienced within the legal profession when advising their clients, and the courts might treat it as an empty affirmation of the common law and equity's dedication to catering to unfair outcomes.[209] He contends that 'the values of commercial certainty and predictability, and the need to keep the law rooted in the ordinary or reasonable expectations of businesses and consumers, would have a salutary restraining effect upon the good faith principle.'[210]

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[204] Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 149.
[205] Mindy Chen-Wishart and Victoria Dixon, 'Good Faith in English Contract Law: A Humble '3 by 4' Approach' in PB Miller, J Oberdiek (eds) *Oxford Studies in Private Law Theory* (Oxford University Press 2020) 194.
[206] Ewan McKendrick, 'Good Faith: A Matter of Principle?' in ADM Forte (ed) *Good Faith* (1999 Hart Publishing) 59.
[207] Neil Andrews, *Contract Law* (Cambridge University Press 2015) 599.
[208] John Cartwright, 'Good Faith in English Contract Law: Lessons from Comparative Law?' in E Peel and R Probert (eds), *Shaping the Law of Obligations: Essays in Honour of Professor Ewan McKendrick KC* (1st edn, Oxford University Press 2023) 37.
[209] Andrews, *Contract Law* (n 207) 590, 599.
[210] ibid 599.

MacNeil understands that the reality of practising commercial law is to embrace the inevitable existence of legal uncertainty.[211] Indeed, contracts are seen as instruments to allocate such risk.[212] Despite the perceived need for legal certainty to facilitate commercial transactions, uncertainty may persist over long periods in commercial law.[213] He acknowledges that there is a close link between effective responses to uncertainty and the length of uncertainty over time.[214] Where legal certainty in commercial law cannot be achieved, the result may not be as catastrophic as imagined. The significance of legal uncertainty is proposed to be low so long as an adequate response is available. Such responses in commercial law may be numerous.

The first response explored by MacNeil is eliminating or reducing uncertainty through contract terms.[215] The parties can, for instance, include specific provisions in a contract where they clearly provide for scenarios for the termination of the contract. While tailoring the contract is likely to cater to the parties' circumstances, the risk is that the courts may construe the contract differently to what the parties had originally envisaged. The purpose of this process is to remove the uncertainty for a mutual benefit. The second response is allocating or transferring risk arising from legal uncertainty through contract terms.[216] This is done where both (or one of the) parties foresee a risk at the time of contracting and thus allocate the risk to either one party, or a third party through for instance insurance. However, where legal risk is not included in the insurable risk, the parties must bear it themselves. A third response is labelled as creative compliance.[217] This is where the parties on surface seem to comply with the letter of the law but the benefit obtained is contrary to its purpose. As such, uncertainty may offer a benefit to the parties. This can be done through searching for loopholes in the rules to use any gaps or exceptions to their advantage.[218] It can also be achieved by structuring commercial deals to fall outside the scope of a rule which regulates a commercial activity.[219] Another way of ensuring creative compliance is by narrowly focusing on the literal meaning of the rule, while disregarding a higher normative principle which cannot directly apply to the circumstances.[220] A fourth response is clearance, guidance and legal opinions.[221] This is where

[211] MacNeil, 'Uncertainty in Commercial Law' (n 175).
[212] See for instance, Jonathan Morgan, *Great Debates in Contract Law* (Bloomsbury Publishing Plc 2020) 182.
[213] MacNeil, 'Uncertainty in Commercial Law' (n 175).
[214] ibid.
[215] ibid 81.
[216] ibid.
[217] ibid 82-83.
[218] ibid 82.
[219] ibid.
[220] ibid 83.
[221] ibid 83-84.

certain regulatory authorities issue decisions that apply to a whole industry or set of transactions, clearing the legal risk in certain circumstances. The regulatory authority can also provide guidance on how it will interpret certain rules or how it will approach specific scenarios. Legal opinions are also efficient in dealing with legal uncertainties where the transactions operate within such markets, as both the market actors and the regulators rely on these opinions.[222] Consequently, various methods exist to reduce or eliminate legal uncertainty, which may not entirely be eliminated in any event; therefore, invoking an argument of legal uncertainty against introducing good faith into commercial law is inherently flawed and unreasonably undermines the development of the law.

The Argument of Efficiency

When uncertainty is met with efficient responses, it is more likely that commercial actors can tolerate it better than when there are no appropriate and effective remedial responses. This can cause the parties not to litigate uncertainties that may have been resolved by the courts much earlier. Moreover, to add to the efficiency debate discussed above, certainty can add to the efficiency of the common law rules, where the more certain the rule, the less likely that it will be litigated.[223] As such, certainty helps develop efficient rules, but inefficient responses to uncertain rules provide a hurdle in clearing out the legal uncertainties.[224] Posner adopts an economic view of the judicial process in arguing that the common law will favour rules that impose fewer costs that will overall promote efficient outcomes in each case, but also in aggregate.[225] Priest provides an alternative view. He concurs that common law is characterised by a judiciary process that is subject to forces pressing toward efficiency.[226] He argues that inefficient rules are deemed to be discarded, as they impose greater costs than efficient ones on the parties subject to them.[227] Priest's argument differs from Posner's in that it does not rely on the judges themselves preferring or making efficient decisions. Rather, the argument is that the common law process itself will 'restrain and channel judicial discretion so that the legal rules in force will consist of a larger proportion of efficient rules than the bias or the incapacity of

[222] ibid 84; the example provided by the author is the legal opinion by the International Swaps and Derivatives Associations on netting of debts which provides opinions (which are provided by a major law firm in each country and annually updated to reflect any changes in law and regulation.)
[223] See text to n 196-197 above.
[224] MacNeil, 'Uncertainty in Commercial Law' (n 175) 78.
[225] Richard A Posner, *Economic Analysis of Law* (7th edn, Aspen Publishing 2007) 249-253, 555-639.
[226] Priest (n 196).
[227] Aditi Bagchi, 'Distributive Justice and Contact' in G Klass, G Letsas, P Saprai (eds), *Philosophical Foundations of Contract Law* (Oxford University Press 2014) 209-210 also argues that '[w]here a regulation alters the default away from the one preferred by most parties, parties will either incur the costs of opting out or if, those are prohibitively high, they will either forgo contract altogether or operate under the inferior term.'

judges might otherwise permit.'[228] Indeed, efficient rules are less likely to be relitigated and changed, whereas inefficient rules are more likely to be discarded because they are more likely to be reviewed and changed. As such, the litigants are in the driver's seat, not the judges.

Similarly, Rubin also argues that parties will litigate inefficient rules rather than efficient rules.[229] Therefore, both authors agree that it will be the behaviour of the litigants rather than that of judges that will affect the evolution towards more efficient rules.[230] As such, the common law is characterised by the lawmaking power of its judges, but also by that of the litigants who participate in the lawmaking process through the cases they choose to litigate before the courts. The more an inefficient rule is litigated, the more likely that it will become efficient and be less litigated over time. As good faith is making its way into the contractual disputes before the courts, it is not implausible that over time the rules relating to the application of good faith will become more efficient, and consequently more certain. Common law's inductive methodology provides for an efficient approach to rule selection, and good faith will certainly not be spared from the evolutionary betterment of its application.

In sum, the argument that good faith would unsettle legal certainty seems to be a knee-jerk reaction to a legal novelty, akin to antibodies reacting to a virus in the body. Lord Leggatt SCJ's response to perceived uncertainty is on point and should provide a good basis to move past the concerns on certainty:

> (...) it is of value that the law should be certain, but I think first of all it would be wrong to exaggerate how much uncertainty there would be in a principle of good faith. At least in the way I conceive it, it is a fairly modest principle. Also, one can exaggerate, I think, the degree to which there is certainty in any event. For example, interpreting contracts often gives rise to questions which judges take different views about, and such cases sometimes reach the Supreme Court, so one cannot avoid uncertainty altogether, nor should one.[231]

Therefore, a crucial aspect of legal efficiency is the adaptability of common law to commercial realities.[232] Legal rules that evolve in response to litigants' needs ensure that

[228] Priest (n 196) 66.
[229] Rubin (n 196).
[230] ibid 63.
[231] George Leggatt, 'The UKSC Blog interviews Lord Leggatt' (*UK Supreme Court Blog*, 25 November 2021) <http://ukscblog.com/the-uksc-blog-interviews-lord-leggatt/> accessed 3 April 2025.
[232] Puig (n 12) 318, this argument supports the facilitative role of commercial role rather than its regulative one. Indeed, this is seen as 'derivative of the larger mission of the common law to meet the very different needs of the community for direction in the marketplace and, of course, elsewhere.'

the law remains relevant and functional. If a legal rule proves inefficient by generating excessive disputes, failing to provide clear guidance, or imposing unnecessary costs, it naturally invites challenge and refinement. This process fosters a self-correcting legal system where inefficient doctrines are gradually replaced with rules that better serve economic and practical interests. The iterative nature of litigation means that, over time, the most frequently contested areas of law will produce clearer and more predictable principles. In this way, the incorporation of good faith into commercial law follows the same trajectory: as courts refine its contours through case law, the principle will become more precise, reducing uncertainty and promoting efficiency. Thus, rather than disrupting certainty, the recognition of good faith will contribute to a more coherent and commercially responsive legal framework.[233]

1.2.2. Incompatibility with Commercial Law, Contract Law and Common Law

Commercial law, as understood in this work, relies on Goode's definition as set out in the introduction.[234] Although some parts of commercial law go through change at different times and rates, other parts are slower to respond to business needs.[235] Rigid rules cannot be compatible with the ever-changing needs of commercial practices.[236] Yet its essential function is to 'allow, so as far as it can, commercial men to do business in the way that they want to do it and not require them to stick to forms that they think to be outmoded.'[237] This liberal view of commercial law materialises through an array of prohibitive, mandatory or default rules, and efficient dispute resolution. However, the need for legal certainty and fairness requires that commercial law adopts a flexible approach to dispute resolution. Eliminating gaps or inconsistencies in the application of the law requires that flexible standards, such as that of good faith, can respond to a variety of legal challenges raised in a given case. Indeed, a legal system needs to balance 'between the competing demands of discretion or flexibility, on the

[233] ibid 325, the pursuit of certainty is posited as the primary reason for the misalignment between commercial law and commercial practice.
[234] See text to n 146 in Introduction above.
[235] For instance, because they are subject to external regulatory pressures such as in the case of the EU consumer regulations.
[236] George Leggatt, 'What is the Point of Commercial Law?' The Fourth Jonathan Hirst Commercial Law Lecture (*Supreme Court*, 2 November 2021) <https://supremecourt.uk/uploads/what_is_the_point_of_commercial_law_eea1e25f15.pdf> accessed 3 April 2025, [12], [49] clearly expresses that 'the point of commercial law is to facilitate commerce.' To achieve this aim, commercial law must provide 'effective procedures for enforcing agreements between commercial parties.'
[237] *Kum v Wah Tat Bank Ltd* [1971] 1 Lloyd's Rep 439, 444 (Lord Devlin).

one hand, and doctrine and certainty, on the other.'[238] Therefore, maybe more so than in any other area of law, commercial law makes space for flexible standards to help the court decide a vast array of circumstances and diverse situations.[239] Consequently, the argument that good faith is incompatible with contract law must be disregarded.

Another incompatibility which is argued is one with the common law. Bridge rejects good faith and any interference in the parties' agreement on the grounds of fairness. [240] He contends that '(...) good faith and fair dealing (...) is an imperfect translation of an ethical standard into legal ideology and legal rules;' that 'good faith is an invitation to judges to abandon the duty of legally reasoned decisions and to produce an unanalytical incantation of personal values;' and that '[f]ar from involving the community ethic in the day-to-day task of law-making and decision-making, with the attendant fruits of such a democratization, good faith is more likely to produce idiosyncratic judgments.'[241] His restrictive approach requires that if good faith were to be admitted, it would have to be on a minimal basis, where it would cause minimal damage. As such, he refers to good faith as a 'bull in the China shop marauding unrestrained through the carefully curated china shop of English contract law.'[242] Such a restrictive strategy is inevitable because it relates to the incremental nature of the common law. Rather than unleashing a revolutionary change, a common law judge would prefer to anchor their reasoning in existing law. Even Leggatt J in *Yam Seng*, as a proponent of good faith, sanctioned it by 'following the *established* methodology of English law for the implication of terms.'[243] As such, good faith as an independent cause of action does not find support in the literature. Similarly, Chen-Wishart argues that such an approach would pose a threat to contractual freedom and certainty, and would contradict the common law's aversion to general principles and preference for 'cautious incrementalism.'[244]

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[238] Ewan McKendrick, 'Doctrine and Discretion in the Law of Contract Revisited' (2019) 7(1) The Chinese Journal of Comparative Law 1, 4.
[239] ibid 5-9, citing Guenter H Treitel, *Doctrine and Discretion in the Law of Contract* (Clarendon Press 1981), Such as the creation of innominate terms, the extension of duress to the person to encompass economic duress, the date of assessment of damages usually being the date of breach except where this would give rise to injustice are just a few of the examples where the courts show flexibility in the exercise of their power.
[240] Michael Bridge, 'Does Anglo-Canadian Contract Law Need a Doctrine of Good Faith?' (1984) 9 Canadian Journal of Business Law 385.
[241] ibid 412-413.
[242] Michael Bridge, 'Doubting Good Faith' (2005) 11 NZBLQ 426, 430.
[243] *Yam Seng* (n 3) [132] emphasis added.
[244] Mindy Chen-Wishart, *Contract Law* (7th edn, Oxford University Press 2022) 627; she further reinforces this argument by referring to the US Uniform Commercial Code, s 1-304, which imposes a mandatory duty of good faith in performance, but explicitly states that it does '*not* create a separate duty [⋯] which can be independently breached.'

Common law is often described as having a more individualistic approach, contrasted to the civil law's more communitarian influences.[245] Teubner, as one of the main proponents of this argument, dismisses any 'transplants' from one legal system to another.[246] He argues that the imposition of a foreign rule causes a 'legal irritant' which is not inherently negative, but operates as a catalyst for disruption and reconstruction within the receiving legal system rather than straightforward integration. The foreign rule is transformed in the process, while also reshaping the domestic system itself. This account nonetheless presumes that legal development occurs through internal systemic evolution rather than through direct or deliberate borrowing from other legal systems, since their experiences are treated as significantly different. It is argued herein that Teubner's view of legal development would deprive the development of good faith in English law of the benefits that comparative law could provide, even where comparative analysis results in diverging concepts across legal systems. Although good faith, for instance, in civil law countries is codified and worded to reflect cultural differences, an English concept of good faith will not necessarily have the same requirements if expressly recognised. The refinement of the concept will eventually come after it is recognised as a principle in its own right. Given that existing principles already are capable of forming a principle of good faith, rather than being an import, a principle of good faith can already be developed within English contract law. Considering the legal history of the common law, English contract law is no stranger to the adoption of general principles in equity to curb the strictness of the common law rules.[247] This is also recognised by Lord Leggatt SCJ in presenting a conception of good faith not as a civil law imposition where it can be perceived as a dangerous tool to override the parties' agreements, but a common law development, which is 'rooted in the parties'' agreement and seeks to uphold the justified expectations arising from that agreement.'[248] He recognises that the concept will not be the same as that of a codified civil law provision; nonetheless, it can still play an important role in the development of

[245] For instance, see Reinhard Zimmermann & Simon Whittaker (eds), *Good Faith in European Contract Law* (Cambridge University Press 2000) 698-699; Gerard McMeel, 'Foucault's Pendulum: Text, Context and Good Faith in Contract Law' (2017) 70(1) CLP 365, 388.
[246] Teubner (n 51) 20.
[247] Alan Schwartz, Robert E Scott, 'The Common Law of Contract and the Default Rule Project' (2016) 102 Virginia Law Review 1523, 1538-1539.
[248] George Leggatt, 'Contractual Duties of Good Faith' (*Courts and Tribunals Judiciary*, 18 October 2016) <https://www.judiciary.uk/wp-content/uploads/2016/10/mr-justice-leggatt-lecture-contractual-duties-of-faith.pdf> accessed 3 April 2025.

English law.[249] A comparative study can also always help to inform the refinement process and contribute to its conceptual cohesion.

Moreover, the courts' lawmaking power is not dissimilar in civil and common law jurisdictions. Courts do create law in civil law countries, same as in the common law jurisdictions. As Hesslink argues, this is done through the interpretation process of abstract rules. He states that 'applying the law necessarily implies creating it.'[250] Even when the rules are written in a code, the rules are abstract concepts that need to be applied to concrete cases, and their application is not fixed and immutable. The issues the court may face, as Hesselink explains, are threefold. First, the court must ensure that the facts defined in the rule and the facts at hand overlap, or that the remedy requested by a party corresponds to that provided for in the rule.[251] Secondly, the court must determine if the facts at hand that do not correspond exactly to those in the rule can be deemed as equivalent to justify the rule's application, or the remedy requested can be deemed to be equivalent to that in the rule. Thirdly, if the facts provided in the rule have occurred, the court must then decide if any other facts in the case influence the applicability of the rule. For the purposes of certainty, the court must continue to approach subsequent cases with the same methodology. As Hesselink argues, 'justice requires like cases to be treated alike,' reminding that 'in most systems the right to equal treatment is even constitutionally protected.'[252] As such, there is no difference between the court's role in concretising abstract rules through interpretation. Therefore, a court's approach to good faith in practice raises the same conundrums in both systems of law. If the civil law were able to codify and apply it through the judicial interpretation process, the same should also be possible for the common law. If similar cases are to be treated alike, then ascertaining the instances of application of good faith should help with legal certainty, not hinder it.

1.2.3. Threat to Freedom of Contract

As much as legal predictability is important, so is freedom of contract. In English law, the parties are free to agree on the content of their agreement within the limits of public policy.

[249] Leggatt, 'The UKSC Blog interviews Lord Leggatt' (n 231), '(...) I think the history and culture of England and Wales does mean that we are unlikely to accept, for example, a general duty of good faith of the kind that is embodied in the French Civil Code. But I don't think that means there isn't room for such a principle in English law, and indeed there has been such a principle in the past. It has actually played, for example, an important role in the development of English insurance law, so I don't see why it shouldn't again in our law in the future.'
[250] Martijn W Hesselink, 'The Concept of Good Faith' in S Hartkamp, MW Hesselink, EH Hondius, C Mak & CE Perron (eds), *Towards a European Civil Code* (4th edn, Kluwer Law International 2011) 636.
[251] ibid, Hesselink gives the example of whether lost profit constitutes part of the damage that must be repaired.
[252] ibid.

Freedom of contract is also referred to as party autonomy. This is because under the classical view of contract law which has favoured the will theory since the 19th century, parties are seen as autonomous and self-reliant.[253] Contractual obligations of the parties derive from their will and as such, contracts are considered in law as 'sacred,' the rationale of which is

> directly traceable to their early religious and ecclesiastical associations, their protection by the Court of Chancery as a court of conscience, their importance to international merchants as the foundation of credit, and the prominent place that the individual freedom which they fostered held in the eyes of nineteenth-century jurists and political philosophers.[254]

If the parties can look after their own interests, then there would be no basis upon which the court would need to intervene in their relationship. The idea of a good faith principle seems at first to be at odds with party autonomy. If parties are autonomous, then they can look after their interest, and whether the act is done in good faith should not be relevant. Brownsword argues that the proponents of a good faith principle have limited solutions by:

> arguing that any exceptions to this default are actually consistent with the classical principle of freedom of contract, or that they are strictly defined, or that they are confined to special pockets of consumer law; or, more ambitiously, that a default ethic of co-operation has better economic or ethical credentials.[255]

Regardless of its importance, the will theory cannot explain the entire set of rules that make up contract law. For instance, the doctrines of frustration, mistake or duress do not derive from the parties' free will. An alternative theory is needed to explain the basis of such doctrines. Although there is no consensus on what this should be, various propositions have been made in the literature.[256] Collins suggests that party autonomy should not be restricted to mean that all contracts entered into freely are valid, especially where it leads to an understanding of autonomy which may force the parties to remove themselves from the market 'by expropriating

[253] Parry (n 8) 15-17.
[254] ibid 18.
[255] Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 90.
[256] Duncan Kennedy, 'Form and Substance in Private Law Adjudication' (1976) 89 Harvard Law Review 1685, (proposes altruism as a complementary basis for contract law); Richard A Posner, 'Utilitarianism, Economics, and Legal Theory' (1979) 8 Journal of Legal Studies 103 (argues that contract law's basis should have an ideal of wealth maximisation); A Kronman, 'Wealth Maximization as a Normative Principle' (1980) 9 The Journal of Legal Studies 227 (argues that contract law should be a tool for redistributing wealth).

all their wealth.'[257] He proposes that other interpretations of party autonomy should be possible and, as such, allow it to be restricted:

> [w]e can argue, for instance, that we should only respect autonomous choices to the extent that they do not destroy autonomy in the future. Alternatively, respect for autonomy might be limited to a broad range of worthwhile choices.[258]

The liberal contract theory might have shaped the common law and many of its principles but these are tempered by the application of principles which favour other ideologies, such as socio-economical or moral.

The freedom to contract is usually understood as having a positive and a negative dimension. The first ensures that the parties can decide on the content of their contract freely, and the second prevents any terms they did not agree on from being imposed upon them.[259] Although the argument for negative freedom is strong, it is limited. Law allows for intervention into private contracts through the use of illegality and or public policy doctrines. These doctrines exist because contract law inherently cannot deny the existence of the state's power in individual contracts.[260] Whether one ideology is preferred over the other will be a balancing act for the judge in question. Freedom of contract and party autonomy might prevail over considerations of fairness, and vice versa. Where the contract is seen as an expression of the parties' autonomy, then a recognition of a principle of good faith can be seen as a recognition of the parties' community norms, and not a violation of their consent. Consequently, it would 'merely mak[*e*] explicit the background assumptions of parties,' rather than being an undue burden on the parties' freedom.[261]

Brooks' conceptual argument contrasts the concepts of 'consensual rationality' and 'contractual morality' and shines further light onto the good faith debate.[262] In the former conception, good faith is understood as dependent on the 'intentions of the parties.' [263] It poses

[257] Collins, *Regulating Contracts* (1999) (n 111) 269.
[258] ibid, he refers in particular to the work of Stephen A Smith on substantive unfairness in S Smith, 'In Defence of Substantive Fairness' (1996) 112 LQR 138, 139-158.
[259] Styles (n 178) 162-163.
[260] Modern contracting is often argued as being characterised by inequality of bargaining power between parties, inherently undermining the presumption of equality that underlies freedom of contract in the first place, thereby justifying legal intervention into private contracting, see Daniel D Barnhizer, 'Bargaining Power in Contract Theory' in DiMatteo LA (ed), *Visions of Contract Theory: Rationality, Bargaining and Interpretation* (Carolina Academic Press 2007) 105.
[261] Styles (n 178) 164.
[262] Brooks (n 3) 503.
[263] ibid.

no threat to the freedom of contract as its limited purpose is to fulfil such intentions from a rational perspective. The parties are as unrestricted as they can be, can even agree to express good faith clauses, and the only limits are those imposed by reasons of public policy. It is the latter conception which is problematic in the context of the freedom of contract debate. Indeed, on this view, good faith allows the courts to impose external standards on the parties. These can go beyond the reasonable expectations of the parties as honest people, but have implications of a moral nature beyond the limits defined by the parties' agreement. It is precisely the moral basis of the conception which irritates the opponents. The belief is that rather than morality, the preference has to lie with logic in applying rules or principles, to keep consistency in judicial decisions. However, this is an illusion. Behind logical choices, there can always be found an explanation grounded in morality. It is simply that the explanation, emanating from the interests inherent to the particular business community in that particular time, will 'generally [be] concealed in claims of rational or logical necessity.'[264]

1.2.4. Unnecessary – Good Faith as a Gap Filler

The opponents of good faith consider it to be an unnecessary addition to the principles of contract law, arguing that other existing principles already cater to the unfairness in contracts.[265] Good faith would essentially act as a gap filler. Bingham LJ's statement in *Interfoto* is reflective of such an approach.[266] Indeed, he argued that 'English law has, characteristically, committed itself to no such overriding principle but has developed piecemeal solutions in response to demonstrated problems of unfairness.'[267] He notably gave examples to these piecemeal solutions from equity (unconscionable bargains), from statute (the regulation of the form of certain hire purchase agreements) and the common law (the prohibition of penalty clauses disguised as agreed estimates of damage).[268] This approach is viewed as the

[264] ibid 505.
[265] John Enman-Beech, 'The Good Faith Challenge' (2019) 1 Journal of Commonwealth Law 35 <https://www.journalofcommonwealthlaw.org/article/8812-the-good-faith-challenge> accessed 3 April 2025, classifies legal theories of good faith into three categories: either there is no principle of good faith ('avoidance'), or good faith operates as a tool to validate the parties' agreement and no more ('containment'), or good faith should operate as an overarching duty ('embrace'). The pragmatists are considered to be part of the 'containment theory' (48).
[266] *Interfoto* (n 100). This approach was later endorsed by the Supreme Court in *Pakistan International Airline Corp v Times Travel (UK) Ltd (Times Travel)* [2021] UKSC 40, [2021] 3 WLR 727 in the context of contract re-negotiation.
[267] ibid 439.
[268] ibid.

functional equivalence approach.[269] Essentially, adopting a principle of good faith is simply recognising what already exists in the common law. These 'piecemeal' solutions often operate as an interpretation tool of problematic contractual clauses, or for implying terms or in some cases, evaluating the performance of the contractual duties. Moreover, any recourse to equitable doctrines, such as promissory estoppel or undue influence, is limited by the pre-existing requirements set down for these doctrines. If the facts do not align with such requirements, the court will have no choice but to refuse the application. However, good faith as conceptualised herein, aims to protect the institution of contracting, 'rather than the contracting parties per se.'[270] Where such fragmented solution-seeking exists in contract law, it becomes all the more important to remedy it by having a uniform and universal approach to the adjudication of contract disputes.

For some authors, good faith is a tool to be used when and as needed to protect the reasonable expectations of the parties in individual contracts against the backdrop of the market in which they are operating.[271] Good faith is seen to be an unsatisfactory basis, yet it could be valid if it incorporates the reasonable expectations of the parties and considerations of fairness into cases on implied terms.[272] As such, good faith is not to be envisaged as an overriding duty but as an instrument in assessing the parties' reasonable expectations and the fairness of the agreement. The issue with this approach is that it does not admit the existence of good faith nor deny it. However, the concept either exists or it doesn't. Even though the supporters of the 'functional equivalence' approach do not want to endorse its applicability across the board, they are faced with the difficulty that admitting to its existence would need to be justified.[273] The justification inevitably dabbles into moral grounds, and this goes beyond their comfort zone.[274] As per Moore-Bick LJ's comment in overturning Leggatt J's decision, the main worry

[269] McMeel, 'Are There Any General Principles of Commercial Law?' (n 144) 194. Also see Andrews, *Contract Law* (n 207) 592-593 (enumerates the existing doctrines dealing with fairness as estoppel doctrines, unconscionability, vitiating factors, specific duties to disclose, fiduciary duties, implied terms, penalties, equitable relief against forfeiture of proprietary or possessory interests, disproportionate or over-severe termination of contracts following breach).
[270] Brooks (n 3) 505, adopting a 'contractual moralist' approach rather than a 'consensual rationalist' approach (see text to n 262 above).
[271] See Stephen M Waddams, 'Good Faith, Unconscionability and Reasonable Expectations' (1995) 9 Journal of Contract Law 55.
[272] ibid 62.
[273] McMeel, 'Are There Any General Principles of Commercial Law?' (n 144) 195, considers that "[p]romise-keeping is itself grounded in social morality, and its limits must have some connection with the same source."
[274] Brooks (n 3) 505.

is that there may be '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.'[275]

The opponents of good faith are quick to dismiss the introduction of an overarching principle of good faith in contracts because good faith does not have the clarity of other recognised principles, which exist as separately applicable doctrines.[276] The inability to demarcate the boundaries of the concept in the context of commercial relationships stagnates the development of the concept. The issue is, however, circular. If the concept is discarded as one lacking conceptual coherence, then it cannot be developed to the point where it will no longer require further clarification. Legal principles in English contract law can only gain conceptual coherence through gradual refinements over time.[277] If the courts fail to consider good faith as a separate doctrine capable of application on its own, then such a principle cannot find ways to develop in its own right. To develop the concept in any way, one must first recognise it in its own right. The recognition of an overriding principle of good faith is all the more important given that a 'functional equivalence' cannot provide a methodical cohesion for the existence of the already existing and recognised principles. They all regulate unfairness in the contractual context, but the legal basis upon which they have been developed is not clear. As recognised by Atiyah, 'the extreme reluctance of courts to acknowledge openly that they are trying to ensure that a contract operates as a fair exchange means that the conceptual apparatus of the law is highly complex and often obscures what is actually going on.'[278] The existing principles float in a vacuum and are called upon depending on the preference of the deciding court; their arsenal is no doubt extensive, but the individual principles are not contained and organised within a logical medium. A principle of good faith provides for a reasonable way forward to bring internal coherence to a very fragmented system of commercial contract law, and none of the main criticisms set out in this chapter fundamentally threaten the predictability and authority of commercial law.

1.3. The Role of Good Faith in the Performance of Contracts

Having looked at the main objections against a principle of good faith, an evaluation of its meaning and purpose is required. Getting a step closer to an overarching principle

[275] *MSC Mediterranean Shipping Company S.A.* (n 49) [45].
[276] Magda Raczynska, 'Good Faith and Contract Terms' in PS Davies, M Raczynska (eds), *Contents of Commercial Contracts – Terms Affecting Freedoms* (Hart Publishing 2020) 88.
[277] McKendrick, 'Doctrine and Discretion in the Law of Contract Revisited' (n 238) 5 citing Treitel (fn 14), such as the evolution of duress to the person into economic duress.
[278] Patrick S Atiyah, *Essays on Contract* (Oxford Clarendon Press 1986) 337.

necessitates that good faith is contoured with sufficient reliability in order for it to translate into concrete applications.[279] Chapter 1.3.1 investigates the purpose of good faith in contract law. Chapter 1.3.2 posits good faith as a norm. Chapter 1.3.3 questions whether a definition based on bad faith is desirable or should rather encapsulate honesty and cooperation. Chapter 1.4 considers the applicability of good faith by default. Finally, chapter 1.5 provides a conclusion to this part.

1.3.1. Investigating Good Faith's Purpose in Contract Law

All legal rules and standards need a purpose.[280] In contract law, as with any other legal field, the instrument and its purpose are intertwined. The investigative work into a general good faith principle inevitably requires an interrogation not only of the definition of the concept but also of its aim within the broader context of contract law. This is because good faith expresses a moralistic view of the law.[281] A formalistic view of the law rejects incorporations of morality and fidelity to commercial practice, whereas contextualism embraces it.[282] A principle that would be at odds with the overall purpose of contract law would be anomalous. Repetitive or potentially contradictory principles would create great uncertainty in the legal system. Therefore, the enquiry into the need for a good faith principle raises two queries that must be tackled. First, what is the aim that contract law seeks to achieve? Second, what is the aim that good faith seeks to achieve in that context?

1.3.1.1. Fairness

In attempting to answer the first question, Steyn proposes that legal rules must at their core use fairness as their guiding compass.[283] Indeed, 'a judge is entitled to take into account

[279] See text to n 250-251 above.
[280] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation? (n 7) 479, considers that contract law has a regulatory role beyond facilitation of commerce. Therefore 'contract law cannot be concerned solely with interpreting commercial contract behaviour, but directing and guiding it according to (...) [a] moral framework. The precise point of many, although not all, rules of law is to articulate this normativity in more concrete terms.'
[281] Jessica Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (2023) 74(3) Northern Ireland Legal Quarterly 528, 536, 540, considers that '[w]hile [law and morals] have different characteristics, laws should not go against morals and some laws find their source in morals,' the concept of good faith expressing a moral duty of fidelity to the bargain and also a prohibition of fraudulent behaviour.
[282] John Gava, 'What We Know About Contract Law and Contract Practice' (2014) 35(2) Adelaide Law Review 409, 426, a supporter of the formalistic view, argues that contract law is not a tool for the market, but a 'historically created and constitutionally validated means of settling disputes.'
[283] Steyn (n 4).

that simple fairness ought to be the basis of every legal rule.' This echoes Dworkin's principle of integrity in respect of statutory interpretation:

> [l]aw as integrity asks judges to assume, so far as this is possible, that the law is structured by a coherent set of principles about justice and fairness and procedural due process, and it asks them to enforce these in the fresh cases that come before them, so that each person's situation is fair and just according to the same standards. That style of adjudication respects the ambition integrity assumes, the ambition to be a community of principle.[284]

If this is true for statutory interpretation, then it should be true for contractual interpretation. Whether contract law is used by the courts in the context of dispute adjudication, or by the parties in ascertaining their rights and obligations in particular before a dispute arises, its integrity will be in direct correlation with its perceived strength by the community to which it applies. In democratic societies based on the rule of law, contract law's integrity is therefore directly linked to its fairness.[285]

Fairness is a complex word with philosophical underpinnings. Usually, it is understood to be synonymous with 'justice.'[286] Fairness can mean procedural fairness, restricted to an assessment of whether the parties have acted in accordance with established rules and principles when entering into the contract. Therefore, circumstances affecting consent will be dealt with under procedural fairness. Further, where the parties are performing or terminating the contract, a different kind of fairness can be envisaged. For instance, in his seminal work, Steyn proposes to recognise the purpose of contract law as giving effect to 'the reasonable expectations of honest men.'[287] This proposal sits nicely within a type of 'commutative' fairness.[288] This means that fairness seeks to hold the parties to their contract, and any deviation

[284] Ronald Dworkin, *Law's Empire* (Hart Publishing 1986) 243.
[285] For a definition of the rule of law, see Guillermo O'Donnell, 'Why the Rule of Law Matters' (2004) 15(4) Journal of Democracy 32, 33, who explains it as 'whatever law exists is written down and publicly promulgated by an appropriate authority before the events meant to be regulated by it, and is fairly applied by relevant state institutions including the judiciary.'
[286] Hans Schulte-Nölke, 'No Market For 'Lemons': On the Reasons for a Judicial Unfairness Test for B2B Contracts' (2015) 23(2) European Review of Private Law 195, 203. Also see Mireille Hildebrandt, Law, Democracy, and the Rule of Law in *Law for Computer Scientists and Other Folk* (Oxford University Press 2020)
[287] Steyn (n 4). Such view of contract law is echoed by many academics, see eg Jay M Feinman, Good Faith and Reasonable Expectations (2014) 67 Arkansas Law Review 525, 549. For a similar view of contract law, see Barnhizer, 'Bargaining Power in Contract Theory' (n 260) 125, where the author posits the purpose of contract law as to correct systemic inequalities of bargaining power in private orderings.
[288] Schulte-Nölke (n 286) 204.

from it would need to be justified to necessitate judicial intervention.[289] This is mainly due to an objective assessment of the contract, which does not involve the subjective intention of the parties.[290] Such assessment materialises through the concept of a reasonable person in contract law.[291] The reference to Steyn's 'honest men' adds little to the objective assessment of the reasonable person, as he rightly concedes.[292] Another type of fairness is 'distributive (or social)' fairness, as the justification for the court's intervention goes beyond the remit of the parties' contract. It seeks to protect the interests of the weaker members of the market.[293] Rather than selecting one type of fairness as an aim, contract law, and the legal system it belongs to, would aim to balance all of these different considerations.[294] As the distinction between different types of fairness can be blurred at times, strict compliance with procedural fairness might result in substantive unfairness, which might contravene the reasonable expectations of the parties.

Fairness can have various applications and can even strive to have a wider institutional impact on the market as a whole. Precisely, Brownsword argues that 'the role of contract law is not simply to track the contingent expectations of the community, but rather to shape the institution of contract in a way that enables it to make a distinctive contribution to the conditions under which cooperative dealing can flourish.'[295] He contends that 'the distinctive institutional mission of contract law must be to facilitate the making of cooperative arrangements as well as to protect contractors' expectations of mutually beneficial performance.'[296] As such, he posits good faith not as a control mechanism over contracts where the advancement of the self-interest of the parties is assured, but recognises a wider, an 'institutional' role for good faith where cooperative dealing becomes the trademark of contractual dealings.[297] Similarly, Dagan and Heller posit that 'contract law should respond

[289] ibid, the author gives the example of the court intervening to discard harsh exclusion clauses where a party seeks to exclude its liability for breach of contract.
[290] Ryan Catterwell, *A Unified Approach to Contract Interpretation* (Hart Publishing 2020) 28.
[291] The topic of reasonable expectations is further explored in chp 1.3.1.2 below.
[292] Steyn (n 4) 434.
[293] Schulte-Nölke (n 286) 204 gives the example of judicial intervention through fairness assessment of clauses providing for high bank charges for unauthorised overdrafts, where the economically weaker clients are seen to subsidise the bank charges of stronger clients who get free or cheaper charges for their accounts.
[294] Robert S Summers, 'General Duty of Good Faith - Its Recognition and Conceptualization' (1981-82) 67 Cornell Law Review 810, 826, had posited the rationale for good faith to be 'a justice and to justice according to the law' in the context of the US statutory duty of good faith. Moreover, he stated that it serves 'faithfulness to an agreed common purpose and consistency with the justified expectations of the other party,' and 'community standards of decency, fairness or reasonableness.'
[295] Roger Brownsword, 'Good Faith in Contracts' Revisited (1996) 49 CLP 111, 156.
[296] ibid 115.
[297] ibid. Brooks (n 3) 501 also echoes a similar sentiment when he contends that '[g]ood faith protects contracting parties, but its principal aim if protecting the practice of contracts.'

favourably to people's innovations even absent significant demand. (...) [A]n autonomy-enhancing contract law should prioritise settings where law's enabling role can best support autonomy through new contracting practices.'[298] Mitchell also posits that contract law's purpose goes beyond a facilitator of commercial transactions, but also has a regulatory role in commercial dealings 'that extends beyond merely curbing the very worst excesses of self-interested behaviour.'[299] McKendrick points out that there are various interests which contract law seeks to protect and these may at times be in conflict; however he recognises that 'underlying motif that marks out the legal treatment of commercial transactions is a recognition of the need to protect the free flow of trade and to avoid as far as possible the application of rules that will operate to the disadvantage of the bona fide purchaser in the ordinary course of business.'[300] This view necessarily rests on developing and enforcing rules in accordance with a given moral framework.[301]

In sum, contract law's aim goes beyond providing a framework for commercial exchanges, and seeks to curb opportunistic behaviour while simultaneously encouraging fair dealings where cooperative dealings can flourish. Although vulnerability is often referred to as a paradigm for addressing corporate responsibility, a similar argument could be made for corporate parties to a contractual deal.[302] The vulnerable party can be viewed as the one with 'weak bargaining power, limited access to justice [...], and information asymmetry.'[302] Protection of the vulnerable in the context of commercial contracts is limited to unfair or unreasonable contract terms in consumer or B2B contracts trading on standard terms in UCTA 1977.[303] However, such a view is based on a traditional view of contract law, where the norms promoted are those of 'self-interest, promoting free-markets, self-sufficiency, and profit maximization.'[304] Instead, vulnerability can be seen as inherent in contract law, because all contractual parties are innately vulnerable and therefore mutuality, interdependence and a desire for fair relationships better serve the law as underlying norms.[305]

[298] Hanoch Dagan and Michael Heller, 'Freedom of Contracts' (2013) Columbia Law and Economics Working Paper 458, <https://scholarship.law.columbia.edu/faculty_scholarship/1825> accessed 3 April 2025, 66.
[299] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 478.
[300] Roy Goode, Ewan McKendrick, *Goode and McKendrick on Commercial Law* (6th edn, LexisNexis Butterworths 2020) 29.
[301] ibid.
[302] Jingchen Zhao, 'Tackling Vulnerabilities Through Corporate Duties' (2024) 73(1) Catholic University Law Review 121, 124, 134-135.
[303] See Consumer Rights Act 2005, and UCTA 1977.
[304] Jonathan Herring, *Vulnerable Adults and the Law* (Oxford University Press 2016), 257.
[305] ibid 258.

1.3.1.2. The Limitations of the Concept of Reasonable Expectations

One of the ways contract law can be viewed is to accept that the law's purpose is not to accommodate the needs of all commercial actors.[306] Rather, it can provide a framework for trade which is optional and efficient.[307] This view rejects any role for morality or social norms and accords with the formalistic school of thought. The opposite view is a contextual one, which gives effect to the expectations of the parties as members of a business community.[308] In the commercial context, the concept of reasonable expectations merits attention as it is ubiquitous in court decisions. The term is used interchangeably with that of 'legitimate expectations.'[309] According to Steyn's view, seeking to uphold such expectations is fundamental to contract law.[310] This would ensure that the contract law is effectively doing what it is supposed to do, that is 'providing an effective and fair framework for contractual dealings.'[311] The concept of Steyn's 'honest men' is understood as requiring an inquiry into the mindset of the parties, which indicates a residual role for the subjective intent of the parties.[312] However, 'in many cases the subjective intentions of the parties will coincide with the interpretation put upon their intentions by the objective test, and to that extent their subjective intentions are protected.'[313] The hypothetical reasonable person is understood as also

[306] Gava, 'What We Know About Contract Law and Contract Practice' (n 282) 416.
[307] Morgan, C*ontract Law Minimalism: A Formalist Restatement of Commercial Contract Law* (n 194) xiii.
[308] Gava, 'What We Know About Contract Law and Contract Practice' (n 282) provides an overview of both approaches.
[309] See John N Adams, Roger Brownsword, *Key Issues in Contracts* (Butterworths 1995) 155-154, state '[l]egitimate expectation is the key to contractual obligation.' The concept of 'legitimate interest' is at times borrowed confusingly from administrative law where it is a well-developed concept, see for instance Chen-Wishart, 'Good Faith in English Contract Law – A Humble "3 by 4" Approach' (n 205) 205 posits 'respect for the legitimate interests of one's counterparty as an equal' as one of the components of good faith. In another publication, Mindy Chen-Wishart, 'Regulating Unfair Terms' in L Gullifer, S Vogenauer (eds), *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (Hart Publishing 2014) 129, states a party's legitimate interest in contract to be that of obtaining adequate redress, receiving the performance reasonably expected from the main subject matter term, avoiding an unreasonable inflation of one's own obligation, avoiding disproportionate liability for breach, and having a balanced power to determine the life of contract. Although the author's argument relates to standard form contracts, it can be extended to all types of business contracts in particular where the parties do not have equal bargaining power. Ryan Catterwell, 'The Limits on Intention in Contract' (2023) 139 LQR 571 further argues that the concept of 'legitimate interest' is a concept of law which operates as a limit on intention. It is a difficult concept to define and has applications in various instances (such as in the assessment of reasonableness of restraint of trade clauses, or in the assessment of penalty clauses, or in the assessment of validity of a purported affirmation).
[310] Steyn (n 4). This approach is also supported by other authors, see for instance Barry J Reiter, 'Good Faith in Contracts' (1983) 17 Valparaiso University Law Review 705, 714 who argues that contract law's purpose 'is to facilitate exchange by adding the law's authority and force as security for the due performance of what can reasonably be expected.'
[311] Steyn (n 4) 434.
[312] ibid.
[313] Ewan McKendrick, *Macmillan Law Masters, Contract Law* (Hart Bloomsbury Publishing Plc 2014) 19-21, he posits that there may be some residual role of the subjective approach in particular in the case of mistake in contract formation.

bound by the community norms which affect the parties. As such, reasonable expectations should be gauged against the backdrop of the parties' community norms.

The law prefers to adopt an objective viewpoint when assessing facts and the context in which they arise. Classic tests of officious bystander and business efficacy are examples of this in implying contractual terms.[314] Interpretation of contracts also requires an objective assessment of the reasonable expectations of the parties. Beyond the contract, the context in which the contract was concluded would also have to be taken into account.[315] Therefore, the parties' reasonable expectations will have to be gauged against the contract and the commercial landscape it inhabits. Thus, 'the judges must interpret a contract in the light of a wide general principle which embodies the values of society at large.'[316] What might be reasonable in a consumer transaction, might not be viewed as objectively reasonable in a deal with parties dealing at arms' length. Similarly, what was reasonable a decade ago in a consumer transaction, might not be viewed as being reasonable today in the same context.

Yet the concept of reasonable expectation itself is not one which is uniform in its application. While an 'expectation' is a subjective notion, 'reasonable' necessitates an objective assessment of the circumstances which itself will draw strength from community standards of appropriate behaviour. These are standards of conduct in contract relations which are widely shared and generally adhered to.[317] Determining the relevant community might not always be an easy task. While most times the members of a specific enterprise will be easily identifiably, there may be circumstances to justify the expansion of the relevant community where the parties' dealings have implications for a wider group.[318]

The main difficulty surrounding the discussion on reasonable expectations is its capacity to create legally enforceable 'entitlements'.[319] For this, a distinction is made between 'practice-based' entitlement and a normatively anchored entitlement.[320] In other words, an '[e]entitlement-based reasonableness', rather than a 'practice-based reasonableness', provides for an alternative framework for positing good faith independently from the contract as a

[314] These are discussed in chp 3.2.
[315] This is further discussed in chp 4.2.
[316] Styles (n 178) 168.
[317] Reiter (n 310) 706.
[318] ibid 707.
[319] Mitchell, 'Leading a Life of Its Own? The Roles of Reasonable Expectation in Contract Law' (2003) 23 OJLS 639, 654.
[320] ibid.

normative standard, rather than one which draws its authority from the contract.[321] The difference in legal entitlement in common law and equity is stark due to the lack of an overarching principle of good faith. For instance, in common law, the motive behind exercising a legal contractual right is not subject to any qualifying criteria, such as good faith, which allows for example a buyer to reject goods if they do not conform to the contract, even if the defect was minor and the real motive was to escape a bad bargain. In contrast, the party seeking an equitable remedy must come with clean hands, thereby allowing the court to take into account 'moral merits on both sides in reaching its decision.'[322]

Mitchell further argues that a reasonable expectation can be determined by reference to the institution of contracting itself.[323] Practice-based entitlement is referred to as an empirical view of reasonable expectations, drawing on the previous experience of the party or the law of probabilities, whereas the normative basis seeks alternatives to the limited solutions presented by contract law, and, for instance, may be general moral principles. Where empirical expectation is concerned, if the parties' expectations are shared and the contract is made in light of such expectations, then this presents no issue. However, where the parties' empirical expectations do not correspond, such as where there is an asymmetry in the bargaining positions of the parties, it would not be a strong basis upon which to rest legal liability.[324] A normative justification would be better suited than an empirical one to address unfairness where the unfairness arises out of the objectively reasonable expectations of each party. The normative basis may be in addition to or an alternative to the empirical explanation. The issue with the normative basis is that when the operative principle is identified, such as fairness, the recourse to the reasonable expectation becomes redundant.[325] Courts may prefer to refer to reasonable expectations of the parties as a concept rather than the underlying moral principle due to their aversion to general moral principles.[326] Consequently, recourse to the reasonable

[321] Roger Brownsword, 'After Investors, Interpretation, Expectation and the Implicit Dimension of the 'New Contextualism' in D Campbell, H Collins, J Wightman (eds), *Implicit Dimensions of Contract: Discrete, Relational, and Network Contracts* (Hart Publishing 2003) 105, 141.
[322] Goode and McKendrick, *Goode and McKendrick on Commercial Law* (n 300) 162.
[323] Mitchell, 'Leading a Life of Its Own? The Roles of Reasonable Expectation in Contract Law' (n 319) 645-646. She also posits an institutional basis rationale for reasonable expectations but accepts that this is adopts a restrictive view of contract law, one that is formalistic and does not take account of social and factual realities of contracting. In that sense, reference to reasonable expectations equates to a breach of contract in its most formalistic sense.
[324] ibid 656.
[325] ibid 657, 660.
[326] ibid.

expectations of the parties may be deemed problematic because it can produce symmetrically opposite outcomes depending on the justificatory basis adopted.[327]

The interesting point about these justificatory bases is not how they help the courts in the adjudication of the cases, but rather that reasonable expectation cannot constitute an all-encompassing principle which can justify the courts' decisions.[328] As such, where the courts favour the institutional basis of reasonable expectations, the adjudication would have favoured a strict application of the rules of contract law. If a more flexible approach is adopted where empirical evidence is relied upon to justify the understanding of the parties' contract in dispute based on their previous dealings, then an empirical approach would have favoured a more flexible approach to contract making. In particular, the concept of reasonable expectations does not assist in spelling out the substantive content of the standard against which the expectation is to be gauged, especially where the parties' actual expectations are lacking or divergent. Mitchell is correct in her argument that '[m]aintaining that fairness requires that reasonable expectations should be protected and that we have a reasonable expectation of fair treatment, simply traps us in a circle and again allows reasonable expectation to 'lead a life of its own.'[329]

In short, the use of the concept of reasonable expectations on its own does not help further define the purpose of contract law beyond what has been set out in chapter 1.3.1.1, since it is inconsistent in its application and does not yield much power in explaining how contractual disputes should be solved.[330] However, the courts are more at ease with referring to reasonable expectations of the parties than explicitly resorting to moral principles such as fairness, thereby softening the rigidity of the classical contract. In particular, reasonable expectations can play an important role in shaping a modern contract law that reflects a relational approach to

[327] Yong Q Han, *Policyholder's Reasonable Expectations* (Hart Publishing 2016) 61, 65, 83 argues that protection of the reasonable expectation is the purpose of contract law, whereas good faith is simply a means by which to achieve it. Therefore, he posits a principle of reasonable expectations as a better alternative to one of good faith, due to the concept of reasonable expectation being broader than that of good faith, 'undoubtedly, contracting parties reasonably assume or expect good faith or honesty, at least from each other.' However, such view is anchored in an empirical view of the contract, and adopts an empirical view of reasonable expectations. The general underlying and unifying philosophy is that of good faith, a component of which is the concept of reasonable expectation which is capable of being concretised by adopting a relational understanding of contract law.

[328] Mitchell, 'Leading a Life of Its Own? The Roles of Reasonable Expectation in Contract Law' (n 319) 664.

[329] ibid 660, Mitchell citing Patrick S Atiyah, *Promises, Morals and Law* (Oxford University Press 1981) 63.

[330] See for instance the examples provided by Mitchell, 'Leading a Life of Its Own? The Roles of Reasonable Expectation in Contract Law' (n 319) 650, 653 where the courts relied on an institutional view of reasonable expectations by grounding them into the contract, rather than the relationship, such as in *Baird Textile Holdings Ltd v Marks and Spencer* [2001] EWCA Civ 274 (where there was a lack of formal contract therefore the relationship could be terminated at will despite being a long-term one), or in *Total Gas Marketing Ltd v Arco British Ltd* [1998] CLC 1275 (HL) (where the court preferred the written terms of the contract over non-contractual understandings in the context of a long-term supply of gas contracts).

contractual obligations anchored in a contextual understanding of the parties' expectations. It can serve as a means for contract law to achieve its aim of providing a framework for contractual exchange, curbing opportunistic conduct and encouraging fair and cooperative dealings between commercial parties.

Moreover, the concept of reasonable expectations is not unique to contract law, but is also present in other areas such as public law and estoppel in equity.[331] The main difference in the application of the concept in these areas of law compared to that in contract law is that in the case of the former, 'protection of this form of expectation lies with the encouragement of the belief by the public authority coupled with a fairly robust general justification for enforcement.'[332] The upholding of underlying public policy justifications, such as that of 'consistency of treatment and equality' is particularly relevant in the use of the concept in public law.[333] However, in contract law, such policies will not be of much use; instead, a fairness-based entitlement would provide a better explanation, in particular in light of the arguments in support of a relational approach to contract law.[334] This is because the policy question underlying 'legal intervention in commercial transactions is […], one of the appropriateness of imposing […] a restriction upon commercial freedom […].'[335] The restriction prevents 'parties from exercising free choice in relation to the conduct of their affairs by imposing a duty upon them and creating a correlative claim upon their conduct.'[336] The tools that help to answer such a question are doctrines or rules of contract law, such as that of good faith.

1.3.1.3. Good Faith's Purpose in Contract Law

Having determined the purpose of the contract law to go beyond facilitation of commercial exchange by emphasising its institutional role as a guarantor of fair dealings, we now turn to the second question posed in the introduction to chapter 1.3.1. What role should good faith assume in contract law? Steyn argues that it is not necessary to have an overarching good faith principle, and that as long as reasonable expectations are used as a point of reference,

[331] Mitchell, 'Leading a Life of Its Own? The Roles of Reasonable Expectation in Contract Law' (n 319) 661.
[332] ibid.
[333] ibid 661.
[334] As discussed in chp 1.3.1.1.
[335] TT Arvind, 'Contract Transactions and Equity' in *Commercial Contract Law: Transatlantic Perspectives*, Larry A DiMatteo and others (eds) (Cambridge University Press 2013) 155-156. Although the author advocates for a better recognition of the role equity plays where classical contract law fails to deal with contractual gaps in particular in the context of complex transactions, he acknowledges that equity is on thin ground due to its 'absence of theorisation' and the 'reluctance with which [it] is invoked [..]' (177).
[336] ibid, 156.

good faith would be redundant.[337] He views good faith as having both a subjective and an objective component.[338] The first one refers to the honesty and constitutes the subjective element which contract law cannot assess except from the viewpoint of the reasonable person. The second component refers to an objective standard which involves community norms. He equates the protection of the reasonable expectations of the parties to the observance of the objective requirement of good faith. Rather than an overriding duty in contract law, he proposes a compartmentalised introduction of good faith duties in specific areas.[339] It is argued that Steyn has a restrictive view of the role of good faith. Arguably, the limitation in Steyn's view stems from viewing reasonable expectations as those that are only 'common to both parties.'[340] However, there is no common expectation that can reasonably be expected to be shared between the parties, given the presumed adversarial nature of contracts, regardless of the cooperative nature of the agreement, in particular where the parties are in dispute before a court.[341] The only commonality may be that they intend to contract with each other, but the basis upon which they decide to contract will always inevitably be in contradiction to each other's intention at the stage of dispute adjudication. Therefore, it is argued that to attempt and gauge the parties' common expectation is futile and the concept is not much help either because it does not have an established substantive justification for resolving any disputes as explained by Mitchell above.[342]

Where the concepts of reasonable expectations or good faith start to implicate moral norms, the discussion inevitably moves out of the confines of the legal discipline and into socio-legal or philosophical discourses. Precisely, Gava takes issue with Collins' labelling of law as discourse, arguing that academic discourses of socio-economic fields cannot be grafted onto an act of governance.[343] Collins advocates for a regulatory role for contract law and argues that this can be achieved by relaxing the procedural rules.[344] For instance, the parole evidence rule would have to be abandoned to take into account the context of the contract rather than the written contract itself. Collins' view of contract law as a tool to assist efficient exchanges

[337] Steyn (n 4) 439, he considers that 'contract law can satisfactorily be left to develop in accordance with its own pragmatic traditions' which echoes the 'functional equivalence' approach discussed above at text to n 278.
[338] ibid 438.
[339] Steyn (n 4) 439.
[340] ibid 434.
[341] The topic of the intention of the parties is discussed in detail in chp 4.2 below in the context of contract interpretation.
[342] See text to n 327.
[343] John Gava and Janey Greene, 'Do We Need a Hybrid Law of Contract? Why Hugh Collins Is Wrong and Why It Matters' (2004) 63(3) Cambridge Law Journal 605, 609-610.
[344] Collins, *Regulating Contracts* (Oxford University Press 2002) 358.

allows questioning the role of contract law in general and exploring whether it needs to be reconfigured into a hybrid law comprising socio-economic discourse. The disruptive effects of a rehaul of procedural rules aside, there would be a major legitimacy issue as the judges' lawmaking power would take precedence over that of the parliament. Regulating the market through contract law would mean that public lawmaking and enforcement would become irrelevant. Conversely, Gava argues that contract law should not be viewed from a regulatory lens.[345] For contract law to adopt a regulatory role would mean that the decisions emanating from the courts would have to reflect the market's needs. This is practically not possible, as most cases are litigated by those with the financial means and temperament.[346] As such, contract law is not suited for a regulatory role at large. Moreover, regulation would require that subjects of that regulation could access the content of it and act accordingly. The fact that dispute resolution results in decisions that are not widely publicised and understood by the market players is a hindrance in itself.[347] Contrary to other disciplines, legal analysis must maintain a coherent structure of its rules and principles so that its legitimacy is not put at risk. Consequently, in its endeavour to provide a just outcome, a court's decision cannot encompass all existing disciplines in the adjudication of legal disputes.

It is difficult to draw boundaries around an innately philosophical concept. Yet, the pragmatism of the legal field requires boundaries. A moral interpretation of good faith would suggest that the act of any party should be gauged based on the undeniable fact that each party's well-being (and in the commercial context, their commercial well-being) matters to them personally.[348] Bond proposes to anchor good faith beyond reason and logic, as these concepts themselves can vary in different cases, what may be reasonable or logical to one person might not be to another. He states that:

> '[j]ust as your well-being or ill-being (...) matters to you as a conscious, reflective, sentient, conative subject-agent, so each similar subject-agent's well-being or ill-being matters to himself or herself. Whatever reality and importance your well- the same kind of reality and importance.' And that is not a logical but a metaphysical truth.[349]

[345] Gava and Greene (n 343) 613.
[346] ibid 614.
[347] ibid 615.
[348] The parties must be understood as 'rational' beings, as posited by Leggatt and further discussed in chp 4.2 text to n 974 below.
[349] Edward J Bond, 'Gewirth on Reason and Morality' (1980) 11(1) Metaphilosophy 36, 53 (quotation marks in text).

In the context of commercial law, beyond the formalities of the conclusion and performance of a contract, the parties must first trust that the other side is capable, all circumstances taken into consideration, of performing the obligations expected for the contract in question. Trust is mainly defined as a 'firm belief in the reliability, truth, or ability of someone or something; confidence or faith in a person or thing, or in an attribute of a person or thing'.[350] It is therefore mutual trust that brings the parties together and keeps the contract in place for as long as necessary. At its core, then, a contract is an instrument of trust.[351] Trust is essential as 'a moral structure which makes self-interested economic action possible.'[352] Violation of such trust may be acceptable by the other party to a degree, or not at all. With such an understanding of the nature of contracts, it then becomes hard not to associate a notion of good faith with the freedom exercised by the parties entering into contracts. It can be argued that it is precisely that intrinsic driving force originating from the parties' free will that generates the trust necessary to bind the parties together with a contract.[353] It would not be unreasonable to suggest that all parties entering into a contract do so in good faith. Such good faith does not exclude calculating behaviour or prioritising one's own interests over those of the other party. It simply means that two parties have come together based on a mutual belief that the other can and will carry out the terms of the agreement as agreed. Indeed, '[t]he principle which allows parties to identify their own legitimate interest is not solipsistic self-interest but self-interest actualised in mutual recognition, and legally institutionalised in good faith as the basis of the agreement of simple contracts.'[354] Whether and how parties perform their obligations is another matter.

[350] Oxford English Dictionary Online, 'Trust' (*Oxford English Dictionary*, 2021) <www.oed.com/view/Entry/207004> accessed 3 April 2025.

[351] Brooks (n 3) 500, posits that '[t]rust in the institutions of contracts is promoted by the legal presumption, irrefutable in most cases, of a good faith reading of contractual agreements.' For different understandings of 'trust' in the contractual context, see Simon Deakin, Frank Wilkinson, 'Contract Law and the Economics of Interorganizational Trust' in C Lane and R Bachmann, *Trust Within and Between Organizations* (Oxford University Press, 1998) 146.

[352] David Campbell, *Contractual Relations: A Contribution to the Critique of the Classical Law of Contract* *Contractual Relations: A Contribution to the Critique of the Classical Law of Contract* (Oxford University Press 2022) 145. See also Oxera for LegalUK (n 12) para 2.3, the report provides that '[f]or transactions to take place, there must be a level of trust between the parties, and some degree of confidence about what will happen if something goes wrong.'

[353] Leggatt, 'What is the Point of Commercial Law?' (n 236) [29], commercial law, by enforcing contracts, overcomes 'the structural problem (...) in order for commerce to flourish' by addressing 'the risk that the other party will not carry out its side of a reciprocal transaction and, in particular, the risk posed by the temptation to cheat.'

[354] Campbell, *Contractual Relations: A Contribution to the Critique of the Classical Law of Contract* (n 352) 243.

This approach is a double edge sword and the issue is more visible in trying to adjudicate a case on the basis of a general principle.[355] Collins accepts that the use of 'open-textured standards' poses problems when used to adjudicate a case.[356] The issue faced by the court may be twofold. First, the court may be criticised for not going far enough in their analysis into the efficiency considerations that underlie the particular contract.[357] Second, the court may also be criticised for lack of sufficient attention paid to the market in which the parties operate.[358] The courts may end up deciding cases on an illusion of fairness, rather than actual fairness.[359] The main reason for underlying these criticisms is posited as being the lack of economic and sociological analysis of contractual behaviour not being allowed into the legal reasoning of the courts. Collins argues that such frameworks should ideally be incorporated into the reasoning of unfairness in legal analysis.[360] However it is suggested that it would be unreasonable to expect judges to know and assess in depth the issues raised by a socio-economical discourse.[361] Formation constraints aside, judges cannot allocate much time to investigate the business relationship of the parties outside of what has been presented to them as evidence, nor should they. Even the parties themselves may have, or opportunistically pretend to have in litigation, a different understanding of the business nature between themselves.

In sum, good faith is envisaged as a powerful concept which gives a justificatory basis to uphold the reasonable expectations of the parties in commercial contracts.[362] Indeed,

> if a basic purpose of contract law is to underpin the parties' expectations, and if a good faith requirement promotes this purpose, then (notwithstanding some

[355] The implications of positing good faith as a general principle are discussed in detail in chp 1.3.2 below.
[356] Collins, *Regulating Contracts* (1999) (n 111) 271.
[357] ibid 272, he gives the example of the examination of a penalty clause, where the court analyses it in isolation without asking whether or not the liability was matched with a proportional increase in price.
[358] ibid. Collins gives the example of the court decision in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803, [1983] 2 All ER 737 (HL), where the court interpreted a limitation of liability clause in a sale of seeds contract as unfair based on the fact that the defendants (seed merchants) often paid substantial damages to farmers, rather than another plausible motive which could have been that the defendants were trying to preserve their long-term business relationship and their business reputation.
[359] Atiyah, *Essays on Contract* (n 278) 352 argues striving for fairness in dispute adjudication does not prevent for such fairness to be used as the basis for understanding contracts, indeed, he posits that 'the search for fairness in exchange cannot (...) be condemned wholesale as violation of market principles.'
[360] Collins, *Regulating Contracts* (1999) (n 111) 274.
[361] Gava and Greene (n 343) 623.
[362] Good faith provides a 'normative' basis according to Mitchell's analysis above, see text to n 327.

> uncertainty) an honest attempt to keep faith with the parties' expectations must be more rational than a covert and inconsistent attempt to do so. [363]

Moreover, good faith promotes cooperation both within the contract but also within the market at large by curbing opportunistic behaviour and ensuring fairness in contract performance. Indeed, the 'more that contract doctrine provides a security against the risks of opportunism and exploitation to which co-operative dealing exposes a contractor, the more willing (other things being equal) contractors will be to deal in a way that optimises their interest (even though they are exposed to risk).'[364] It also serves to bring rational coherence to contract law by putting floating concepts of fairness under one roof and unifying existing legal and equitable principles into a cohesive unit.[365] Consequently, it has wider implications than just for the individual commercial actors, it has normative implications pushing the contract law debate forward in a new direction.

1.3.2 Good Faith as a Norm?

The courts construct new legal concepts by dissecting and adjusting existing ones. Adjusting existing concepts inherently means that what is available in the arsenal of the courts is not sufficient to remedy the legal failings of the case at hand. They investigate close alternatives, like scientists, induct or deduct from such alternatives and conclude on a new approach which attempts to fill the gaps not filled by existing legal categories. The courts have the power to establish a new rule in a single judgment, which becomes binding on subsequent cases.[366] The same cannot be said of establishing new principles. Principles require more than a single judgment. A good amount of support is needed to confirm the continued existence and application of a principle. If an attempt to create a new principle is not embraced with sufficient authority in later cases, it does not come into existence at all.[367] If adopted, the principle is then refined over time. English common law relies on inductive reasoning. The principle of precedent requires that comparable situations be decided coherently through consistent

[363] Brownsword, ''Good Faith in Contracts' Revisited' (n 295) 151. His analysis on rationality in contract law is inspired by Robert Nozick, *The Nature of Rationality* (Princeton University Press 1994).
[364] Roger Brownsword, 'Positive, Negative, Neutral: The Reception of Good Faith in English Contract Law' in R Brownsword, N Hird N and G Howells (eds), *Good Faith in Contract, Concept and Context* (Ashgate/Dartmouth 1999) 32.
[365] As discussed in chp 2 below. Chen-Wishart and Dixon, 'Good Faith in English Contract Law: A Humble '3 by 4' Approach' (n 205) 193, consider that an explicit recognition of good faith as underlying the 'piecemeal rules' in response to problems of unfairness 'can only enhance our understanding of these rules, assist in taxonomizing them (...), and facilitate their orderly development.'
[366] Atiyah, *Essays on Contract* (n 278) 96.
[367] See notably Lord Denning's attempt to introduce a principle of inequality of bargaining into contract law in *Lloyds Bank Ltd v Bundy* [1975] QB 326, (1974) 3 All ER 757.

application of previously applied rules. The courts are conscious of their lawmaking power and tread carefully not to step into a legislative void that might have been intentionally left by the Parliament. Such an inductive approach in deciding cases results in a reluctance to adopt general principles.[368]

Rather than a general approach to problems, English contract law prefers a fragmented and formal methodology to resolving disputes. Formalism in law is, of course, necessary and, as argued by Atiyah, cost and time-effective in resolving disputes.[369] He distinguishes between formal and substantive reasons in evaluating the rightness of the applicable rule.[370] A formal reason is only based on complying with the appropriate procedure, for instance accepting that signature makes the contract binding for the parties. A substantive reason is where an inquiry is made into the fairness resulting from the application of the rule, for instance where the signature is valid but the parties did not read and understand the agreement, to ask whether it would be fair to hold that they were bound by its terms.[371] By nature, only substantive reasoning is used in the application of principles because it requires an inquiry into the substance of the matter. Consequently, a formal approach to ensuring fairness in contracts is not possible without recourse to general principles of law.

Rule vs Principle

A norm is understood to be either a rule or a principle, and a distinction is drawn herein between (i) norms, as legally recognised reference points for evaluating conduct, (ii) principles, as normatively weighty legal reasons that guide and justify the development and application of rules, and (iii) rules, as determinate prescriptions applied through precedent. A principle can be seen as standing somewhere between what is definitively valid and non-obligatory.[372] Robert proposes to distinguish commands to optimise and commands to be optimised for best understanding the nature of principles.[373] As commands to be optimised, principles can also be

[368] Piers (n 58) 167.
[369] Atiyah, *Essays on Contract* (n 278) 93-120.
[370] ibid 93.
[371] John Gava, 'How Should Judges Decide Commercial Contract Cases?' (2013) 30 Journal of Contract Law 133, 146, argues that pure formalism is not possible in practice as it would fail to 'appreciate the nature of adjudication in common law.; Indeed, '[c]ommon law judges have often inserted common sense notions of justice even at the cost of doctrinal incoherence when the justice of a case demands a result that might not fit within the existing architecture of rules in an area of the law.'
[372] Alexy Robert, 'On the Structure of Legal Principles' (2000) 13 Ratio Juris 294, 303. Also see MacNeil, 'Uncertainty in Commercial Law' (n 184) 6, who argues that principles as 'broad statements that apply to a range of acts and, in the Common Law systems, tend to develop through a series of cases rather than being established in a single case.'
[373] Robert (n 372) 294.

referred to as 'ideals.' A principle in that sense is an ideal to be optimised and transformed into a real 'ought.'[374] Whereas rules are principles that have gone through the process of optimisation in a particular case, and they have been relativised to the actual and legal possibilities. This conceptual work relies on an understanding of principles as norms that command something to be realised to the highest degree actually and legally possible.[375] Therefore, the facts of each case and the legal possibilities will determine the point of trigger for the application of the principle for that particular case. Whereas rules are executory and 'can only be either complied with or not.'[376] They are, by nature, more specific and relate to specific scenarios.

Raz points out that rules and principles themselves have different types.[377] There are rules that are prohibiting, and others that confer powers on certain classes of persons, and those that do not fall within either of these two categories. Raz emphasises the importance of principles which are principles of obligation. He admits to the universality of some principles, and the applicability of others only in certain circumstances.[378] As such, 'all rules are subject to all principles and may be overridden by any of them in particular circumstances.'[379] The principles themselves compete with each other in the context of particular cases. Rules of obligation prescribe more specific actions than those prescribed by principles, which usually remain highly unspecific. Raz defines the specificity of an act as follows:

> [a]n act is highly unspecific if it can be performed on different occasions by the performance of a great many heterogeneous generic acts on each occasion. It is more specific to the extent to which there is only a small number of generic acts by the performance of which it is performed.[380]

Consequently, the distinction between rules and principles is argued to be one of degree, and not of type. In some instances, it may be difficult to decide whether the norm is a rule or a principle. Raz goes beyond a logical explanation of the distinction between rules and principles and approaches the matter from a legal policy standpoint. He does that by focusing on the various functions of principles in law, of which he identifies five. First, the principles can be

[374] ibid 300.
[375] ibid.
[376] ibid 295.
[377] Joseph Raz, 'Legal Principles and the Limits of Law' (1971) 81 Yale Law Journal 823.
[378] ibid 837.
[379] ibid.
[380] ibid 838, he gives the example of smoking as being a highly specific act, assault or murder as being a relatively specific act, and acting unjustly or unreasonably as being highly unspecific acts.

grounds for interpreting laws. This is arguably the most important function. Principles can even serve to interpret other principles of a narrower application. Where a decision conforms to the law, an interpretation of that law that conforms to a principle is presumably preferred to one which does not. As such, courts can make coherent decisions where various laws apply to the same matter.[381] Second, principles can act as grounds for changing and qualifying laws. The doctrine of precedent allows for laws to be changed through the use of principles, albeit conservatively. Third, principles can act as grounds for particular exceptions to laws. The law can remain the same while it is disapplied in a particular case because applying it would contravene important principles. Fourth, principles can serve to make new rules. Where the courts cannot apply any other laws but only principles, then they can regulate the area by making new rules based on established principles. Finally, principles can serve as the only ground of action in particular cases. This can happen where, for instance, the law has provided an individual a discretionary right, but has not delimited its scope of application.

Another way of distinguishing rules and principles is through the solutions they offer to specific legal decisions. If the application of one rule leads to a direct conflict with another rule, then either one can be declared to be the exception to the other, or one can be declared invalid in that particular context. Contracts regularly override general rules and provide for exceptions to their application in the context of that particular contract, such as force majeure clauses displacing the application of the doctrine of frustration. The lack of a general good faith principle does not mean a prohibition of good faith duties in contracts. Where the parties provide for a good faith duty in a contract, the court must consider and apply it as a contractual term as much as possible. Where an express good faith clause clashes with, for instance, requirements of certainty, then either an exception must be created or one of the applicable rules or approaches must be disapplied. To determine which approach is to be labelled as an exception or which method is to be disapplied necessarily implies that one must take priority over the other in that context.[382] Prioritising rules or norms in a hierarchy of importance is no easy task. Robert provides that 'collision law' allows for prioritising rules which are in

[381] ibid 840, he reinforces the strength of the interpretative function of the principles on the basis of comparative law where different legal systems reach different conclusions on similar rules because they apply different principles for their interpretation.

[382] An example of this is in *The Golden Victory* where the compensatory principle that the damages awarded should represent no more than the value of the contractual benefits of which the claimant had been deprived, was prioritised over the need for certainty in commercial law.

conflict.[383] The conditions where one rule will take precedence over another rule necessitate that the priority between principles is ever-changing depending on the conditions of the case.

An interesting parallel can be made with the investigation of good faith as a norm and business customs' incorporation into contracts. Customs are not clear-cut rules which the courts can draw from to adjudicate a case, nor can the parties expect that precise customs be automatically incorporated into the deal. Bernstein's research into certain large commodities industries' endeavour to codify their respective customs shows that they could not identify customs, let alone agree on the 'meaning of common terms of trade or discover the content of many basic commercial practices.'[384] She distinguishes weak-form customs as 'a set of vaguely defined yet workable relationship-creating norms that initially add tremendous value to contracting relationships but that gradually diminish in importance as contracting relationships mature.'[385] Therefore, any semblance of a custom which operated at the beginning of the business relationship is purported to be of little value where a dispute needs to be resolved later on. Any custom which becomes the subject of a dispute will have to be defined and explained within the context of that particular dispute. Such a task will undoubtedly be more suited for an industry expert rather than a judge. This is because judges can at best make an educated guess, as they do not have the resources to carry out an empirical study to determine the relevant custom.[386] Moreover, there can be doubts as to the fairness of such customs, and unfair customs may result in unfair decisions.[387]

An important point must be raised when distinguishing between principles and rules, and the preference of the law for one or the other. It is sometimes assumed that specific legal rules are more certain than general principles, and therefore, rules should be preferred for reasons of legal certainty.[388] The types of action involved in commercial law may range from small, simple or stable acts that are constant across time, to complex acts in fluctuating markets where economic interests involved are high. Where the latter is involved, insisting on rules rather than

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[383] Robert (n 372) 297.
[384] Lisa Bernstein, 'The Questionable Empirical Basis of Article 2's Incorporation Strategy: A Preliminary Study' (1999) 66 University of Chicago Law Review 710, 715.
[385] ibid 717.
[386] This argument is further supported by Robert E Scott, 'The Uniformity Norm in Commercial Law: A Comparative Analysis of Common Law and Code Methodologies' in JS Kraus and SD Walt (eds), *The Jurisprudential Foundations of Corporate and Commercial Law* (Cambridge University Press 2009) 166; and by Richard Danzig, 'A Comment on the Jurisprudence of the Uniform Commercial Code' (1974) 27 Stanford Law Review 621, 628-629.
[387] Eric A Posner, 'Law, Economics, and Inefficient Norms' (1996) 144 University of Pennsylvania Law Review 1697, suggests that customs in use are unlikely to be the most efficient or fair ones, rather they reflect the needs of the most powerful players in the market.
[388] See eg Raz (n 377) 841.

relying on principles may produce an environment where financially advantageous market players can pursue creative compliance strategies to seemingly comply with the letter of the law but not with its spirit.[389] Similar strategies can be used when parties are dealing with principles, where the parties look for loopholes to evade their application .[390] Responses to the uncertainties inherent in the law level the playing field for arguments in regards to the prevalence of rules over principles or vice versa. Regarding good faith, the lack of a rule of good faith in commercial law should not discourage the development of good faith as a principle.[391] Conversely, the lack of a principle of good faith in commercial law does not hamper the introduction of a rule over time, whether through concretising a principle into a rule, or through enacting it into a legislative instrument as suggested herein.[392]

Good Faith as An Open Norm

If the content of a norm cannot be determined, it may be argued that it is no norm at all. Hesselink considers good faith to be an open norm.[393] Whether the norm is open or closed depends on whether it applies to a wide or a restricted number of situations. Where such a number is restricted, so that all situations are excluded but one, or where such a number is open-ended, so that no situations are excluded from its scope, then a norm is less likely to be characterised as a rule.[394] The only way to determine the extent of a norm is by its concretisation through the facts of a case to which it purports to apply.[395] He conceives rules as 'an abstract formula that links certain legal consequences to certain facts: if facts *a*, *b* and *c* occur the legal effect will be *x* (...)'.[396] Gradually, this allows for sub-rules to be developed that constitute the content of the main norm.

[389] MacNeil, 'Uncertainty in Commercial Law' (n 175**)** 73.
[390] ibid.
[391] See chp 1.2.
[392] See chp 6.4. Also see, Waddams, *Principle and Policy in Contract Law* (n 33) 216, who states that the 'adoption of good faith as a general principle could not eliminate the need for particular rules in the various contexts in which it has been invoked, (...).'
[393] Hesselink (n 250) 640.
[394] Julia Black, *Rules and Regulators* (Oxford University Press 1997) 25, the author refuses a classification based on rules vs standards as she contends that such dichotomy tends to focus only on the linguistic dimension of the rule or standard involved, where the rule is always considered as precise and certain, and a standard is always viewed as vague and unclear. Instead, she posits that it is the inclusiveness of the rule/standard which determines its purpose, not its linguistic precision nor its certainty. Therefore, the interpretative strategy adopted in relation to it also affects its inclusiveness (27), for instance the provision itself may allow for rule making powers including how to interpret the legislative rule or standard (26).
[395] Hesselink (n 250) 622.
[396] ibid 636.

Where good faith is not a norm, but 'a mouthpiece (a *porte parole*) for new rules', a decision cannot be based on it:[397]

> [g]ood faith is not the highest norm of contract law or even of private law, but no norm at all, and is merely the mouthpiece through which new rules speak, or the cradle where new rules are born.[398]

This argument stems from the observation that the variety of norms and legal effects that have been based on good faith by the courts are in fact devoid of any meaning insofar as good faith stands no more than what justice stands for.[399] Hesselink justifies his position on the basis that good faith's functions have been assimilated by the three main tasks of the judge as generally understood in European civil legal systems. Teubner also refers to the functions of good faith as being threefold.[400] These three functions are interpretation, supplementation of duties and correction or limitation of rights.[401] As such, good faith helps courts to interpret agreements where the terms of the contract are vague, incomplete or non-existent.[402] Moreover, it implies duties of loyalty, care, cooperation or information to protect the parties' expectation interest.[403] Finally, it prohibits abusive use of rights. Instead of concretising an open norm, Hesselink argues that each task should be further developed and concretised individually and separately from good faith.[404] Furthermore, an argument is made that the three functions of the court spill into all areas of law and therefore create a difficulty in determining the scope of a concept with an unlimited field of application. As such, good faith's application goes beyond contact law and is weaved into the whole fabric of the legal system. The lack of coherence between the sub-rules developed on the basis of good faith is also seen as an argument against conceptualising good faith as a rule in its own right.[405] Viewing the three functions of the courts as the content of good faith would be impractical and unjustified, and would lead to such distinction being abolished.[406]

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[397] ibid 641.
[398] ibid 645.
[399] ibid 628-634; these categories relate to the formation, validity, interpretation of the contract, determining the content of the contract, issues relating to privity of contract, performance of contract, the legal basis of the doctrine of hardship, and remedies for non-performance.
[400] Teubner (n 51) 20, the author particularly refers to the German *Treu und Glauben*, where he states the three functions as being (1) expansion and establishment of contractual duties, (2) limitation of contractual rights, (3) transformation of contract.
[401] Hesselink (n 250) 627, 640.
[402] ibid 629.
[403] ibid 631.
[404] ibid 636.
[405] ibid 642, 644.
[406] ibid 664.

Consequently, good faith is seen as no more than a mysterious cloak behind which the judges hide in order to create law, more so in civil law countries than the common law. The civil law judges worry about legitimising their decision, and rightly so, if they do not provide a legal basis for it in a legislative instrument. The common law judges are of course used to being lawmakers but Hesselink argues that equity fulfils practically the same role for common law judges in that it corrects the rigidity of the common law rules where abstract rules lead to unjust results in specific cases and correction is required to provide an exception based on those facts or to create a new rule to disapply the old one.[407]

Piers attributes the aversion to a principle of good faith in English law to the distinct reasoning approach used in civil and common law countries.[408] Indeed, common law uses an inductive methodology, where rules are adopted by resolving disputes based on analogous cases. As such, overarching principles are avoided and incremental development of the rules is favoured, by analogy with existing authorities. McKendrick echoes this sentiment when he states that it is not good faith as a concept that is the issue, but '[i]t is the elevation of good faith and fair dealing to the status of a general principle which is the real stumbling block.'[409] And once the courts have decided that there is no general principle of good faith, it will be very hard to change course and reverse on that position because the court 'will not throw out years of learning and embrace a new general principle which is of uncertain ambit and distinctly dubious pedigree.'[410] On the contrary, the civil law tradition embraces abstract principles and resolves disputes within the framework of established rules.

Alternative Doctrinal Conceptions of Good Faith

Teubner's projection on the potential direction of good faith in English law, despite having been published over 20 years ago, remains insightful. He had predicted that good faith would be developed (...) in forms of judicial activism similar to those in other common law countries, combining close fact-oriented case analysis with loosely arranged arguments from broad principles and policies:[411]

> [t]he predictable result will be a judicial doctrine of good faith that is much more 'situational' in character. (…) As opposed to abstract and general 'conditional

[407] ibid 621.
[408] Piers (n 58) 167.
[409] McKendrick, 'Good Faith: A Matter of Principle?' (n 206) 46.
[410] ibid 48.
[411] Teubner (n 51) 21.

> programmes' and to a series of finely circumscribed doctrinal figures based upon good faith, they will distinguish and elaborate different factual situations of contracting. They will not rely primarily on abstract distinctions developed by legal and economic theory (complete/incomplete, discrete/relational, consumer/commercial), but rather begin to typify different 'relationships which are of common occurrence' (landlord and tenant, doctor and patient, carrier and shipper etc) and will see the pressures of the factual situations (...).'[412]

He concluded that English law would develop new rules which would apply by analogy derived from other similar factual situations, where the application of a new rule would be justified as a result of frequent occurrence. As such, it would not translate into a 'strictly conceptualised and systematised doctrine,'[413] but will be a loosely organised principle upon which ad hoc arguments could be built. Teubner's observation of English legal reasoning is correct in that it is 'rule-oriented, technical, concrete but loosely systematised.'[414]

Despite warning against dabbling in abstract moral theory when dealing with law and good faith, Powell has continued to advocate for a requirement of good faith.[415] Brownsword goes one step further than Powell and advocates for a good faith 'regime', although he admits that we are not there yet. He states that:

> [t]o the extent, however, that Powell advocated eschewal of abstract moral theory, he was, I believe, mistaken; for, failure to engage with moral theory will inhibit the development of what I have called a good faith regime, which may well prove to be the most rational doctrinal option.[416]

He contrasts a good faith requirement with a good faith regime. The former refers to an understanding of good faith as a norm where the parties respect the terms of their contracts 'in line with the spirit of the agreement and, more generally, [*where*] they should pursue their individual self-interest in a way that is consistent with the community's sense of fair dealing.'[417] The latter refers to a reframing of the underlying adversarial ethic of traditional theory of

[412] ibid.
[413] ibid.
[414] ibid 11.
[415] Powell (n 163).
[416] Brownsword ''Good Faith in Contracts' Revisited' (n 295) 157.
[417] ibid 113.

contract law, where this is replaced by a systematic application of an ethic of cooperation.[418] Brownsword's view of good faith requirement disassociates the evaluation of disputes from the classical theory of contract law, where utility maximisation is prevalent, and situates it in the actual setting in which the parties dealt.[419] The courts can better give effect to the expectations of the parties, and this does not permit them to replace their own version of fairness with that agreed upon by the parties.[420] The good faith regime goes one step further and supposes the setting to be a cooperative one rather than one of short-term gain maximisation. Parties are still held to be pursuing self-interest, but this is held to be in a context of a community of interest between the contracting parties in which autonomy is valued. It also presupposes that the contracts are exchanges of promises that are mutually beneficial, and not simply an exchange of promises. Where both parties act with an understanding that the institution of the contract allows each to be in a better position than the one before entering into the contract, they need not be concerned with each other's position.[421] The trust is more so in the contract as an institution, rather than the contract itself. However, this results in a dilemma which Brownsword also recognises. The institutional theory of contract law cannot provide an answer as to what is fair and what is not. The best it can do is present an option between recognised community standards or standards prescribed by a moral theory, which can prove difficult to translate into legal rules.[422]

More recently, there is a move towards distinguishing good faith as a distinct operative principle as an actor taking main stage, or a principle directing the show from the sidelines. McMeel focuses on two alternatives, first being the functionally equivalent doctrines approach, and second being a general principle.[423] The first alternative would frame good faith as grouping discrete rules and doctrines based on comparative law, and potentially providing a grounding for future development or as a cross-check for difficult cases. The second alternative would conceptualise good faith as a general principle but would raise the question as to whether it would intervene to regulate the various stages of contract of formation and performance.

[418] ibid 114. For a similar approach, also see Davies, *JC Smith's the Law of Contract* (n 56) 298, 'Commercial parties are characteristically viewed as adversaries, each seeking to conclude the best bargain possible for themselves, without any need to worry about the position of the other party.'
[419] Brownsword ''Good Faith in Contracts' Revisited' (n 295) 127.
[420] ibid 131.
[421] This is in line with Leggatt's rational choice theory, see George Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (2015) 131 LQR 454, discussed further in chp 4.2 below.
[422] Brownsword, ''Good Faith in Contracts' Revisited' (n 295) 143, 151.
[423] McMeel, 'Are there Any General Principles of Commercial Law?' (n 144) 194-196.

Similarly, Chen-Wishart labels the less radical option as good faith being a 'relentless woodpecker' aggressively pecking away 'to make non-conforming parts of contract law align with good faith.'[424] This would presumably allow for uniformity in the application of the law across the board and discard incompatible rules, supporting the inefficient rules argument explored above.[425] It would be able to create new doctrines and expand existing ones.[426] She argues, however, that English law is not ready for good faith being in the spotlight, as this would require good faith to be implied in law, and would shut out other principles such as contractual freedom, certainty and avoidance of waste.[427] Her other alternative is labelled as the 'measured tortoise,' where good faith provides a framework for understanding the existing law, by explaining its content through a restatement rather than necessitating an active change.[428] As such, it does not clash with other principles and fits perfectly into the incremental approach acceptable to the judiciary. It operates as an explanatory, organisational and legitimising principle underlying existing law. Nothing revolutionary is afoot; instead, the law is simply evolving. She views Leggatt J's judgment in *Yam Seng* as evidence to support her argument. Indeed, Leggatt J 'draws together several different threads running through the case law and derives a principle, cautiously expressed, but capable in time of broader application, via the familiar common law incrementalism.'[429] Consequently, such various normative conceptions of good faith are possible because it can operate both as a guiding principle of law and also as a precise duty where it has been devised for concrete application either through case law or legislation. This is a strength of good faith, not a weakness.

1.3.3. An All-Encompassing Taxonomy

Vagueness

Good faith is a vague term. Halpin offers a threefold categorisation of linguistic vagueness that arises in legal language.[430] First, the vagueness can arise from linguistic

[424] Chen-Wishart, *Contract Law* (n 244) 627. Also see Chen-Wishart and Dixon, 'Good Faith in English Contract Law: A Humble '3 by 4' Approach' (n 205) 199 where the authors refuse the most radical form of good faith, as an independent cause of action, or as 'the charging bull' alluding to the proverb of the 'bull in the China shop.' Such a version of good faith would pose a significant threat to freedom of contract and English's law preference for incrementalism.
[425] See text to n 321.
[426] For example, see Andrew Dahdal, 'Good Faith and Post-Repudiation Conduct' (2015) 40(1) University of Western Australia Law Review 72, the author demonstrates that good faith can provide a legal basis and further illuminate the criteria of application for the legitimate expectation test laid out in *White and Carter (Councils) Ltd v McGregor* [1962] AC 413 in a post-repudiation pre-termination context.
[427] Chen-Wishart, *Contract Law* (n 244) 628.
[428] ibid.
[429] ibid.
[430] Andrew Halpin, *Reasoning with Law* (Hart Publishing 2001) 97-99.

infelicity. As such, 'good faith' and 'not bad faith' would not mean the same thing. Rather than focusing on the meaning of each, the best course of action is to choose between the two variants to decide a case. Second, the vagueness may be attributed to conflicting usage within the community as to what constitutes good faith. A party may be unsure as to whether the other party would use the term good faith in the same sense as imagined by that party. The parties can, of course, define good faith in their contract and decide on the agreed-upon meaning. As such, their chosen meaning may be different than how the rest of the community uses the term. Third, the vagueness may also be due to the absence of an agreement on the recognised usage of the terms 'good faith' and 'not bad faith' in the relevant community. A term can remain vague 'for as long as there may arise novel situations for which the application of the term can be considered, or situations over which conflicting usage has not conformed to an accepted usage.'[431] The courts are therefore always confronted with vagueness in words, nonetheless they must resolve disputes and settle usage over any vagueness over time. MacNeil recognises that even though this poses risks for existing contracts, it carries benefits in terms of legal certainty for the future.[432]

Burton does not shy away from the vagueness in legal terms.[433] To the contrary, he embraces it as being an inherent part of the judicial process: 'legal rules and doctrines are cast in language. All language, except some proper names, is abstract (...). Indeed, laws are just abstractions.'[434] Eventually, as laws go through the process of interpretation and application to particular cases, they become less intimidating. As such, there is no reason to distinguish between the abstraction of other concepts of law, which have had many examples of application over the years and good faith. If 'laws are just abstractions,' they all must go through a process of concretisation, so that English law can get comfortable with the concept of good faith too.

The various concepts which have been attributed to good faith are numerous. Such diversity can boil down to a range of standards which are triggered in specific scenarios. Stapleton proposes the common conceptual denominator as one which fuses concepts of advertent pursuit of self-interest and unconscionability.[435] One is free to pursue its own interest as long as this is not done in an unconscionable manner. She provides several examples; a

[431] ibid 99.
[432] MacNeil, 'Uncertainty in Commercial Law' (n 175**)** 77.
[433] Steven J Burton, 'Reply to Ewan McKendrick, 'Good Faith in the Performance of a Contract in English Law', in L DiMatteo, and MA Hogg (eds), *Comparative Contract Law: British and American* Perspectives (Oxford 2015; online edn, Oxford Academic 2016) accessed 3 April 2025, 220-222.
[434] ibid, Burton finds English law's discomfort with abstractions 'curious' and considers that English law has no trouble with 'familiar abstractions, just with new ones.'
[435] Stapleton (n 47) 7.

person being dishonest, a person conducting himself contrary to his word or a person exploiting a position of dominance or power over a person who is vulnerable relative to him.[436] Essentially, she posits good faith as the exact opposite of opportunism. An economic view of bad faith as opportunism was presented by Muris, who described opportunism as being one party's 'behaviour contrary to the other party's understanding of the contract, but not necessarily contrary to the agreement's explicit terms, leading to a transfer of wealth from the other party to the performer.'[437] As such, opportunism is seen as an unagreed wealth transfer, and good faith is posited as a concept which can deter such transfer. Cohen's view was also in line with Muris'. He defined opportunism as 'any contractual conduct by one party contrary to the other party's reasonable expectations based on the parties' agreement, contractual norms, or conventional morality.'[438] Such an economic view of contracts highlights the purpose of contract law as having to combat opportunism wherever it arises.[439] Consequently, while the concept of good faith is inherently vague, this vagueness is neither unusual not insurmountable within legal reasoning. The notion of good faith ultimately functions as a safeguard against opportunistic behaviour and provides contract law a basis from which to justify the resolution of contractual disputes in line with reasonable expectations, and an ethic of cooperation as discussed above.

Excluder Theory

Despite the large number of academic debates on good faith, there has been no consensus on the exact meaning of good faith. In the performance and enforcement of the contract, it primarily refers to considerations of fairness balanced against the parties' self-interest. Conversely, Summers' excluder theory presents good faith as the absence of bad faith.[440] In simple terms, good faith is defined in opposition to bad faith. This approach relies on the premise that bad faith conduct is easily identifiable and, therefore, separating good faith and bad faith conduct is not difficult. Accordingly, the task of the courts would be simply to

[436] ibid 7-8.
[437] Muris (n 109) 521.
[438] George M Cohen, 'The Negligence-Opportunism Tradeoff in Contract Law' (1992) 20 Hofstra Law Review 941, 957.
[439] See Richard A Posner, *Economic Analysis of Law* (Aspen Publishing 2014) 125, who also supports the idea that the basic aim of contract law is to deter opportunistic behavior between contracting parties in order to obviate costly self-protective measures.
[440] Robert S Summers, 'Good faith in General Contract Law and the Sales Provisions of the Uniform Commercial Code' (1968) 54 Virginia Law Review 195.

meticulously identify types of bad faith in previous decisions and create new categories either directly or by way of analogy.[441]

The main issue with the excluder approach is that it prevents the development of a principle based on good faith. Summers explicitly advocated against the courts adopting 'reductionist definitions' of good faith.[442] The case-by-case determination of bad faith, and by default of good faith, would mean that there is no unifying guideline which could direct future decisions. This inevitably puts in jeopardy the certainty in decision-making. Moreover, the restriction of good behaviour into bad faith categories does not take into account the purpose of a good faith principle set out herein. Bad faith conduct is already effectively dealt with in English contract law under the existing doctrines.[443] At best, an excluder approach would see good faith confined to a functional equivalence role.[444] It would not serve to take into account the reasonable expectations of the parties or to promote cooperation within contracts, and potentially even within contract law as an institution. This is because the excluder approach does not take into account the fact that there may be positive obligations which can be imposed upon the parties for a fair outcome. The case of a party withholding from a negative action, such as expressly stating a lie, is not the same as the case of a party who withholds information which does not equate to a lie but would cause their contracting party to arrive at a different contracting decision if they were made aware of that information. In the latter scenario, a principle of good faith can potentially impose such a duty requiring an action on behalf of the party with the relevant information. Conversely, a bad faith approach is by design restricted to condemning active behaviour which blatantly creates an unfair outcome between the parties.

Further, the excluder approach is also tainted with similar definitional difficulties advanced by the opponents of good faith. Bad faith is at least as vague as good faith. A lack of proper definition means that it is not clear when the existing principles can be used to adjudicate cases or whether a new category needs to be created under the excluder approach. As such, bad faith does not offer a better definition than good faith. Without a positive definition of good faith, there is no yardstick for defining bad faith. The courts' case-by-case determination of bad faith instances leaves much to be desired in terms of legal certainty, where there is no litmus test for bad faith. The alternative proposed by Burton is not much help either. He posits bad faith as an attempt to recapture opportunities forgone as a result of the making of the

[441] ibid 207.
[442] ibid.
[443] See chp 2 below.
[444] See text to n 269 above.

contract.[445] The limitation of this approach stems from a definition of opportunities forgone as expectations of reasonable persons, which only include economic elements of the contract. Any other dimensions of good faith, which focus on normative considerations, such as loyalty or honesty, are ignored. As such, the role of good faith is reduced to 'enhanc[*ing*] economic efficiency by reducing the costs of contracting.'[446]

Honesty

In attempts to define good faith, frequent references are made to honesty, reasonableness, loyalty, cooperation and fairness.[447] While each of these concepts is vague in itself, they do help to elucidate the conception of good faith as a principle. Where honesty is in question, the obvious dilemma is whether to favour the subjective intention of the parties or the objectively determinable conduct.[448] An objective assessment of honesty inevitably entails a moral dimension. What is honest may differ from one person to another, and there may be differences in opinion as to dishonest conduct from one market to another. Some conduct will be dishonest, for instance, encouraging others to lie or deliberately acting to cause another to suffer an avoidable loss. Other conduct might not be as clear-cut. For instance, whether silence can amount to dishonesty where a party does not rectify the other's mistake, which causes it to suffer a loss, can be debated.

A parallel can be drawn from the approach adopted in criminal law; the two-stage test laid out in *R v Ghosh (Deb Baran)* was overruled in *Ivey v Genting Casinos UK Ltd (t/a Crockfords Club).*[449] The Supreme Court insisted on an objective assessment of honesty. Similarly, in trust law, the majority of the judges in the House of Lords in *Twinsectra Ltd v Yardley*, arrived at a mixed test of subjective and objective test in the context of dishonest assistance.[450] However, Lord Millett dissented and insisted on a sole objective requirement, discarding the subjective one. As such, the objective assessment of a party's conduct overrides the state of mind, whether it was an honest one or not. Upholding the reasonable expectations of the parties can only be possible if the subjective viewpoints of the parties can be set aside, in particular, where most parties in commercial law will be corporate entities, the conduct of

[445] Burton, 'Breach of Contract and the Common Law Duty to Perform in Good Faith' (n 108) 369, 373.
[446] ibid 393.
[447] See eg Chen-Wishart, *Contract Law* (n 244) 632, she refers to honesty, fair dealing and fidelity to the contractual purpose as the main components of good faith.
[448] See text to n 152, 312 above.
[449] *R v Ghosh (Deb Baran)* [1982] QB 1053, [1982] 4 WLUK 44; *Ivey v Genting Casinos UK Ltd (t/a Crockfords Club)* [2017] UKSC 67, [2018] AC 391.
[450] [2002] UKHL 12, [2002] 2 All ER 377.

which will be easier to assess than the mindset. Overall, it is difficult to argue that honesty, even where it is to be assessed objectively, adds anything to the assessment of whether a conduct goes against the reasonable expectations of the parties. This is because if we are upholding the reasonable expectations of the parties assessed against objective criteria, then honest conduct can also only be assessed against an objective criterion, which necessarily corresponds to an evaluation of whether such expectations were met. Therefore, it is hereby argued that subjective honesty can only be used in the determination of other doctrines, such as fraud, mistake as to terms or rectification, not in the determination of whether good faith was breached.[451] Further support for this argument lies in the recognition that public policy concerns make it hard to justify the enforcement of an agreement in which both parties can deliberately lie to the other.[452] However, this view relies on a subjective view of honesty. Where the parties agree that they can contravene the reasonable expectations arising out of the contract, this view relies on an objective assessment which cannot be distinguished from that of the reasonable expectations themselves. In simpler terms, this would mean that the parties would be agreeing to being able to breach the contract without any consequences, which defeats the purpose of contracting itself. Even though the parties provide for any consequences for such a breach, this would equate to agreed contractual terms which the parties would be free to agree to, subject to the restrictions on penalty clauses.

Consequently, honesty is not a separate test or component in the assessment of good faith. In the context of commercial contracts, a party acting honestly means a party acting in line with the reasonable expectations of the parties. If they have acted dishonestly, they may be contravening to traditional doctrines, such as fraud, and also good faith as they would have breached fair conduct as reasonably expected under the contract.

Reasonableness

Like honesty, reasonableness includes elements of societal norms. Acting in good faith and acting reasonably are not synonymous.[453] A person may act in good faith, but the conduct may not be reasonable, gauged against objective standards of reasonable behaviour independently from outside the contract. The distinction is further supported by the wording of

[451] Chen-Wishart, *Contract Law* (n 244) 634, other doctrines where honesty is part of the assessment criteria is well-established however whether honesty adds anything to the assessment of good faith and should therefore be an integral part of the test is not justified by the author.
[452] On the topic of contracting out of good faith, see chp 4.5 below.
[453] Stapleton (n 47) 8 acknowledges that acting reasonably implies good faith in any event, dishonest, deliberate contradictory or exploitative behavior is always unreasonable.

some legislation defining good faith. For instance, the Sale of Goods Act 1979 s 61(3) and the Bills of Exchange Act 1882 s 90 provide that acting in good faith means acting honestly, whether it is done negligently or not. The good faith principle as envisaged herein is understood to encapsulate the reasonable expectations of the parties as discussed above.[454] It does not mean that the parties are under an obligation to act reasonably.[455] Consequently, good faith does not equate to a subjective state of mind characterised by honesty as argued by some authors.[456] The reference to reasonableness of conduct is usually posited as entailing an objective assessment against which the party's honesty is measured, for instance, in exercising a discretion; but good faith is separate from such reasonableness in that the reasonable expectations it encompasses reflect the parties' objectively assessed intentions, which may or may not overlap with assessments of reasonableness of conduct.[457]

Reasonableness of conduct and reasonable expectations are confusingly similar but should be distinguished. The expectations of the parties, whether reasonable or not, are separately assessed from those that are imposed by objectively reasonable standards of conduct. An unreasonable expectation is not protected, however much the parties' subjective and honest belief in their entitlement. In that sense, subjective reasonableness is no different from a requirement of honesty.[458] This tension between objective norms and subjective beliefs is further explored by Waddams, who critiques good faith as a vehicle for fairness. He argues that beyond good faith, there is a wider and more predictable principle, that of protecting reasonable expectations, which operates.[459] He posits good faith as a tool for determining the reasonable expectations of the parties and the fairness of their agreements. In this line of argument, unconscionability is then seen as the only way in which fairness can be administered outside of the usual doctrines. Where a party derives an immoderate gain from an inequality of bargaining power, unconscionability requires that the contract be set aside, regardless of the parties' good faith. He argues that a criterion of good faith would weaken the position of the weaker party.[460] However, this view is based on a classical understanding of the theory of

[454] See chp 1.3.1.2.
[455] Elisabeth Peden, 'When Common Law Trumps Equity: The Rise of Good Faith and Reasonableness and the Demise of Unconscionability' (2006) Sydney Law School Legal Studies Research Paper No. 06/57 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=947361> accessed 3 April 2025, 12.
[456] Richard Hooley, 'Controlling Contractual Discretion' (2013) 72 Cambridge Law Journal 65, 74; Stapleton (n 47).
[457] Hooley (n 456) 74.
[458] Stapleton (n 47) 8.
[459] Waddams, 'Good Faith, Unconscionability and Reasonable Expectations' (n 271) 60.
[460] ibid.

contracts where the parties are seen as adversaries, and an understanding of good faith which does not involve an objective assessment of the parties' reasonable expectations.

Protecting the reasonable expectations of the parties can be found under different terminology, such as obtaining the benefits of the contract, or effectuating parties' intents, or carrying forward the purpose of the contract.[461] It will usually be difficult to pinpoint the parties' expectations when there is a dispute and the parties are already at cross purposes. A retrospective assessment of the contractual expectation needs to be carried out, and that needs to be done in an objective manner. The express terms of the contract will be the starting point to identify the expectations, and at times the courts may refer to the parties' previous dealings.[462] An objective assessment of reasonableness is no new task in contract law, in particular when the courts are implying terms into contracts through the classical tests of officious bystander or business efficacy where the viewpoint of the reasonable person is always the deciding factor.[463] In such instances, the court will have to resort to evidence that is external to the parties' agreements, such as the community standards. This approach is sometimes referred to as contextualism.[464]

These standards can be derived from actual practice in a relevant industry or from moral beliefs held by the relevant community.[465] Practically, the distinction will be irrelevant. Where the court is trying to determine actual practice, it needs to look at past behaviour in that industry.[466] For this, the court will have to rely on evidence produced by experts in litigation. Similarly, where the court is ascertaining the relevant perceptions of morality in a specific community, it will again have to rely on the perceptions of a member of that community. The court will then have to use its discretion to determine the weight which needs to be accorded to each type of evidence. The issue with this approach is, of course, that the findings may change depending on the evidence and the identity of the expert or community member. There may be as many views on what the community standards are as there are experts or community

[461] Alan D Miller, Ronen Perry, 'Good Faith Performance' (2012) 98 Iowa Law Review 689, 716.
[462] The issue of interpretation is further explored in chp 4.2.
[463] Implied terms are discussed in chp 3.2.
[464] Brownsword 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 112.
[465] Miller and Perry, 'Good Faith Performance' (n 461) 725-726. For an approach that favors the reasonable expectations of the parties instead of community standards as the applicable standard to good faith in the performance of contracts, see Jeannie Marie Paterson, 'The Standard of Good Faith Performance: Reasonable Expectations or Community Standards?' in M Bryan (ed) *Private Law in Theory and Practice* (1st ed, Routledge-Cavendish 2007) 165, and Andrew Terry, Cary D Lernia, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions?' (2009) 33 Melbourne University Law Review 542, 564.
[466] These may be derived from trade associations, professional standards, and values of society at large, Ian R Macneil, 'Values in Contract: Internal and External' (1983) 78 Northwestern University Law Review 340, 367-368.

members.[467] One way of choosing the applicable community standard may be to pick the view of the majority. There are other ways too, but they all suffer from an inherent defect.[468] Regardless of whether an actual common practice or a common morality basis is preferred in determining the community standard applicable, they will inevitably have to be derived from a set of individual perceptions.[469] However, this conclusion does not divorce reasonable expectations from good faith.[470] To the contrary, it serves as an impetus to envisage good faith as an objective norm, one that has to tie itself to normative principles.[471]

Chen-Wishart's classification of contracts into four categories helps with a pragmatic categorisation of different components of good faith.[472] The categories are arm's-length contracts, symbiotic (or relational) contracts, contracts with recognised vulnerability and fiduciary relationships.[473] The first two of these categories are relevant for our purposes.[474] Good faith requirements of honesty, fair dealing and fidelity to the contractual purpose are present in all categories but differ in intensity.[475] A minimum content for good faith would be inclusive of "some limit on self-interested conduct" on the one hand and "some regard for the interest of the other party" on the other.[476] 'Honesty' and 'fair dealing' would gauge the respect for the 'legitimate interest of the other party as an equal', and 'fidelity to the contractual purpose' would gauge the 'respect for the contract made.'[477] Although such dissection of the concept may be helpful in better enforcing good faith duties in a contractual dispute, the common thread for all such compartments is the upholding of reasonable expectations of the

[467] Miller and Perry, 'Good Faith Performance' (n 461) 732, Miller and Perry criticise this approach through the application of a social-choice theorem. They propose various methods to combine the multitude of available community standards.
[468] ibid 744.
[469] ibid.
[470] For reasonable expectations being argued as the basis of good faith, see eg Feinman (n 287) 529.
[471] For a similar interrogation regarding the reasonable person in negligence law, see Alan D Miller, Ronen Perry, 'The Reasonable Person' (2012) 87 New York University Law Review 323, where the authors argue that the reasonable person concept, which has applications beyond tort law and potentially in contract law, cannot be positively defined by reference to the perceptions of the community in which the parties belong. Rather the concept needs to be defined by reference to normative principles, such as welfare maximisation, equal freedom, or ethic of care. For example, facilitating the efforts of contracting parties to maximise the joint gains in an efficient way can be one of such principles, see eg, Alan Schwartz and Robert E Scott, 'Contract Theory and the Limits of Contract Law' (2003) 113 Yale Law Journal 541.
[472] Chen-Wishart, *Contract Law* (n 244) 633.
[473] ibid 634, Chen-Wishart defines 'symbiotic' as those contracts that are 'characterised by the parties' interdependence in achieving the contractual purpose.' Therefore, they must not be 'zero-sum games' but require the parties' cooperation to maximise their joint profits; and it must be 'difficult or impossible to provide for all eventualities' therefore adjustments may be required in an ongoing contract.
[474] The reference to contracts involving recognised inequality of bargaining power does not include those between commercial parties with unequal bargaining power because those would be covered under the first two categories.
[475] Chen-Wishart, *Contract Law* (n 244) 634, for examples of application of such requirements. These are also referred to by Leggatt J in *Yam Seng* (n 3).
[476] ibid 621.
[477] ibid.

parties understood in an objective sense.[478] If a party does not deal honestly, fails to deal fairly or lacks fidelity to the contractual purpose, because, for instance, it exercises a contractual right capriciously, then this conduct can always be interpreted as breaching the reasonable expectations of the parties. Any assessment or alternative proposals for the contents of good faith are therefore intrinsically tied to the reasonable expectations of the parties, and simplify their application to concrete cases.

The paradigm arm's-length contract is posited as an individually negotiated contract between commercial parties which involves a spot transaction rather than a long-term cooperation and where the contract attempts to provide for all eventualities. The good faith requirements would be more stringent the further we move away from the paradigm case. For instance, in a relational contract, the parties are interdependent, they must cooperate to maximise their gains and their contract cannot provide for all eventualities due to the length and the high level of cooperation required. Consequently, honesty would require a positive duty of disclosure of information beyond that of which is required in arm's-length contracts. Moreover, fair dealing would prevent each party's pursuit of self-interest in spite of the other party's interests, however this does not prevent a party to pursue its own interests. Further, loyalty to the contract would prohibit any conduct which would prevent the proper performance of the contract and warrant that both parties are able to obtain the gains from their contract as agreed. Although Chen-Wishart provides for three constitutive components for good faith, it is argued that these relate to the upholding of the reasonable expectations of the parties as discussed above.[479]

In sum, the concept of good faith is an undefinable one which can only be demarcated in its factual applications. The standard of good faith is ultimately tied to the purpose of contract law itself, which is to provide a framework for contractual exchange by upholding the reasonable expectations of the parties and promote an ethic of cooperation and fair dealing, which is possible through a relational understanding of contracts.[480] Depending on whether a traditional or a more modern view of contract law is adopted, good faith's boundaries will shift accordingly. There have been numerous calls in the doctrine to rethink and understand the ideological foundation of modern contract law, none of which has led to a consensus.[481] The

[478] As discussed above in chp 1.3.1.2.
[479] See chp 1.3.1.2.
[480] As discussed in chp 1.3.1.3.
[481] Linda Mulcahy, 'The Limitations of Love and Altruism – Feminist Perspectives on Contract Law', in L Mulcahy, S Wheeler (eds), *Feminist Perspectives on Contract Law: Law and the New Politics of Postcolonialism* (Routledge 2005) 6-7.

quest was necessitated by fundamental changes in the markets, such as globalisation, the relegation of public functions to the private domain, the increase in size and length of trade contracts, including franchising.[482] The feminist academic discourse has even hinted at feminist views to offer potential ways forward, however, their attempt at connecting with the relational theory of contract reveals that it does not have much more to add to the debate than the work of relational theorists.[483] In sum, it is futile to search for a precise definition of good faith; rather, the inquiry should focus on the direction contract law takes in shaping its understanding of the nature of contractual relationships.

1.4. Good Faith as a Default Rule?

Despite an implication in fact of good faith in *Yam Seng*, Lord Leggatt argued extra-judicially that an obligation of good faith in the performance of contracts should be recognised as a default rule.[484] In general, the rules of English commercial law are not mandatory. The freedom of contract protects the parties' free choice and lets them contract outside of the default rules, delimited by public policy. First, default rules can operate as gap-filling in incomplete contracts. As such, implied terms operate as default rules where parties' express agreement fails to record their full agreement. Second, default rules contribute to reducing transaction costs.[485] Indeed, 'life is too short to negotiate contract terms designed to cover every contingency that may occur.'[486] Third, default rules serve to avoid unfair outcomes, 'whether through inertia, lack of opportunity or foresight, or deliberate choice, have not negotiated express terms to cover certain significant contingencies.'[487] Where the default rules themselves are efficient, the parties would be less inclined to exclude them, so not only does the presence

[482] ibid 6.
[483] ibid 10-11; where the rational theory already offers an emphasis on contextual and flexible understanding of contractual relationships, it is debatable whether the feminist theory can propose any alternative views in understanding contracts. Its main emphasis is the value of trust and cooperation in contractual performance however this is already achieved by the relational theory and the increased references to such concepts post-*Yam Seng* (15).
[484] Leggatt, 'Contractual Duties of Good Faith' (n 248) 9, although he adds that such default rule would have the greatest value when applied to relational contracts due to involving expectations of cooperation and loyalty by design.
[485] ibid. Muris (n 109) 524, the author suggests that '[r]esources spent to implement or prevent opportunistic behavior do not help produce a commodity or service that the contracting parties mutually value. Accordingly, the elimination or reduction of these expenditures will improve the wealth of society by freeing the resources for productive use.'
[486] *Barton v Morris and another (in place of Gwyn-Jones, decd)* [2023] UKSC 3, [2023] AC 684 [729] (Lord Leggatt SCJ).
[487] ibid [730]; CJ Goetz, RE Scott, The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Contract Terms (1985) 73(2) California Law Review 261, 265-266.

of default rules contribute to efficient contract making, but also the default rules themselves become more efficient over time as the less efficient ones are litigated and discarded.[488]

The efficiency of the default rule is influenced by its clarity; however, this is not the only factor. The parties may opt out of a default rule being influenced by costs, logistics, or other commercial concerns. Where the parties (or their legal advisers) have sufficient knowledge of contract law to expressly override any default rules that have not yet been made clear, thus efficient, the parties themselves contribute to making their contract clearer, but the default rules remain less efficient than if they were operative and litigated.[489] Where most negotiations crucially focus on the fundamental aspects of the deal, much of the non-negotiated terms would fall within the standard or boilerplate terms category or implied terms. If the issue later arising in litigation relates to fundamental terms which the parties have made clear in their express terms, then any inefficient (or uncertain) default rules do not raise any problems. The parties' express contract terms apply. However, if the issue relates to an inefficiency (or uncertainty) in regards to a standard non-negotiated clause or an implied term, the courts have to go through the process of interpretation to determine their extent. The most efficient, or 'optimal' default rules necessarily reflect 'prevailing social norms and expectations and therefore create rights and obligations which reasonable parties would be likely to agree between themselves.'[490]

Whether express good faith clauses qualify as a standard or boilerplate term is moot because there is no default rule applicable in English law. Nevertheless, the possibility of having good faith operate as a default rule is a question raised in the literature.[491] An interesting parallel can be drawn with tort law in this context. The introduction of the reasonableness criteria might have been seen as an overwhelming one, but the reality was that its later applications were not.[492] In fact, the reasonableness criterion was applied in an 'episodic manner' in tort law.[493] A similar argument can be mounted for good faith in contract law. Translating general abstract principles into concrete applications requires that the courts determine firstly the situations of application of the principle, secondly the standard of

[488] See the efficiency argument explored chp 1.2 above.
[489] This is the contracting response which was discussed in text to n 188 above in respect of possible responses to legal uncertainties.
[490] *Barton* (n 486) [730] (Lord Leggatt SCJ).
[491] See eg, Stapleton (n 47) 18 who refers to a 'presumption' of good faith.
[492] Stapleton (n 47) 28-29.
[493] ibid 29, the example given relates to the negligence principle where the rule is that a person should not cause injury by his unreasonable conduct; but such requirement is not applied in the context of where a person watches a stranger drown. They are not under any duty to save them, no matter how unreasonable the inaction is.

application and thirdly the remedial response for the breach.[494] Indeed, the situations of application of the principle would indicate the instances where the principle of good faith is triggered. This would not necessarily mean a 'single formulaic test.'[495] As such, not all deliberate pursuit of self-interest will merit legal sanction. An overarching good faith principle would not, as such, impose blanket good faith obligations. The references to reasonable expectations as explored in the previous section can, in this respect, be misleading as imposing a legal entitlement across the board.[496] However, in the context of commercial contracts, the reasonable expectations are determined directly by the benefit each party is expected to receive from the contract, and the value it has agreed to provide in exchange for it.[497] As such, a breach of good faith would occur where a party's conduct would negatively affect such benefit.

Where an alternative to the classical contract theory is envisaged, the parties' autonomy may be seen to be enhanced through the adoption of a liberal theory of contract. Dagan and Heller propose a 'freedom of contracts' lens to enhance party autonomy in contracts.[498] Such a lens recognises a freedom to choose form '*among'* contract types, not only to bargain for terms '*within'* a contract.[499] As such, its approach to default rules is also interesting. Where the parties can choose terms from other contract types, contract law seeks to uphold or regulate the opt-outs to ensure that the contract indeed reflects the parties' informed and rational choices. However,

> to the extent possible, contract laws should try overcoming problems of information asymmetry, cognitive biases, and strategic behavior as well as engage in the cultural production of stable expectations regarding contract types by prescribing sticky defaults, rather than curtailing choice by using mandatory rules.[500]

This approach moves the focus away from arm's length transactions in commercial law and encompasses those where the parties do not have equal bargaining power. However, regulating 'sticky defaults' for each contract type would need to be justified, which would necessarily

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[494] ibid.
[495] ibid 31.
[496] See text to n 319.
[497] For instance, in a sales contract, the seller's benefit is the monies to be generated from the sale in exchange for its time, effort and monies spent in creating the product or service. The buyer's benefit is the product or service obtained, in exchange for an amount equivalent to the sales price. In the context of revenue generating and sharing contracts, a categorisation which is proposed in chp 3.2.3.1.2, the function of the reasonable expectations is rather to determine the extent of the revenue to be generated by that contract through mutual effort and the respective share of each party out of that revenue.
[498] Dagan, Heller 'Freedom of Contracts' (n 298) 68.
[499] ibid 4.
[500] Hanoch Dagan, 'Pluralism and Perfectionism in Private Law' (2012) 112 Columbia Law Review 1409, 1436.

limit the ability to opt out of them. For this, (1) the regulation must be essential to the viability of that contract type; (2) people must be able to freely involve the regulated contract type; and (3) the regulation must be at a minimum to avoid interference with party autonomy.[501] The first condition recognises the limitation of the feasibility of contract types without any legal basis; where the existence of the contract type depends on the availability of legal rules, then such rules must exist to ensure its continued existence. This is not particularly an issue in commercial contracts that do not feature consumers. Where the commercial parties wish to contract, they can do so and even if they don't draw up a contract, they can fall back on the minimum default rules applicable in similar dealings. The second condition is where the parties can choose to apply one contract type instead of another, for instance, where they wish to avoid a heavily regulated sphere. However, in business contracts, this is not possible where the statutory provisions impose mandatory rules for specific types of contracts.[502] Outside of any statutory provisions, commercial parties are free to opt out of any rules subject to public policy and fairness considerations. Thirdly, to justify the presence of a sticky default rule, it must be more efficient for the parties to choose to keep the default rule rather than choose to opt out. This is because default rules can be justified on efficiency grounds.[503] This is particularly important in commercial deals where standard contract terms are widely used.

The parties cannot draft complete contracts and must rely on default rules wherever possible. Where the parties have omitted to provide for a particular contingency, the default rule may be triggered. It is not to say that the default rule applies to interpret the contract. Rather, it applies to supplement the agreement of the parties and arrive at a resolution in litigation. The presence of a default rule also has a socially justifiable gain, which is that it can provide efficient solutions to common contracting problems, thus saving money for the commercial parties. However, this view implies that the default rules are those which would have been chosen by the parties had they put their minds to the issue at the contracting stage. This is not true because commercial parties themselves are the only ones who can best judge

[501] Dagan, Heller 'Freedom of Contracts' (n 298) 63.
[502] For instance, the parties cannot escape the application of the Insurance Act 2015, s 16(1) which provides that the parties cannot opt out of the provisions of the Act which have the effect of putting the insured in a worse position than the protection accorded to it under the Act.
[503] See eg Ian Ayres, 'Regulating Opt-Outs: An Economic Analysis of Altering Rules' (2012) 121 Yale Law Journal 2032, 2097 (sticky defaults serve to minimise the costs of party and judicial error); Omri Ben-Shahar, John A Pottow, 'On the Stickiness of Default Rules' (2006) 33 Florida State University Law Review 651 (the parties may not choose to opt out of a default even where a better provision can be easily identified and articulated at a negligible drafting cost due to fears of upsetting the contract altogether); Schwartz, Scott, 'Contract Theory and the Limits of Contract Law' (n 471) 594 (commercial parties contract out of inefficient default rules, increasing transaction costs).

what would have been an ideal contracting term. The efficiency of the default rules is sometimes gauged by whether they maximise the parties' joint surplus (namely the total value created by a contract for both parties), rather than being assessed on fairness grounds (such as the fair or equal distribution of the surplus).[504] As such, a good default rule is argued as one which is dependent on only a limited instance of applicability, simple in form and efficient for a wide variety of parties.[505] The first criterion is justified by pragmatism, whereas the third one acknowledges that a default rule cannot be satisfactory for every commercial actor on the market; rather, it has to be efficient, meaning maximising surplus in most cases.

The default rules in contract law are scarce due to the difficulty of satisfying all three above criteria. If good faith itself were to be envisaged as a default rule, then it should be capable of providing a clear answer to contracting problems in advance of the contracting parties' actions.[506] However, this is not possible due to its context-dependent nature to determine whether the act is in line with the reasonable expectations of the parties in a specific contract. When a rule intended for broad application is vaguely formulated, parties are more likely to contract out of it.[507] Even if the parties do not contract out, the party relying on it might seek to resolve the ambiguity, thereby jeopardising the joint returns.[508] Whereas, a standard will be deemed efficient, and unlikely to be opted out of, 'only when the party on whom it confers discretion has the incentive to maximise joint returns in the course of maximising its private gain.'[509] Understandably, commercial parties that incorporate a standard into their contract typically supplement it with specific rules to delineate its intended scope and application. Where there is no indication of an express standard, the common law can thus develop over time transcontextual rules to supplement the parties' agreement.[510] Although it is argued, in chapter 4.5, that good faith, if recognised as an overarching standard in

[504] Schwartz, Scott, 'Contract Theory and the Limits of Contract Law' (n 471) 596.
[505] ibid.
[506] For the difference between rule and standard, see Schwartz, Scott, 'The Common Law of Contract and the Default Rule Project' (n 247) (a rule specifies required behaviour in advance of the contracting parties' actions, whereas a standard allows a court later to decide whether actions the parties have already taken satisfied the relevant contractual requirement).
[507] Schwartz, Scott, 'The Common Law of Contract and the Default Rule Project' (n 247) 1530, in the context of US contract law, rather than the Restatement and Uniform Commercial Code proposing transcontextual default rules and standards, the common law is argued to be a better vehicle for creating transcontextual default rules. This is because commercial parties are averse to publicly supplied transcontextual standards and much rather prefer to contract out of them, thus increasing the contracting costs.
[508] Schwartz, Scott, 'Contract Theory and the Limits of Contract Law' (n 471) [603].
[509] ibid.
[510] Schwartz, Scott, 'The Common Law of Contract and the Default Rule Project' (n 247) 1587, the arguments are made in the context of US contract law but are relevant for English law due to the shared common law origins of both systems of law.

commercial contracts, should not be subject to exclusion, it could nonetheless serve as a foundation from which specific default rules may be developed over time as needed.

1.5. Conclusion

This chapter offered an overview of the main conceptual issues surrounding good faith in English contract law. The fears raised by its opponents proved to be unfounded and rather unjustified by misplaced contempt for general principles. The process of constructing new legal concepts by the courts is crucial in understanding the future of good faith in contract law. This is different for establishing new rules and principles, with principles requiring more extensive support for recognition. The courts' adoption of inductive reasoning necessarily brings its own challenges, when developing general principles; however, an aversion to general principles of law cannot be justified as the underlying rationale of the law itself draws on philosophical concepts such as fairness. The unquestioned dedication to certainty and freedom of contract has muddied the waters for a long time, however, a modern understanding of contract law necessitates an explicit recognition that contract law norms fairness just as much.[511]

Good faith's purpose is directly linked to the purpose of contract law. Whilst it is accepted that contract law seeks to uphold the expectations of reasonable people, it has a wider regulatory role, which is that of curbing opportunistic behaviour and thereby encouraging cooperative dealings. Such a view necessitates a modern understanding of contract law, which moves away from the confines of the classical contract theory in which the parties are posited as adversaries. Good faith's normative nature allows for furthering such an agenda. It can operate as an overarching standard to bring coherence to a fragmented approach to unfairness issues in contract performance. Moreover, efficient rules can be devised based on such a standard to sanction unfairness in specific scenarios.

Despite its vagueness, good faith does not need a precise definition to serve the institution of contract law. Honesty, fair dealing and fidelity to the contractual purpose are all possible explanations for the concept, the ultimate common thread being the reasonable expectations of the parties, which links back to the purpose of contract law. Thus, an overarching recognition of good faith in contract performance is not only desirable but necessary as long as contract law seeks to uphold the parties' reasonable expectations and

[511] Catterwell, 'The Limits on Intention in Contract' (n 309) 583.

regulate fairness in contractual dealings. The next chapter provides evidence of contract law's such endeavours.

CHAPTER 2 INSUFFICIENCY OF LEGAL DOCTRINES IN REGULATING UNFAIRNESS IN THE PERFORMANCE OF COMMERCIAL CONTRACTS

2.1. Introduction

The 'functional equivalence' approach posits that an overarching principle of good faith is not required, as the common law already provides functionally equivalent solutions.[512] Doctrines such as duress, undue influence, or mistake can be used to set aside contracts where a party's consent has been vitiated. However, doctrines that regulate unfairness in contractual performance are fewer and elusive.[513] The use of a doctrine of inequality of bargaining power is controversial, whereas unconscionability and estoppel are more acceptable to the courts as they have been developed over the years.[514] The effect of the Judicature Act 1873 and Judicature Act 1875 has been detrimental to the development of equitable concepts.[515] Indeed, despite the Acts providing that in case of conflict, equity was supposed to prevail over common law rules, equity was 'marginalized because it came to seem inconsistent with common law rules.'[516] The law has instead embraced 'a simplified account of contract law.'[517] Nonetheless, equity marginally operates as a reassuring mechanism in cases where contractual interpretation or the implication of terms into a contract produce unsatisfactory outcomes. As such, an estoppel can be raised as a defence against unconscionable behaviour to prevent a party from going back on its promise or representation. It can even be the basis of a cause of action in the context of a proprietary estoppel.[518] Andrews summarises the state of the law correctly when he states that:

> (...) many doctrines can be marshalled to substantiate the easy and indeed 'open-door' assertion that English law displays pragmatic ethical sensitivity in its treatment of private law issues, notably contractual matters, by deployment of an array of legal techniques rooted in notions of 'good faith' or 'fair dealing.' In this sense, English law

[512] See text to n 269.
[513] For the discussion on the concept of fairness, see chp 1.3.1.1. Also see Catterwell, 'The Limits on Intention in Contract' (n 309) 583 who states that fairness, outside of contract formation issues, 'acts as a limit on the role of intention in contract.'
[514] McKendrick, *Contract Law* (n 1) 110.
[515] Stephen M Waddams, 'Equity in English Contract Law: The Impact of the Judicature Acts (1873–75)' (2012) 33(2) The Journal of Legal History 185, 192, 208.
[516] ibid.
[517] ibid.
[518] McKendrick, *Contract Law* (n 1) 110.

> is alert to arguments which can be generalised as facets of 'good faith'—but it is not driven by a nominate doctrine (...).[519]

If the deployment of good faith serves to carry out the purpose of the contract to regulate unfairness in contractual performance, as discussed in the previous chapter, we must also investigate how and if the existing doctrines are helping with such a task. Such an investigation is necessary to the extent that the principle of legal certainty does not allow for principles being stacked on top of each other, in particular if they aim to serve the same purpose. The analysis is not intended to be all-encompassing; this chapter rather serves to provide an insight into the insufficiency of existing legal doctrines in regulating unfairness in contractual performance.

2.2. Unconscionability and Estoppel

Following the enactment of the Judicature Acts 1873 and 1875, the marginalisation of unconscionability as a doctrine reached its peak when 'in Halsbury's Laws of England (1907–15) (...) unconscionable contracts were excluded altogether from the article on Contract, and dealt with, anomalously, in a different volume in the article on Fraudulent and Voidable Conveyances (a quite separate topic).'[520] Unconscionability was enshrined in a few statutes in regards to specific transactions; however this further 'weaken[*s*] support for a general judicial power to set aside other kinds of contracts for unfairness.'[521] Much later, in *Alec Lobb (Garages) Ltd v Total Oil (Great Britain) Ltd,* the court restated the requirements of the doctrine, namely that (i) one party must be at a serious disadvantage to the other, (ii) the weakness of that party has been exploited by the other in a 'morally culpable manner' and (iii) the transaction is 'overreaching and oppressive.'[522] There must be an element to the resulting transaction which would shock 'the conscience of the court.'[523] It may be that under the first criteria, the party was 'elderly', 'illiterate' or 'on a very low income.'[524] It may also be that the serious disadvantage is due to 'ignorance, or lack of advice or otherwise, so that circumstances

[519] Neil Andrews, 'Reliance in the Breaking-off of Contractual Negotiations: Trust and Expectation in a Comparative Perspective by Isabel Zuloaga' (2021) 137 LQR 176, 177-178.
[520] Waddams, 'Equity in English Contract Law: The Impact of the Judicature Acts (1873–75)' (n 515) 192.
[521] ibid, fn 43.
[522] [1983] 1 WLR 87, 94-95 (Peter Millet QC). The argument of unconscionability failed in this case as the party alleged to be suffering the disadvantage was an experienced businessman who had received advice and the transactions were not oppressive. Moreover, the other party had not taken advantage. Although the bargaining position of the claimant was weak due to suffering financial difficulties, he had rejected the legal advice received and entered into an unfavourable leaseback arrangement.
[523] ibid 95.
[524] Portman Building Society v Dusangh [2000] 2 All ER (Comm) (CA) 221, 229 (Simon Brown LJ).

existed of which unfair advantage could be taken.'[525] The stronger party need not have contributed to the other party's weakness.[526] The second criterion requires that the exploiting party knew of such weakness and actively exploited it.[527] The third criterion requires a high threshold, the deal cannot simply be unreasonable or unjust without an exploitation element.[528] Moreover, if the weaker party has sought legal advice before entering into the deal, this would 'weigh heavily in neutralising [its] serious advantage.'[529] Consequently, the stronger party is prohibited from exploiting the weakness of the other if to do so would result in an oppressive deal. It is the moral culpability of the exploiting party which triggers the intervention of the doctrine.[530] Notably, unconscionability is often used alongside other doctrines, one of which we shall now discuss.[531]

Estoppel

In *Cobbe v Yeoman's Row Management Ltd*, the House of Lords decided that unconscionability alone would not suffice on its own to provide a remedy to a litigant. Indeed, the court concluded that to grant a proprietary estoppel, the conditions for such an estoppel must be satisfied and that unconscionability alone could not grant a remedy to the litigant. Lord Scott opined that:

> [t]o treat a 'proprietary estoppel equity' as requiring neither a proprietary claim by the claimant nor an estoppel against the defendant but simply unconscionable behaviour is, in my respectful opinion, a recipe for confusion.[532]

The different categories of estoppel are the subject of a debate in themselves. Estoppel is not confined to contractual law. It is often debatable whether it operates independently of other doctrines or rather, deserves a doctrine on its own. For instance, distinguishing between an estoppel by representation and a promissory estoppel is straightforward, as the former relates to reliance and the latter to a promise to assert or not assert a right. However, they both relate to 'the rights of those who rely (to their detriment) on promises which are not otherwise

[525] *Alec Lobb* (n 522) [94-95] (Millet QC)
[526] Ying Khai Liew and Debbie Yu, 'The Unconscionable Bargains Doctrine in England and Australia: Cousins or Siblings?' 45(1) Melbourne University Law Review 206, 216.
[527] ibid 221, 226.
[528] ibid 228.
[529] ibid 233.
[530] Charlotte Thomas, 'What Role Should Substantive Fairness Have in the English Law of Contract - An Overview of the Law' (2010) 6 Cambridge Student Law Review 177, 186.
[531] Such as estoppel, rectification, undue influence, injunctions, specific performance. Similarly, penalty clauses and restraint of trade doctrines also benefit from an assessment of unconscionability, see Thomas (n 530).
[532] [2008] UKHL 55, [2008] 1 WLR 1752 [16] (Lord Scott).

enforceable.'[533] A promissory estoppel arises where a party makes a promise as to future conduct to the promisee, and the promisee relies on such promise, not necessarily to his detriment, and if inequitable to do so, the promisor will not be able to go back on his promise. It will usually be inequitable for the promisor to go back on his promise where the promisee has relied on the promise. In *Collier v Wright*,[534] the court held that it was inequitable for the creditor to go back on its promise not to claim the remainder of the debt from all of the debtors.[535] As such, the acceptance of part payment of the debt by the creditor had the effect of extinguishing the creditor's right to the balance of the debt.

In contrast, in an estoppel by representation, representation relates to a fact and the other side must have relied on it to its detriment. In *Avon County Council v Howlett,*[536] the defendant received more than he was entitled to by his employers due to the employers' mistake. The employers claimed the monies back but the defendant relied on an estoppel by representation. He argued that the employers should be estopped because they had made a representation of fact to him that he was entitled to the money and he had acted to his detriment by relying on that representation and spending it. However, the courts do have a wider view of the facts and can prevent the operation of the estoppel as a full defence on the basis of unconscionability. Indeed, in *National Westminster Bank plc v Somer International (UK) Ltd,* a bank claimed back monies paid by mistake to its client company. The company relied on the representation of fact that the receipt of monies into the company's account were the expected monies as previously stated to the bank.[537] The company then despatched certain goods to the concerned client before actual payment from the client was made. The Court of Appeal allowed estoppel by representation to operate only partially and not as a defence to the whole of the bank's claim. The court stated that, having regards to the overall detriment suffered and the benefit obtained by each party, unconscionability should operate to alleviate the unfairness in such mistaken payment cases.[538] As such, the company was not allowed to retain the balance over and above the value of the goods shipped.[539]

In the context of a proprietary estoppel, unconscionability seeks to play a different role than in other types of estoppel such as promissory or by convention. Indeed, rather than being

[533] Ewan McKendrick, *Contract Law* (n 1) 116.
[534] [2007] EWCA Civ 1329, [2008] 1 WLR 643.
[535] The word 'inequitable' and 'unconscionable' are used interchangeably by the courts.
[536] [1983] 1 WLR 603.
[537] [2001] EWCA Civ 970, [2002] 1 All ER 198.
[538] ibid [68] (Gibson LJ).
[539] ibid [48] (Potter LJ).

a tool for regulating bad behaviour, it operates as a mechanism to control that the necessary formality requirements have been respected in the creation or transfer or property rights.[540]According to Dixon, one must distinguish between an assurance as to the transfer of the property right ('the rights assurance'), and an assurance as to the transfer of the right regardless of whether the formalities to transfer the right are complied with ('the formality assurance').[541] He argues that unconscionability operates as to the formality assurance, and not to the rights assurance, and as such '[u]nconscionability exists when a 'formality assurance' is withdrawn after detrimental reliance.'[542] Therefore, a 'formality assurance' must have been given, explicitly or implicitly, to make going back on a 'rights assurance' unconscionable. If no such 'formality assurance' was given, then it would not be unconscionable to go back on the 'rights assurance'. The main issue with this approach, also accepted by Dixon himself, is that in commercial cases it would be very hard to prove that a 'formality assurance' was given, because the parties would usually understand that formality is required, therefore in the absence of an express 'formality assurance' an implied 'formality assurance' will be unlikely, so will be an estoppel.[543] Moreover, the court's discretion to have a broad view of the facts and determine the extent and the effect of the estoppel to be granted will depend on the factors which the court determines to be decisive on a case-by-case basis.[544]

A more recent category of estoppel is contractual estoppel. In reality, this is no estoppel at all.[545] It is different from an estoppel by convention, such estoppels require proof that it would be unconscionable for the maker of the statement to go back on it. In a contractual estoppel, there is no criterion of reliance, detriment and unconscionability as for other types of estoppel. The source of the cause of action is contractual rather than reliance. The parties are agreeing to a certain state of facts or law, subject to all the formation requirements, as the basis of their agreement, they will then be precluded from reneging on such agreement. This rule remains valid even if they knew that the state of affairs they were relying on was not true.[546] Although considerations of mistake and misrepresentation may be useful to consider, due to

[540] Martin Dixon, 'Confining and Defining Proprietary Estoppel: The Role of Unconscionability' (2010) 30(3) Legal Studies 408, 408–420.
[541] ibid 417.
[542] ibid.
[543] ibid 417-418.
[544] ibid 420.
[545] Jo Braithwaite, 'The Origins and Implications of Contractual Estoppel' (2016) 132 Law Quarterly Review 120 argues that even if the contractual estoppel is no estoppel at all, it is in fact a hybrid of authority and principle which has over time become a well-established and distinct rule based on freedom of contract.
[546] In *Springwell Navigation Corp v JP Morgan Chase Bank & Ors* [2010] EWCA Civ 1221, [2010] 2 CLC 705, [748] Lord Justice Aiken states that there is no reason why the parties cannot knowingly agree on the basis of an untrue state of affairs, unless such agreement is against a certain public policy rule.

being a contractual claim, the reasonableness test under the UCTA 1977 will have to be satisfied if the parties are contracting based on the other's standard terms. In *Springwell Navigation Corp v JP Morgan Chase Bank & Ors,* the Court of Appeal allowed the operation of a contractual estoppel and provided that the bank could rely on the contract's strict boilerplate term that no investment advice was being given to the claimant.[547] Surprisingly, a large investment bank could deny responsibility for the loss caused to the claimant in its investment made through that bank, and it begs the question as to whether contractual estoppel goes in the opposite direction from what other doctrines seeking to achieve fairness try to do in the context of commercial contracts. There is support in the doctrine for the eradication of contractual estoppel altogether.[548]

Consequently, unconscionability is hard to define and will vary on a case-by-case basis. It may not always be unconscionable when a party has relied on the other party's promise if no added detriment can be shown.[549] Unconscionability, as seen from the above paragraphs, does play a role in determining whether an estoppel arises and to what extent. However, the unconscionability considerations are limited and not uniform across the estoppel case law. Thus, questioning the ultimate purpose of a doctrine of estoppel should help illuminate the relationship between unconscionability and estoppel. As such, the question regarding the function of a doctrine of estoppel is whether it should prioritise (i) the protection of the aggrieved party's reliance by punishing the other party's unconscionable behaviour, or (ii) the protection of the aggrieved party's expectation by upholding the original promise.[550] Such a question necessarily requires an answer from either a tortious or contractual standpoint.

An Independent Doctrine of Unconscionability?

The use of unconscionability alongside other doctrines raises the question of whether it merits recognition as a standalone doctrine. McKendrick summarises four principles objections which can be raised against the creation of an independent unconscionability doctrine. He states

[547] In *Springwell* (n 546), JP Morgan was providing banking services including investment activities to a large shipping company. The company sued for losses resulting from bad investment advice, but the bank argued and won on a strict interpretation of the no investment advice clause contained in their agreement.
[548] See for eg Gerard McMeel, 'Banks, the Judiciary and 'Documentary Fundamentalism'' (Counsel Magazine, April 2015) <https://www.counselmagazine.co.uk/articles/banks-the-judiciary-and-documentary-fundamentalism> accessed 3 April 2025.
[549] *Societe Italo-Belge Pour le Commerce et L'Industrie SA (Antwerp) v Palm and Vegetable Oils (Malaysia) Sdn Bhd (The Post Chaser)* [1982] 1 All ER 19, [1981] 2 Lloyd's Rep. 695, it was held that by requesting that the declaration of the ship be provided from the sellers not to the buyers but to the sub-buyers, the buyers were waiving any defect in the documents. The court held that the sellers had not been prejudiced in the reliance, and it was not inequitable for the buyers to reject the documents. No damages were awarded to the sellers.
[550] McKendrick, *Contract Law* (n 1) 116.

first the difficulty for the courts to determine the unfairness of a transaction within the context of litigation without necessarily an understanding of the market; second, the risk of introducing an unacceptable degree of uncertainty into transactions; third, English law's general aversion to general legal principles and preference for case by case development of the law; and finally, the ultimate purpose of contract law not being redistribution of wealth.[551] Nonetheless, fairness considerations do come into play in contract law. The way the courts approach interpretation of exclusion or liability clauses, their refusal to hold valid the incorporation of onerous terms, their creation of the category of innominate terms providing the courts with flexibility in determining the remedies depending on the seriousness of the breach, their expansion of estoppel and misrepresentation types, are all hints that point towards a hope of fair outcome in contractual dispute resolution. McKendrick considers that although the Parliament should continue to play the main role in curtailing freedom of contract, the courts can create a doctrine of unconscionability to fill the gaps left by the Parliament.[552] He accepts that it is difficult to identify 'the principle which explains why the law is concerned with the fairness of the contract.'[553] This is because of the lack of an overarching principle of good faith. Sanctioning unconscionable behaviour does not necessarily negate the need for such an overriding principle. Indeed, a principle of unconscionability could emanate from an all-encompassing good faith principle and be in line with the prohibitive-type principles which already exist in English law, by seeking to deter and sanction inequitable conduct in commercial transactions.

Further support for this approach can be found in the argument that the doctrine of unconscionability, although it is usually seen as correcting a procedural unfairness in the formation of the contract, is seeking to ensure substantive fairness in contracts.[554] Procedural unfairness relates to unfairness in the way the contract was formed, and substantive fairness relates to unfairness in the terms of the contract, where they may be more favourable to one party than the other.[555] However, the regulation of substantive fairness is sometimes considered to curtail contractual freedom and individual autonomy, therefore, a Parliamentary intervention

[551] McKendrick, *Contract Law* (n 1) 351. For a similar view, see Davies, *JC Smith's the Law of Contract* (n 56) 292 who considers that 'any theoretical advantages that may follow from endorsing a broadly applicable concept of unconscionability are outweighed by the uncertainty it would provoke in (probably) expanding the grounds on which a court will set a contract aside, when the general principle is that contracts should be upheld and given effect.'
[552] ibid 352.
[553] ibid.
[554] Thomas (n 530) 182-183, 188.
[555] ibid 177.

is suggested as more adequate due to its ability to 'take a wide view of the different interest grounds concerned (...).'[556]

A narrow view of good faith is sometimes labelled as unconscionability in the context of contract interpretation and implication of terms.[557] It is used to mean that a party may not seek to take advantage of an omission in risk allocation at the time of contracting and seek to exploit that gap. This can be done by advancing arguments for the implication of terms in fact where the parties had effectively failed to provide for an express allocation of risk in the contract. However good faith is broader than such narrow labelling.[558] In sum, unconscionability remains of limited application.[559] It is usually said to be included as an argument of last resort in addition to other claims, such as misrepresentation and undue influence, which are easier to establish as 'their ingredients are conceptually more certain.'[560] The courts use it when faced with an outrageous contract. More importantly, it is understood as a doctrine to protect against defective consent rather than deter opportunistic contractual performance.[561]

There has been a recent attempt to introduce statutory reform on unconscionable conduct. The Unconscionable Conduct in Commerce Bill HL (2019-2021) [37] (UCCB) was proposed in 2020 to create an offence of conduct in trade and commerce that is unconscionable. Any type of unconscionable conduct in trade or commerce carried a criminal penalty, including an unlimited fine or prison sentence not exceeding seven years.[562] Although a criminal type of statute in nature, it attempted to regulate conduct and dealings anchored in commercial law. Notably, it provided a guideline for the courts to determine whether the conduct in question was unconscionable, such as reviewing the terms of the contract, the relative strengths of the bargaining positions of the parties, or whether the conduct was in good faith.[563] After the first

[556] ibid 196.
[557] Hugh Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (2014) 67 CLP 297, 314-315.
[558] See chp 1.3.1.3.
[559] Some authors have suggested that undue influence and unconscionability should be merged into one doctrine, see eg David Capper, 'Undue Influence and Unconscionability: A Rationalisation' (1998) 114 LQR 479, 501 however the author's proposal is rather a doctrine of unconscionability which deals with procedural unfairness. The author does not support a general doctrine of unconscionability which would correct substantive unfairness, stating that English law's response to substantively unfair contracts is to alter them, but only in very limited circumstances, such as where penalty clauses are concerned or where unfair portions of a restraint of trade clause is severed.
[560] Robert Merkin, Severine Saintier, *Poole's Casebook on Contract Law* (16th edn, Oxford University Press 2021) 571.
[561] Severine Saintier, 'Defects of Consent in English Law: Protecting the Bargain?' in L DiMatteo, M Hogg (eds), *Comparative Contract Law: British and American Perspectives* (Oxford University Press 2015) 129-130.
[562] UCCB, s 1(2).
[563] UCCB, s 2.

reading took place, the UCCB made no further progress as the 2019-2021 session of Parliament had prorogued. Despite a useful attempt at drawing attention to the matter, and encompassing all types of transactions, whether consumer or otherwise, it was an inappropriate means of regulating fairness through the imposition of criminal sanctions. A better way is proposed further below.[564]

2.3. Abuse of Rights and Fraud on a Power

Another concept which is relevant in the context of regulating unfairness in contractual performance is that of abuse of rights. A civil law concept in origin, it is not recognised as a doctrine in English contract law. It is understood to mean 'the exercise of power predominantly for the purpose of damaging the other party's interests rather than serving the interests of the power-holder.'[565] However, an argument can be made that the abuse of rights concept is already present but hidden in English law.[566] Indeed, the rationale behind specific legislation can be based on the concept itself.[567] Usually, the rejection of the doctrine is dealt with in tort cases.[568] The purpose behind the concept is to prevent parties from relying on rights in a way that the simple fact of relying on them would be contrary to their aim. In relying on a concept of abuse of rights, there is an attempt to curtail the protection of any legal interests that the relationship did not intend to protect at the outset. Looking beyond the motives of the parties, the concept of abuse of rights seeks, like the good faith concept argued herein, to subject the use of rights to an objective assessment of honesty.[569]

In *Times Travel*, although not a contractual performance dispute, the reference to abuse of rights in Lord Hodge's judgment is interesting.[570] Although he stated that there is no doctrine

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[564] See chp 6.4.

[565] Hugh Collins, 'Discretionary Powers in Contracts' in D Campbell, H Collins and J Wightman (eds.), *Implicit Dimensions of Contracts: Discrete, Relational and Network Contracts* (Hart Publishing 2003) 223.

[566] Solene Rowan, 'Abuse of Rights in English Contract Law: Hidden in Plain Sight?' (2021) 84(5) MLR 1066.

[567] Harold C Gutteridge, 'Abuse of Rights' (1933) 5 Cambridge Law Journal 22, 30 gives the example of the Judicature Act 1922, s 51 to prevent abusive proceedings, Moneylenders Act 1911-1927 to restrict the rights of the money-lenders, or the Landlord and Tenant Act 1927, s 5 to restrict the rights of landlords to refuse the renewal of a lease of certain premises. However, the author does not support a recognition of an abuse of rights doctrine, similar to that in civil law, 'which may in effect be destructive of the liberty of the individual' (45).

[568] See eg *Bradford Corp v Pickles* [1895] AC 587 (HL); *Allen v Flood* [1898] AC 1 (HL).

[569] Gutteridge, 'Abuse of Rights' (n 567) 26-27, argues that if an abuse of rights doctrine were to be recognised in English law, the assessment of it would be objective, understood as an 'unreasonable' or 'excessive' exercise of a right.

[570] *Times Travel* (n 266). This was a case in which the court had to consider whether lawful acts could make up a claim of economic duress in the context of a travel business deal. Times Travel (TT) was a small travel agent who sold tickets for flights on Pakistan International Airlines Corporation (PIAC). In 2008, PIAC and TT entered into an agency contract whereby TT would receive commission on the sale of tickets on PIAC flights to the public. At the time of the facts, PIAC was the only carrier for direct flights between Pakistan and the UK and TT's business

of abuse of rights in English contract law, he recognised that there are instances where judges will have to rule in favour of socially objectionable behaviour to preserve the legal certainty. The certainty referred to therein is questionable in that the judges are free to expand existing principles depending on the approach they choose to take; however, it is often unclear the legal basis they rely on. On the topic of abuse of rights, which is closely related to good faith, Lord Hodge SCJ stated that:

> [a]ll that is not prohibited is permitted and there is no general doctrine of abuse of rights. If therefore a person is permitted to do something, he will generally be allowed to do it for any reason or for none. (...) Again, this is soundly based for judges should not, as a general rule, be the arbiters of what is socially unacceptable and attach legal consequences to such conduct.[571]

Although Lord Hodge SCJ's reference was made in the context of commercial negotiations, the remarks are relevant for the performance of the contract too. Lord Hodge SCJ further commented on the implications of the *CTN Cash and Carry Ltd v Gallaher Ltd (CTN)* judgment.[572] He stated that:

> (…) the dishonest assertion of a pre-existing entitlement to payment accompanied by a threat to carry out a lawful act, such as to withdraw credit arrangements on future contracts or to refuse to enter into further contracts, could amount to lawful act duress as a form of an abuse of right.[573]

Lord Hodge SCJ interestingly extended the benefit of the doubt to an abuse of right doctrine, but not to a good faith one. He recognised that the issue with extending the economic lawful duress doctrine further would encounter an anchoring problem. The absence of a general principle of good faith stops the expansion of the lawful duress doctrine in its tracks and

almost entirely consisted of its dealings with PIAC. In 2012, a dispute arose as to an alleged commission due to TT. During negotiations, PIAC asked the agent to waive previously earned commissions, significantly reduced TT's allocation of tickets on its planes under threat that their contractual relationship would not continue if they did not enter into the new contract. With no viable alternatives, the agent waived the commissions and renewed the contract with PIAC. Later, TT argued that the waiver was not binding on the basis that it was obtained under duress. High Court held that TT was entitled to rescind the contract on the basis of economic duress. The decision was overturned by the Court of Appeal. The Supreme Court has upheld the Court of Appeal's decision holding that there was no economic duress.

[571] *Times Travel* (n 266) [28] (Lord Hodge SCJ citing Jack Beatson, *The Use and Abuse of Unjust Enrichment* (Oxford University Press 1991)).

[572] [1994] 4 All ER 714, [1993] 2 WLUK 202.

[573] *Times Travel* (n 266) [44] (Lord Hodge SCJ).

confines it to instances where the courts have previously recognised such an extension in cases with specific particularities. If the same particularities do not apply in the case at hand, then the court is faced with the difficulty that the doctrine cannot be extended, unless there is an acceptable anchoring.

The larger issue with this restrictive type of reasoning is that it does not take into account scenarios where there may be no bad faith demand as argued in *Times Travel*.[574] There will be instances where the demand will not be made in bad faith, but where the exercise of the right will defeat its original purpose. For that, a right must exist in the first place. Echoing Sir Beatson's view above that '[a]ll that is not prohibited is permitted' where a right does not already exist, the list of prohibited behaviour would be long and near impossible to determine ahead of a dispute.[575] The better view is that all that is not prohibited by the rights conferred upon the parties in the contract should be permitted. Therefore, the analysis goes beyond the extent of the right conferred, but encompasses how such right should be exercised.[576] If such a view were to be adopted, then the analysis in *Times Travel* could be rephrased as follows: were the rights to terminate the contract and to decrease the number of allocated seats to the agent, even though not strictly made in bad faith, used in an abusive manner by the airline company? Consequently, the issue would not be whether the doctrine of economic duress could be extended on the finding of a suitable anchor, but whether the exercise of the rights already present in the contract was defeating the original purpose of the parties. It could, for instance, be argued that the parties' reasonable expectations when concluding the contract were that they did not set out the termination or seat allocation clause to be used as a pressuring tool on the other side.[577] Therefore, using such clauses for purposes other than what they were originally intended defeats the purpose of the contract and goes against the reasonable expectations of the parties.[578]

[574] ibid [40]-[57].
[575] ibid [28].
[576] Contractual discretions are further explored in chp 3.3.
[577] However, at present the exercise of termination rights are not made subject to any fettering, see for instance *TAQA Bratani Ltd v Rockrose UKCS8 LLC* [2020] EWHC 58 (Comm) where the court found that the right to terminate a joint operating agreement in relation to oil production blocks in the North Sea was not fettered by an obligation of good faith. The court arrived at this conclusion by adopting a literal analysis of the contract, giving the words their natural and ordinary meaning in the context of other relevant provisions and by reference to the overall purpose of the provision and the contract in that the parties were not intending to create a partnership and were entitled to act in their own interests.
[578] The concept of reasonable expectations was explored in chp 1.3.1.2.

There may be an argument to say that abuse of rights doctrine is already operative in English law, as put forward by Rowan.[579] She contends that, at least in relation to assessing the use of discretionary powers granted in contracts, that 'abuse of rights offers a better explanation.'[580] She relies on Stapleton's analysis that good faith's purpose is 'to restrain the advertent pursuit of self-interest where that would be unconscionable through being dishonest or deliberately contradictory or exploitative of dominance over another.'[581] Such an analysis restricts the applicability of good faith to instances of dishonesty or deliberate exploitation. Indeed, the abuse of rights doctrine is proposed as a limitation on the parties' freedom to use their contractual rights as they see fit. The freedom of contract would not, in that sense, extend to the parties' freedom on how they exercise those rights. Rowan argues that it is important to curtail such freedom, since the parties 'may be tempted to exploit the power and any vulnerability of the other party to their own advantage' and that it would not make commercial sense for either party to leave itself to the complete discretionary mercy of the other.[582] Considerations of the intention of the parties come into play, and this is usually resolved against a criterion of reasonable expectations.[583]

Yet there are instances where the courts recognise that, despite the lack of an intention to mislead or exploit the other party, the exercise of any discretionary rights needs to abide by a certain standard of good faith, such as in *Braganza v BP Shipping Ltd; The British Unity.*[584] And this goes beyond what an abuse of rights doctrine could achieve. The better view is to embrace abuse of rights as a component of a doctrine of good faith, or to have an abuse of rights doctrine derive from good faith. The opposite is, however, not true as good faith encapsulates much more than what an abuse of rights doctrine can ever achieve in English law. In sum, a doctrine of abuse of rights does not operate at all (or at least sufficiently enough) in English law to leave good faith administer a gap-filling role in contract performance.

Another doctrine which merits attention in this context is that of 'fraud on a power,' also known as the 'proper purpose rule.'[585] Some authors suggest that, rather than using good

[579] Rowan (n 566) 1080.
[580] ibid.
[581] ibid, citing Stapleton (n 47).
[582] ibid 1072-1073.
[583] *Medirest* (n 97) [82], [92]; *Braganza* [2015] UKSC 17 (SC), [2015] 1 WLR 1661 [1670] (Lady Hale SCJ); *Paragon Finance plc v Nash (Paragon Finance)* [2001] EWCA Civ 1466, 1 WLR 685 [36] (Dyson LJ).
[584] *Braganza* (n 583). Contractual discretions are further explored in chp 3.3.
[585] Paul S Davies, 'Excluding Good Faith and Restricting Discretion' in PS Davies, M Raczynska (eds), *Contents of Commercial Contracts – Terms Affecting Freedom* (Hart Publishing 2020) 104; Philip Sales, 'Use of Powers for Proper Purposes in Private Law' (2020) 136 Law Quarterly Review 384.

faith, whether through construction or implication, or to refer to a public law concept of *Wednesbury* unreasonableness, a better approach for private law is to rely on the equitable doctrine of 'fraud on a power' to fetter the exercise of contractual powers.[586] He explains that this long-standing doctrine 'ensures that powers are only validly exercised in pursuit of a proper purpose for which the power was granted […].'[587] He distinguishes it from requirements of good faith, positing that a power may be exercised in good faith but for an improper purpose. His justification relies on an understanding of how powers should be exercised in the context of company law.[588] Further, he contends that such a rule should not be limited to fiduciary powers, again drawing from the experience of the concept in trust law.[589] Although he concedes that the basis of the rule is unclear, but argues that it might be viewed as a rule of construction. Where the document conferring the power is silent 'as to the purposes sought', then the 'intention of the donor conferring the power' can be examined to determine the relevant proper purpose.[590] Indeed, in interpreting contracts, courts do refer to the purpose of a clause in their investigation.[591] Whilst Davies distinguishes between the narrow scope of the proper purpose rule from an inherent restriction that may be applied to all contracts to restrict the exercise of a power for a proper purpose, he does not extend it to an obligation to, for instance, act in a reasonable way.[592] Although the analysis of the proper purpose rule as discussed by Davies resembles closely to the good faith proposed herein, it is different in the following fundamental way. Good faith is understood to be the essence of the contract; therefore, it applies to all commercial contracts, it does not come into existence by way of implication, and it can form the basis of the interpretative exercise in order to reach the purpose of the clause in dispute. It forms the basis of the reasonable expectations of the parties. Therefore, where such expectations are set out ambiguously in a contract, a purposive approach to the parties' presumed intentions as rational parties should be undertaken.[593] An assessment of the exercise

[586] Davies, 'Excluding Good Faith and Restricting Discretion' (n 585) 104-105, Sales, 'Use of Powers for Proper Purposes in Private Law' (n 585) 387-388.
[587] ibid 105.
[588] ibid 106, he refers to the Australian company case of *The Bell Group Ltd (in liquidation) v Westpac Banking Corporation (No 9)* [2008] WASC 239 [4456] (Owen J) and to the distinction drawn between 's 171 (proper purpose rule) and s 172 (good faith)' of the Companies Act 2006 (fn 121).
[589] ibid 106 referring to *In Re Gulbenkian's Settlement* [1970] AC 508 and the New Zealand case of *Wong v Burt* [2005] 1 NZLR 91.
[590] ibid 107.
[591] ibid 108-110.
[592] ibid 110.
[593] Sales, 'Use of Powers for Proper Purposes in Private Law' (n 585) 395-396, Sales's approach is closely related to proposed approach herein regarding the application of good faith in the performance of contractual obligations and rights, including discretions, as he posits that contract law should not resort to the equitable doctrine of 'fraud on power.' This is because he considers that interpretation of contractual powers should be based on the parties' intention that the power be used for proper purposes, 'the ambit of which is given by what is within the

of contractual powers that distinguishes between (i) the purpose of a clause and (ii) good faith understood as the reasonable expectations of the parties as rational parties shows the limitation of the proper purpose doctrine as posited by Davies. The two elements should not be separated in the assessment of the exercise of contractual powers.

2.4. Inequality of Bargaining Power

Inequality of bargaining power is another concept which appears in the discussions of unfairness in contracts. However, it is referenced in the context of procedural unfairness rather than substantive unfairness. For instance, in *Times Travel*, the Supreme Court considered but refused to expand the doctrine of lawful economic duress based on the inequality of bargaining power.[594] Lord Hodge SCJ stated:

> [i]n any development of the doctrine of lawful act duress it will also be important to bear in mind not only that analogous remedies already exist in equity, such as the doctrines of undue influence and unconscionable bargains, but also the absence in English law of any overriding doctrine of good faith in contracting or any doctrine of imbalance of bargaining power.[595]

However, the Court emphasised that the purpose of English contract law is to protect the reasonable expectations of honest people when they enter into a contract and not to regulate the inequality of bargaining power. [596] Indeed;

> [a] commercial party in negotiation with another commercial party is entitled to use its bargaining power to obtain by negotiation contractual rights which it does not have until the contract is agreed. A powerful commercial party, such as a monopoly supplier or monopoly purchaser, can impose onerous terms, for example demanding a premium, as a condition for entering into a transaction with another party.[597]

contemplation of the parties in a broad sense, as derived from indications in the text and scheme of the contract and from the business context (…)'.
[594] *Times Travel* (n 266).
[595] ibid [3] (Lord Hodge SCJ).
[596] *Times Travel* (n 266) [26], [27] (Lord Hodge SCJ).
[597] ibid 746.

Previously, Lord Denning's judgment in *Lloyds Bank v Bundy (Bundy)* intended to create such a separate principle applicable in the context of pressures exercised by the powerful party on the vulnerable one in the context of undue influence.[598] However, no such consideration was required in the usual operation of the undue influence doctrine. The majority of the court founded their decision on the doctrine of undue influence, and Lord Denning's attempt at introducing a separate test in the context of bank and customer relations, where mortgage was obtained without independent legal advice, failed. Lord Scarman in *National Westminster Bank plc v Morgan* criticised Lord Denning's attempt, and emphasised that the curtailing of parties' contractual freedom is best left to Parliament.[599] Although these were cases dealing with pre-contractual matters, the rejection of a separate doctrine of inequality of bargaining power does not restrict the court's intervention on the grounds of equity during the performance phase of the contract.

A common thread among doctrines dealing with unfairness, as suggested by Lord Denning in *Bundy*, is undeniably an explicit or implicit reference to bargaining power. In a recent decision, the Court of Appeal, in *Dwyer (UK Franchising) Ltd v Fredbar Ltd (Dwyer)*, held the inequality of bargaining power to be a deciding factor in assessing the enforceability of a restraint of trade clause in a franchising agreement post termination.[600] As such, in assessing the reasonableness of the clause, the court considered that where the bargaining power between the parties was highly disproportionate in the franchising context, the contract was more akin to an employment contract. It was accepted in an earlier Court of Appeal Decision in *Quantum Advisory Ltd v Quantum Actuarial LLP*, that the inequality of bargaining was the gateway to the restrictive covenant doctrine in the context of commercial contracts, beyond employment and sale of business contexts as usually covered by the doctrine.[601] Indeed, '[a]bsent an inequality of bargaining power, on the facts of this case, it is very difficult to see on what basis public policy would justify engagement of the doctrine.'[602]

Overall, the arguments in favour of recognising unequal bargaining power relate to the procedural unfairness which may taint some contracts.[603] Even in the context of UCTA 1977, the strength of the bargaining position of the parties relative to each other is amongst the list of

[598] [1975] QB 326, (1974) 3 All ER 757.
[599] [1985] AC 686 (HL).
[600] [2022] EWCA Civ 889, [2023] FSR 4 [73], [77] (Sir Julian Flaux).
[601] [2021] EWCA Civ 227.
[602] ibid [85] (Carr LJ).
[603] Ewan McGaughey, 'Is Unequal Bargaining Power an Unjust Factor?' (2018) King's College London Law School Research Paper No. 2018-17 <https://ssrn.com/abstract=3200512> accessed 3 April 2025, 21.

factors to be taken into account by the court to decide if a contractual term is unreasonable.[604] Whilst the bargaining power can serve to measure the parties' contractual expectations, such an assessment is limited to examining whether consent for the contract was validly obtained.[605] Further, it may operate as a factor in the application of doctrines such as unconscionability.[606] However, as we have noted above, unconscionability also operates to correct instances of vitiated consent in contract formation.[607] In sum, inequality of bargaining power does not operate to regulate unfairness during the performance of the contract.[608] At most, where the bargaining process leads to a substantively unfair outcome during the performance of the contract, the inequality of bargaining power can then serve as a useful indicator to evaluate whether the bargaining process itself was unfair in the first place.[609] This argument posits any substantive unfairness in the resulting transaction merely as evidence of procedural unfairness. Even though the inequality of bargaining doctrine is not recognised in the context of the validity of contracts, fairness is still relevant in the assessment of the validity of contracts.[610] Therefore, substantive fairness should also be relevant during the performance of the contract. Despite the close relation between procedural and substantive unfairness, these two concepts are separate and require equal attention; this thesis is only concerned with the latter.[611]

2.5. Uberrimae Fidei of Insurance Law

Another doctrine to consider in the context of the performance of contracts is the uberrimae fidei doctrine of insurance contracts which was reformed by the enactment of the Insurance Act 2015. The Law Commission considered that maintaining a duty of utmost good faith in the new legislation, albeit in the form of a guiding principle, was important.[612] Their Explanatory Notes for the Insurance Act 2015 state that '[u]tmost good faith represents an important difference between insurance contracts and other commercial contracts.'[613] The imbalance in

[604] UCTA 1977, sch 2 (a).
[605] McGaughey, 'Is Unequal Bargaining Power an Unjust Factor?' (n 603) 21.
[606] Blake D Morant, 'The Salience of Power in the Regulation of Bargains: Procedural Unconscionability and the Importance of Context' (2006) Michigan State Law Review 925, 927.
[607] See chp 2.2.
[608] See eg McGaughey, 'Is Unequal Bargaining Power an Unjust Factor?' (n 603), or Spencer N Thal, 'The Inequality of Bargaining Power Doctrine: The Problem of Defining Contractual Unfairness' (1988) 8(1) Oxford Journal of Legal Studies 17, 33.
[609] Thal, 'The Inequality of Bargaining Power Doctrine: The Problem of Defining Contractual Unfairness' (n 608) 33.
[610] ibid 18-20.
[611] Patrick S Atiyah, 'Contract and Fair Exchange' (1985) 35 University of Toronto Law Journal 1, 6, 17, 24, argues that contract law should continue to be concerned with substantive fairness too.
[612] Law Commission, *Insurance Contract Law: Business Disclosure, Warranties, Insurers' Remedies for Fraudulent Claims, and Late Payment* (Law Com No 353, 2014) para 30.22.
[613] ibid.

access to information underlies the Law Commission's reasoning as to such distinction. For the transfer of the risk from the insured to the insurer, disclosure duties must be imposed on the insured, and this is done based on an utmost good faith duty. While the old legislation did not distinguish between pre-contractual (i.e. before the conclusion of the contract) and post-contractual (i.e. after the conclusion of the contract) duties of utmost good faith, the new legislation took the duty of disclosure outside of good faith's domain (save for interpretative purposes).[614] Post-contractual duty of good faith in insurance contracts was not initially intended by the Marine Insurance Act 1906, given the absence of authority on the point up until then. But over time, the courts extended the application of the duty into the post-contractual phase.[615]

Section 14 of the Insurance Act 2015 provides that '[a]ny rule of law permitting a party to a contract of insurance to avoid the contract on the ground that the utmost good faith has not been observed by the other party is abolished.' Moreover, pre-contractual disclosure duties based on utmost good faith under the old Marine Insurance Act 1906 were repealed by section 21(2) of the 2015 Act and replaced by a 'duty of fair presentation' at section 3, formulated on the basis of pre-1906 authority and considered to be a better terminology for the duty.[616] Moreover, fraudulent claims were divorced from breaches of post-contractual utmost good faith and were set out in section 12 of the Insurance Act 2015. With this amendment, a fraudulent claim under an insurance contract would not allow the insurer to avoid the contract retrospectively, but would give the insurer the right to forfeit the fraudulent claim, a remedy which is of a prospective nature and is independent from good faith. What remains from the previous utmost duty of good faith is unclear. Not only are post-contractual applications not prohibited by the Insurance Act 2015 but also no discernible remedy has been provided for any such breach therein.

It may be argued that insurance contracts should never have been classified as uberrimae fidae contracts in the first place, as the duty of disclosure which arises out of insurance law does not arise due to the nature of the contract itself. Insurance contracts are commercial

[614] ibid, para 30.23.
[615] Rob Merkin and Özlem Gürses, 'The Insurance Act 2015: Rebalancing the Interests of Insurer and Assured' (2015) 78 MLR 1004, 1007, citing *Black King Shipping Corp v Massie (The Litsion Pride)* [1985] 1 Lloyd's Rep 437; *K/S-Merc Scandia XXXXII v Lloyd's Underwriters (The Mercandian Continent)* [2001] 2 Lloyd's Rep 563; *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] UKHL 1, [2003] 1 AC 469 [57].
[616] Merkin and Gürses (n 615) 1007.

contracts, at least those taken out by parties in the course of their business.[617] When defining the parameters of commercial law, Goode, as mentioned above, includes insurance in commercial law.[618] Whilst there may be an argument to say that insurance contract law should no longer be viewed as a sub-set of commercial contract law due to the size of the insurance market and the variety of issues it tackles, it continues to provide 'interesting questions of general importance to contract law (...).'[619] The importance of the insured's duty of disclosure for the development of the insurance industry is undeniable. It may be argued that the effect of the Insurance Act 2015 was to disprove insurance contracts as good faith contracts, despite the lack of such qualification for any other type of commercial contract, to justify the creation of a duty of disclosure. The sentiment is echoed in the doctrine:

> [w]e have over time, it seems, become distracted by the labelling 'good faith' and 'utmost good faith', neither of which serves as the rationale for the law's requirement of mutual disclosure in the insurance setting; rather 'utmost good faith' is made manifest in the context of insurance by the expectation of mutual disclosure prior to contract formation and to this extent it is qualitatively distinct from 'good faith' insofar as that is an acknowledged presence in contracts more generally.[620]

As such, honesty norms expressed through good faith can expand beyond the limits of insurance law, and would not require any special treatment in the insurance context, since there is 'no firm basis for concluding that the content of the 'good faith' is markedly different in the insurance setting than in many other commercial relationships; in this respect, at least, insurance contracts are far from unique.'[621] Indeed, in a recent case, the High Court applied *Braganza* in the insurance context to find that an insurer had acted irrationally in concluding that misrepresentations made by the insured were fraudulent.[622] Consequently, it is not unreasonable to think that insurance disputes might continue to apply non-insurance decisions

[617] Consumer insurance falls outside the scope of this analysis and is governed by the provisions of the Consumer Insurance (Disclosure and Representations) Act 2012.
[618] See text to n 146 above.
[619] James Davey, 'The Shape of Insurance Contract Law' in J Burling, K Lazarus (eds), *Research Handbook on International Insurance Law and Regulation* (2nd edn, Edward Elgar Publishing 2023), 22.
[620] Margaret C Hemsworth, 'The Fate of 'Good Faith' in Insurance Contracts' (2018) 1 LMCLQ 143, 153.
[621] ibid.
[622] *UK Acorn Finance Limited v Markel (UK) Limited* [2020] EWHC 922 (Comm), [2020] 1 CLC 632 [63] (Mark Pelling QC). Another similar example is the Court of Appeal decision in *Equitas Insurance Ltd v Municipal Mutual Insurance Ltd* [2019] EWCA Civ 718, [2020] QB 418 [111] (Males LJ), [162] (Leggatt LJ) where the court implied a good faith duty, to respect the reasonable expectations of the parties, so that the insurers' rights to present a reinsurance claim had to be exercised in a matter which was not arbitrary, irrational or capricious.

in the future, and that post-contractual good faith in insurance disputes might be informed by the developments of non-insurance commercial disputes.

It can be said that the dissociation of a pre-contractual duty of disclosure from a post-contractual duty of good faith aligned insurance law with the rest of commercial contract law. It is then questionable why insurance contracts should continue to be classified as uberrimae fidei contracts since the only reason for such qualification was the imbalance of information, and this has been remedied by the creation of a duty of fair presentation. Parallels with other types of uberrimae fidei contracts are not helpful, as there is doubt as to whether such categorisation should exist in the first place.[623] Viewing insurance contracts as a subset of commercial contracts that require cooperative engagement by both parties would be a more pragmatic way of furthering the development of a good faith principle in commercial contracts in general.[624] Nevertheless, Macdonald Eggers and Picken argue that 'the imbalance of information accessible to the underwriter and the assured respectively, in all probability still justifies the classification of the insurance contract as one requiring the utmost good faith.'[625]

Yet there is scepticism as to the applications of post-contractual good faith in the insurance context.[626] These were already problematic under the old statute. In the context of post-contractual fraudulent claims, viewing such claims as operating outside the scope of a good faith duty would offer 'no deterrence to a putative fraudster who considers making a claim that is entirely fraudulent, since the fraudster is merely precluded from recovering claim proceeds to which he is not in any event entitled.'[627] In that case, only the fraudulent claim may be forfeited, and the contract would stay intact. Whereas if the post-contractual fraudulent claim were to be seen as a breach of a duty of good faith, rather than arising under common law fraudulent misrepresentation, such breach would give the insurer the possibility to avoid the whole contract, not merely reject the payment for the specific fraudulent claim. The preference is therefore to hold onto good faith in insurance contracts despite the uncertainty surrounding

[623] Hugh Beale (ed), *Chitty on Contracts* (31st edn, Sweet & Maxwell 2012) 6–150, enumerates contracts for the sale of land, contracts or suretyship, and partnership among others as examples of uberrimae fidei contracts but casts doubt on whether such categorisation should exist since these are not uberrimae fidei contracts in the strict sense as they do not involve extensive duties of disclosure. Similarly, Peter Macdonald Eggers and Simon Picken, *Good Faith and Insurance Contracts* (Informa Law From Routledge 2018) 10, state that contracts other than insurance contracts, whether uberrimae fidei or not, which require full disclosure, 'do not normally demand disclosure of matters which go beyond the fabric of the contract itself, that is, the expected basis and function of the contract. Insurance contracts are more demanding.'
[624] Soyer and Tettenborn (n 129) 635. The concept of relational contract is discussed in chp 3.2.3.1.1.
[625] Macdonald Eggers and Picken (n 623) 11.
[626] ibid.
[627] ibid, preface xxviii.

its post-contractual applications. This is because the imbalance in the parties' knowledge is not limited to the pre-contractual phase but also arises when a claim is presented to the insurer. Indeed, there is a distinction between the duty of disclosure pre-contractually and post-contractually. Lord Hobhouse's statement in *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* remains accurate:

> [i]t is not right to reason, (...) from the existence of an extensive duty pre-contract positively to disclose all material facts to the conclusion that post-contract there is a similarly extensive obligation to disclose all facts which the insurer has an interest in knowing and which might affect his conduct. The courts have consistently set their face against allowing the assured's duty of good faith to be used by the insurer as an instrument for enabling the insurer himself to act in bad faith.[628]

The duty of good faith may serve to deter fraud and correct the imbalance in the parties' knowledge both before and after entry into the contract.[629] However, the lack of a remedy for breach of post-contractual duty of disclosure in the Insurance Act 2015 points to a Parliamentary unwillingness in having an operative post-contractual good faith in insurance law, similar to the approach taken in regards to other commercial contracts.[630] It is unlikely that good faith will find any further application in the context of the Insurance Act 2015 save as an interpretative tool. Indeed, the Law Commission maintained it as an 'interpretative principle' stating that:

> (...) this concept should continue to inform the approach of the courts in this field. The further advantage to retaining this as an interpretative principle is that resort may continue to be had to the substantial and well-developed jurisprudence on the subject.[631]

Further, the Law Commission explained that maintaining such a principle was useful as it would play a role in three scenarios.[632] First, it was suggested that it would help interpret the duty of fair presentation. Yet it is doubtful that good faith can inform the relevancy of information that should have been disclosed. Second, it was hoped that it would help assess whether to imply terms under the traditional business efficacy test. However, the courts have

[628] *The Star Sea* (n 615) [57].
[629] Macdonald Eggers and Picken (n 623) preface xxix.
[630] Macdonald Eggers and Picken, (n 623) 9.
[631] Law Commission *Insurance Contract Law: Business Disclosure, Warranties, Insurers' Remedies for Fraudulent Claims, and Late Payment* (n 612), citing the Faculty of Advocates, para 30.22.
[632] Law Commission *Insurance Contract Law: Business Disclosure, Warranties, Insurers' Remedies for Fraudulent Claims, and Late Payment* (n 612) para 30.23.

been using the business efficacy test without any need for a good faith component. The questioning of the courts concerns whether the contract would make commercial sense without the term being implied. The Law Commission is attempting to make good faith a component of the business efficacy test in interpreting insurance contracts by attempting to find a middle ground between the 'reluctance of the courts to allow avoidance for breach of good faith with their desire to see that the contract is performed in good faith.'[633] Therefore, it is not clear how good faith would inform the implication in fact of a term into the contract based on necessity. Existing principles on the interpretation of contractual terms already cater for the first two suggested roles that good faith could continue to play in insurance law.[634] The third suggestion was that it would provide flexibility in the judicial decision-making process to correct any manifest unfairness.[635]

Such a proposition posits good faith in insurance law as a substantive legal principle.[636] Consequently, there would not be a need to develop two separate good faith doctrines, one for post-contractual insurance contracts and the other for ordinary commercial contracts. The separation would be a futile exercise, as the considerations applicable to insurance contracts would no doubt be relevant for other commercial contracts too. For instance, exercise of rights would be subject to the requirement that they are not exercised capriciously or arbitrarily, and this would of course emanate from contractual rules in respect of discretions and be similarly applicable to insurance cases.[637] In referring to non-insurance cases where the courts have implied on the decision-maker a duty not to assert their discretionary right in an arbitrary or capricious way, Soyer submits that such decisions will also be relevant for insurance contracts too but that the specifics of the contract in question will determine the scope of the implied term.[638] Similarly a duty to correct mistakes would not be needed, for instance an incorrect information provided to the insurer, where the insurer knew of the mistake, would likely preclude the insurer from denying a claim on the basis of doctrines of estoppel or mistake.[639]

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[633] ibid para 30.59.
[634] Soyer and Tettenborn (n 129) 622.
[635] Law Commission *Insurance Contract Law: Business Disclosure, Warranties, Insurers' Remedies for Fraudulent Claims, and Late Payment* (n 612), para 30.23.
[636] Soyer and Tettenborn (n 129) 624, enumerates examples of instances where good faith duties continue to arise post-contractually, such as in connection with the insurer's right to take over and control legal proceedings against the insured.
[637] Soyer and Tettenborn (n 129) 624. See discussion on contractual discretions in chp 3.3. This is exemplified in the recent cases of *UK Acorn Finance Limited* (n 622) and *Equitas* (n 622).
[638] Baris Soyer, 'The Insurer's Duty of Good Faith: is the Path Now Clear for Introduction of New Remedies?' in M Clarke and B Soyer (eds), *The Insurance Act 2015- A New Regime for Commercial and Marine Insurance Law* (Informa Law by Routledge 2017) 47.
[639] ibid 626-627.

In sum, the insurance law reform has implications beyond the scope of insurance contracts. Any development affecting post-contractual good faith in insurance contracts has the potential to also affect other types of commercial contracts due to the dissociation of pre-contractual duty of disclosure from the post-contractual good faith duties, the scope of which is still debated.

2.6. Conclusion

In the post-contractual phase, the 'functional equivalence' approach does not appear to regulate the fairness in contract performance.[640] Unconscionability is confined to issues tainting the contracting process, whereas abuse of power and inequality of bargaining power are not independently operating doctrines. Overall, these doctrines intend to 'correct a failure of contract.'[641] The doctrine of estoppel may be of limited assistance to an aggrieved party, as it is of inconsistent application depending on its type and rationale. Moreover, the reform of the uberrimae fidei doctrine in insurance law signifies a shift towards aligning insurance contracts with general commercial contract principles, and might signal a green light for transposing insurance law's good faith into other commercial contracts. These insights suggest that while the 'piecemeal solutions' to unfairness in contracts largely deal with contract formation issues, the development of a more unified and comprehensive approach is also required in the context of the performance of contracts.[642] This would be possible by adopting an overarching good faith principle as envisaged herein, which goes beyond protecting the reasonable expectations of honest contracting parties, but also protects the institution of contracting.[643] The next chapter will explore the extent to which good faith has found acceptance in the case law by way of an implied term.

[640] See text to n 269 above.
[641] Brooks (n 3) 506.
[642] The term 'piecemeal solutions' refer to the statement made by Bingham LJ in *Interfoto* (n 100).
[643] See text to n 270, 295 above.

CHAPTER 3: GOOD FAITH AS AN IMPLIED TERM

3.1. Introduction

There is a growing number of case law which tackles issues of implied good faith duties.[644] However, the reluctance of the courts to enunciate the breadth of the concept is not helped by the limited number of scenarios in which good faith is raised in court.[645] Although the courts' primary function is to resolve disputes rather than to set out a theoretical analysis, the cases on the implication of terms present an opportunity to concretise the practical applications of such a legal principle.[646] The use of traditional methods of implied terms or contract interpretation is the primary way in which courts prefer to tackle good faith in practice.[647]

In the context of implied terms, the distinction between implication in fact or in law has implications for how much expansion good faith is allowed into contracts as a general principle.[648] Similarly, in contract interpretation, the distinction between the traditional literal method of interpreting contracts, and that of a contextual one, necessarily raises questions as to good faith's place in contract law.[649] At times, the lines between interpretation and implication can seem blurred, but there is a clear preference in judicial decisions to keep each methodology separate.[650]

Although the underlying rationale for a good faith principle should be to provide for an efficient legal default standard in contract performance, this efficiency must be balanced by considerations of fairness, ensuring conformity to the parties' reasonable expectations as

[644] Following Yam Seng (n 3), many more decisions followed on the topic of good faith such as *Al Nehayan* (n 48), *UTB LLC v Sheffield United Ltd* [2019] EWHC 2322 (Ch), *Globe Motors, Inc (a corporation incorporated in Delaware, USA) v TRW LucasVarity Electric Steering Ltd* [2016] EWCA Civ 396, [2016] 1 CLC 712, *Russell v Cartwright* [2020] EWHC 41 (Ch), *Cathay Pacific Airways Ltd v Lufthansa Technik AG* [2020] EWHC 1789 (Ch)

[645] Philippa Hopkins, 'Commercial Contracts, Individual Terms and Good Faith: Where Do We Go From Here?' (2021) 3 Journal of Business Law 219, 219, states that in many of the disputes where good faith is raised, the dispute relates to the exercise of its contractual discretion or the exercise of its rights.

[646] On the need to concretise principles, see text to n 250-251.

[647] Contractual interpretation is discussed in chp 4 below.

[648] Indeed, the possibility of implying good faith in law was only explicitly made by Leggatt LJ in *Al Nehayan* (n 48).

[649] See chp 4 discussing good faith as an interpretative tool.

[650] See n 894 below.

honest people.[651] The difficulty is of course that the courts struggle to determine the presumed intentions of the parties, let alone their actual intentions, but must yet adjudicate the case based on norms governing contract law, freedom of contract being the preferred norm on which to anchor decisions as a result of a traditional approach to contract law.[652]

This chapter seeks to demonstrate that the use of implied terms restricts the development of a principle of good faith. Moreover, its development will be further restricted if its use is confined to the development of relational contracts as mentioned in *Yam Seng*.[653] The uncertainty surrounding what constitutes a relational contract has not been resolved to date.[654] An alternative categorisation of contracts where good faith can be more easily recognised is revenue generating and sharing contracts.[655] When an incremental adoption of good faith as a general principle in a specific category of commercial contracts is accepted, fewer steps will then be required to adopt it in the remainder of commercial contracts.[656] In this context, the debate of good faith can learn from the evolution of the doctrine of frustration.

Chapters 3.2.1 and 3.2.2 will provide an overview of the methods of implying terms in fact and in law. Chapter 3.2.3 will discuss how good faith is implied in contract performance. It will also provide a criticism of relational contracts, and will propose the alternative of revenue generating and sharing contracts. Chapter 3.3 will address the role of good faith in contractual discretion cases. Chapter 3.4 will conclude the chapter.

3.2. Implied Terms

The courts are obliged to determine the intention of the parties where the contract has not provided for the matter at hand adequately.[657] This does not mean that the Courts can make

[651] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 458; normative considerations are relevant, beside the respect for parties' autonomy, which is not a new approach in English law. For instance, rules regarding economic duress, undue influence or fraud can be justified beyond the respect for party autonomy, and viewed as prevention of the abuse of freedom to exercise contractual powers; similarly, the duty to mitigate liability for loss is informed by a conception of fairness. Also see chp 1.2.1 on the need for efficiency of default standards.
[652] ibid 456, '[u]pholding the intentions of the parties and freedom of contract have been presented as the defining philosophy of the English common law of contract for upwards of 150 years.'
[653] *Yam Seng* (n 3). Also see chp 3.2.3.1.1.
[654] Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (n 281) 553.
[655] See chp 3.2.3.1.2.
[656] Chen-Wishart and Dixon, 'Good Faith in English Contract Law: A Humble '3 by 4' Approach' (n 205) 192, provide the example of the 'familiar neighbour principle in negligence law' as an example to the incrementalism which is preferred by the common law.
[657] Gerard McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (3rd edn, Oxford University Press 2017) 29.

up the contract; to the contrary, they are bound by an objective ascertainment of the parties' intentions.[658] Implied term is considered itself to be a distinct legal doctrine.[659] The primary function of the process of implication is gap-filling.[660] The identification of the gap is crucial. There may be different types of gaps in a contract. First, the parties may have completely forgotten to consider the issue.[661] Second, the parties may have considered the issue but did not provide an express term, mistakenly believing that the contract already adequately addressed the issue.[662] Third, the parties may have considered the issue and decided not to draft any term to that effect because they could not agree.[663] The third scenario is clearly unsuited for the use of an implied term; the parties' actual intention was not to provide for a term, therefore the court cannot intervene to make the contract for the parties. The second scenario is best catered to by the process of rectification rather than implication.[664] This is because the process of interpretation is an objective ascertainment of the parties' actual, not presumed intentions. However, where the actual intention cannot be determined, the court may have recourse to the 'presumed common intention' of the parties and decide that the issue can be dealt with by the contract's existing clauses, or that there is no agreement on the issue.[665] As such, if there was any disparity between the parties' agreement and the instrument of contract, a party can benefit from the equitable remedy of rectification.[666] Another relevant remedy is that of estoppel by convention, which would also depart from an objective assessment of the parties' intentions and consider evidence of a common subjective understanding.[667] The only type of gap suitable

[658] ibid. Also in *Marks and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd and another* [2015] UKSC 72; [2016] AC 742 [72] (Lord Neuberger SCJ) the court emphasised the objective interpretation of the parties' intention by referring to 'a notional reasonable people in the position of the parties at the time at which they were contracting.'

[659] Andrew Phang, 'The Challenge of Principled Gap-Filling: A Study of Implied Terms in Comparative Context' (2014) 4 Journal of Business Law 263, the author argues that the doctrine also has a theoretical function to justify the doctrine of frustration.

[660] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 18.

[661] Phang (n 659) 265.

[662] ibid.

[663] ibid. If the contract is silent on a point, the most natural conclusion is that the loss should simply lie where it falls, Paul S Davies, Philip Sales, 'Controlling Contract Discretions: Wednesbury Reasonableness, Good Faith and Proper Purposes' (2024) 140 LQR 106, 117.

[664] ibid. Also see McMeel *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 18-19.

[665] McMeel *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 158. This type of intention (i.e. where the parties probably actually held but did not bother to express) is sometimes referred to as 'presumed actual intentions.' In contrast, where the parties have not considered the issue, 'hypothetical intentions' refer to those that the parties would probably have agreed to had they considered the issue. However, it would be difficult to reliably distinguish between both, see Jeannie M Paterson, 'Terms Implied in Fact: The Basis for Implication' (1998) 13(2) Journal of Contract Law 103, <https://search.informit.org/doi/10.3316/agispt.19984288> accessed 3 April 2025, 4-5.

[666] McMeel *McMeel On the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 529.

[667] ibid 140.

to be filled by implying a term is therefore the first scenario. The reason being that 'the implication of terms is so potentially intrusive that the law imposes strict constraints on the exercise of this extraordinary power.'[668]

Terms can be implied by statute, by custom, by previous course of dealing or at common law.[669] Only the common law rules are relevant for the implication of good faith into English contracts. This is because there is no relevant statutory implied term of good faith applicable to all contracts.[670] Where terms are implied by custom, the custom itself would have to be certain, notorious, established as having binding effect and reasonable.[671] A custom can potentially be converted into a term to be implied in law over time. However, customs do not lend themselves to applications beyond their distinctive industry and are relatively rare. It is considered that, in most cases, a custom can serve as a tool to interpret the contract, as part of the background available to a reasonable person.[672] Therefore the development of good faith by way of a custom would be very restrictive and unsatisfactory. Alternatively, good faith can be developed through implied terms however this also presents its own challenges. First, we shall explore how terms are implied into contracts.

3.2.1. Terms Implied in Fact

The aim of an implication in fact is considered to be 'a precise surgical operation to revise the allocation of risk in the context of a particular transaction.'[673] The courts use the tests of officious bystander and business efficacy to imply terms in fact. The business efficacy test was set out by Bowen LJ in *The Moorcock*.[674] The defendants owned a wharf and a jetty, and they contracted with a shipowner to dock the ship and unload cargo on the wharf. The ship was damaged at the ebb of the tide due to the uneven nature of the ground. It was held that there was an implied undertaking by the defendants that they had to take reasonable care to ascertain that the bottom of the river at the jetty was not going to cause damage to the ship.[675] The court set the standard for business efficacy to be a low one for 'honest business.'[676] Esher LJ posited

[668] *Socimer* (n 156) [105] (Rix LJ).
[669] Phang (n 659) 265.
[670] UCTA 1977 regulates unfairness in B2B contracts subjecting terms to a reasonableness criterion however, it is restricted in its scope of application. Moreover, good faith as envisaged herein is more expansive than the concept of reasonableness as discussed in chp 1.
[671] As set out in *Cunliffe-Owen v Teather & Greenwood* [1967] 3 All ER 561, 1 WLR 1421.
[672] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 303; Edward Peel, *Treitel on the Law of Contract* (15th edn, Sweet & Maxwell 2020) 6-029.
[673] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 303.
[674] (1889) 14 PD 64 (CA).
[675] ibid 68 (Esher LJ), 71 (Bowen LJ).
[676] ibid 67 (Esher LJ).

the duty to be implied to be 'the least onerous duty which can be implied' and without having to determine 'the whole of the duty'.[677] What is the least onerous duty is gauged as one being determined against a reasonableness criteria. The wharfingers should have taken 'reasonable care to find out the bottom of the river was reasonably fit' for the intended purpose.[678] Similarly, Bowen LJ also questions the 'minimum of efficacy' which has to be expected of the contract.[679] The emphasis is on reason as 'it may well be said that the law will not imply that the persons who have not the control of the place have taken reasonable care to make it good, but it does not follow that they are relieved from all responsibility.' Indeed, the learned judge noted that the inferences to be drawn from the circumstances of the case must be those that are reasonable to draw from the nature of the transaction.[680] Regardless of the references to reasonableness, the test laid out is one of necessity. The necessity relates to the 'necessity for the business efficacy of *the contract*; not some wider business purpose of a contracting party.'[681]

The officious bystander test was devised in *Shirlaw v Southern Foundries (1926) Ltd*.[682] Southern Foundries appointed Shirlaw as its managing director for a term of ten years. The defendant's articles were amended when Federated Foundries took over all of Southern Foundries' shares and abrogated the old articles of association and adopted new ones, giving the power to the defendants to remove the claimant before the end of the ten years. Shirlaw sued both companies, Southern Foundries for wrongful repudiation, and Federated Foundries for wrongly procuring, causing or inducing the company's breach of the agreement. The House of Lords held that it was an implied term of the contract that the defendants should not remove the claimant as a director before the end of the ten years, thereby upholding the Court of Appeal's decision.[683] The most famously referenced passage is that of Mackinnon LJ:

> [p]rima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some

[677] ibid.
[678] ibid.
[679] ibid 69 (Bowen LJ).
[680] ibid 70.
[681] *Kason Kek-Gardner Ltd v Process Components Ltd* [2017] EWCA Civ 2132 [55].
[682] *Southern Foundries (1926) Ltd v Shirlaw* [1939] 2 KB 206 (CA).
[683] [1940] AC 701 (HL).

> express provision for it in their agreement, they would testily suppress him with a common 'Oh, of course!'[684]

Whether Mackinnon LJ intended to replace or to expand the business efficacy test is not clear, as he posited the officious bystander one as being 'at least as useful' as the business efficacy test.[685]

In a leading Privy Council case, *BP Refinery (Westernport) Pty Ltd v Shire of Hastings*, Lord Simon succinctly summarised and combined both tests as follows:

> for a term to be implied, the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that 'it goes without saying'; (4) it must be capable of close expression; (5) it must not contradict any express term of the contract.[686]

Lord Simon's unification of both tests was later used by Lord Hoffmann to conceive the implication of terms as part of the construction process of a contract in *Attorney General of Belize v Belize Telecom Ltd*.[687] This was indeed a departure from the traditional tests. Precisely, he posited that the most crucial question in uncovering the intention of the parties is to ask 'what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?'[688] He warned that

> diverting attention from the objectivity which informs the whole process of construction into speculation about what the actual parties to the contract or authors (or supposed authors) of the instrument would have thought about the proposed implication.[689]

Lord Hoffmann's view was that the traditional tests were merely different ways of expressing the only question, which relied on the viewpoint of the reasonable person. As such, he posited implication as a process of interpretation; 'the implication of the term is not an

[684] *Southern Foundries* (CA) (n 693) 227.
[685] ibid.
[686] *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1978) ALJR 20, 26.
[687] [2009] UKPC 10, [2009] 1 WLR 1988.
[688] ibid [21] (Lord Hoffmann).
[689] ibid [25] (Lord Hoffmann).

addition to the instrument. It only spells out what the instrument means.'[690] Consequently, the court's duty is to elucidate the intention of the parties, and not substitute its own intention. The process can be criticised as being a work of fiction.[691] Nonetheless, the court is limited in its assessment to the objective evidence before it to ascertain the presumed intentions of the parties had they been aware of the issue concerned. As such, the intention of the parties to be ascertained is presumed, not actual or subjective.[692]

It was later clarified by the Court of Appeal in *Mediterranean Salvage & Towage Ltd v Seamar Trading & Commerce Inc (The Reborn)* that to imply a term, it must be necessary to imply it, not merely reasonable.[693] The Supreme Court also discredited Lord Hoffmann's approach to implication and affirmed the application of the traditional tests based on necessity in *Marks and Spencer*.[694] Lord Neuberger SCJ stated that the necessity must relate to a business necessity, but it was not an absolute one. The court must therefore ask whether the contract would 'lack commercial or practical coherence' or whether it is necessary to 'make the contract work.'[695] Whether one test or the other is preferred, usually the outcome will be the same due to the courts' insistence on the necessity element. It may be suggested that, indeed, both tests are complementary.[696] Reasonableness and fairness are held not to be sufficient considerations by themselves in implying terms.[697] Lord Neuberger SCJ further states that Lord Simon's first requirement of reasonableness and equitableness usually, if ever, does not add much to the necessity element.[698] He argues that where necessity is not satisfied, it would be unlikely to be reasonable and equitable to imply the term. It is suggested that this is because the necessity implies a reasonable standard by design. And the reasonableness, in implying a term, is

[690] ibid [18] (Lord Hoffmann). This approach does not correspond to the stance earlier taken by the courts in distinguishing the processes of implication and interpretation, see for instance in *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408 (HL) 458, Lord Steyn said it was 'necessary to distinguish between the processes of interpretation and implication.' For criticism of the approach, also see Phang (n 659) 279, where the author considers that implication should not be artificially forced into the confines of interpretation, thereby discarding the subjective intentions of the parties in favour of those of the reasonable observer.
[691] Paterson, 'Terms Implied in Fact: The Basis for Implication' (n 665) 7.
[692] Phang (n 659) 282, does not agree that the process of ascertaining the presumed intention of the parties is a legal fiction; rather, the court sifts through the 'objective evidence before it,' fully cognizant that it is not to 're-write the contract for the contracting parties.'
[693] [2009] EWCA Civ 531, [2009] 1 CLC 909 [916] (Clarke LJ).
[694] *Marks and Spencer* (n 658).
[695] ibid [21] (Lord Neuberger SCJ), [77] (Lord Clarke SCJ).
[696] See Phang (n 659) 289-291, the author argues that the officious bystander test is the practical mode by which the business efficacy test is implemented. To determine what is necessary to achieve business efficacy in a contract, first one must determine the parties' presumed intention, which can be done through the application of the officious bystander test. As such, the business efficacy test assists in the identification of the gap, whereas the officious bystander test assists in the filling the gap by providing a substantive response.
[697] Martin A Hogg, 'The Implication of Terms-in-Fact: Good Faith, Contextualism, and Interpretation' (2017) 85 George Washington Law Review 1660, 1673.
[698] *Marks and Spencer* (n 658) [21] (Lord Neuberger SCJ).

assessed from the viewpoint of 'notional reasonable people in the position of the parties' at the time of contracting.[699] However, he does qualify the necessity test to be a fair one.[700] The point is further emphasised in the conclusions where he states that 'not merely would an implied term be fair, but that clause 8 could be said to work rather unfairly without the implied term.'[701] *Yam Seng*, although not revolutionary in its application of the law, has shown that the fairness considerations can and should figure alongside contract law's loyalty to freedom of contract, thereby providing an alternative lens through which to view contracts.[702]

3.2.2. Terms Implied in Law

Where a term is implied in law, is it implied as a matter of public policy?[703] The primary concern is not to give effect to the parties' presumed intentions. Implied terms in law are prevalent in contracts with bargaining power asymmetry, such as in employment contracts.[704] For example, an employer cannot 'without reasonable and proper cause conduct [himself] in a manner calculated or likely to destroy or seriously damage the relationship of confidence and trust between the parties.'[705] They can also be found in commercial contexts, such as in construction contracts.[706] The courts do not use the officious bystander or the business efficacy test to imply a term in law. Rather, they rely on one which is based on the nature of the relationship of the parties and whether it is necessary to imply such a term of the particular type in question. Indeed, 'wider considerations' need to be taken into account compared to the classic tests based on necessity.[707] In doing so, the court must focus on 'reasonableness, fairness and the balancing of competing policy considerations.'[708]

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[699] ibid.
[700] For the discussion on the concept of fairness, see chp 1.3.1.1 above.
[701] *Marks and Spencer* (n 658) [49] (Lord Neuberger SCJ). Also see Paterson, 'Terms Implied in Fact: The Basis for Implication' (n 665), 17-18 who argues that the legal basis for implication of terms would better serve the requirements of certainty in contract law if it were premised on presumed intent and business efficacy rather than on one of generalised moral standards of fairness or reasonableness.
[702] *Yam Seng* (n 3). Atiyah, 'Contract and Fair Exchange' (n 611) 3 submits that 'law of contract is today greatly concerned with substantive fairness of exchange (...).'
[703] McMeel *McMeel On the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 338.
[704] For instance, in the context of employment, see *Scally v Southern Health and Social Services Board* [1992] 1 AC 294 (HL) where the court implied a term in law and held that the employer should inform the employee of the right to purchase further pension years. In *Malik* (n 46) 45 (Lord Steyn), the court further implied a term in law of mutual trust and confidence into an employment contract and posited such rules as operating as 'default.'
[705] *Malik* (n 46) 44–45 (Lord Steyn).
[706] See for instance *Young & Marten Ltd v McManus Childs Ltd* [1969] 1 AC 454 (HL), [1968] 3 WLR 630 where the court found that contractors must carry out work with all proper skill and care, and materials should be reasonably fit for purpose and of satisfactory quality.
[707] *Scally* (n 704) 306 (Lord Bridge).
[708] *Crossley v Faithful & Gould Holdings* [2004] EWCA Civ 293, [2004] ICR 1615 [36] (Dyson LJ), it was held that there were no obvious policy considerations to impose on employers a general duty to protect their employees'

It is generally understood that the criteria for necessity is not a strict one, but one of reasonable necessity, where, without the term, the contract, viewed as a whole, would be unreasonable, which does not mean that any reasonable term may or should be implied.[709] As such the reasonableness, when implying a term in law, needs to be gauged not just within the context of the parties' relationship but within a wider context of parties entering into contracts of the type in question.[710] Moreover, the necessity required for implication in law is different from that in fact. The House of Lords has indicated that there is a distinction between 'the search for an implied term necessary to give business efficacy to a particular contract and the search, based on wider considerations, for a term which the law will imply as a necessary incident of a definable category of contractual relationship.'[711] The implication in law does not make it necessary to imply the term to give business efficacy to the individual contract, but instead it will be based on policy considerations related to that particular category of contracts. Peden proposes that the courts' public policy considerations should focus on various factors beyond the standard of necessity, as this may be hard to gauge. She enumerates these to be customary practices in the trade; the relationship with (other) obligations imposed by law, derived from statute and the law of tort; the question of which party is best able to bear the loss or insure against the risk; the parties' respective bargaining positions and relative size; the size of the burden imposed by parties likely to be subject to the proposed standard incident; and questions of consistency with general principles, the impact on wider society, and fairness.[712]

The main difference with terms implied in fact is that terms implied in law have the force of precedent for contracts of the same category. The transition from a term implied in fact to one implied in law is not easy, and 'requires significant reorientation in legal reasoning.'[713] Until then, the precedents for terms implied in fact provide 'an unreliable source of a general default rule.'[714] It may further be said that terms implied in law can act as a precursor to terms implied by statute, where these are enacted into legislative instruments by

economic wellbeing. However, in an earlier decision, in *Liverpool City Council v Irwin* [1977] AC 239, 253-254, Lord Wilberforce sitting in the House of Lords, had rejected Lord Denning MR's argument in the Court of Appeal of implication of reasonable terms. The House of Lords laid a necessity test and implied in law a term into a tenancy contract that the landlord should use reasonable care to keep the common parts of a block of flats in reasonable repair.

[709] Richard Austen-Baker, *Implied Terms in English Contract Law* (3rd edn, Elgar Commercial Law and Practice series 2023) 44.

[710] ibid 45.

[711] *Scally* (n 704) 307.

[712] Elisabeth Peden, 'Policy Concerns Behind Implication of Terms in Law' (2001) 117 LQR 459, 467-75.

[713] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 303.

[714] ibid.

the legislative power. Another difference relates to the 'burden of expression.'[715] Where an implication in law is envisaged, the presumption is that the contract of the specified type is presumed to include any implied term in law, unless expressly excluded. Conversely, where an implication is in fact, the presumption is, where the contract is detailed, that the contract is complete, and the terms fully express the parties' agreement.[716] As such, if the contract is silent on a matter, then the presumption is that there is no term to be implied in fact, but a term can be implied in law if the contract is of a certain type. Collins sets out four possible scenarios to demonstrate the approach taken by the courts when deciding between a term implied in fact or in law.[717] He argues that rather than asking the court to take on a legislative role which they do not easily embrace, and when they do, they do so by having recourse to strict tests of necessity, and it is better 'to disguise the measure by hiding behind precedents and to claim merely to be applying a well-established implied term for this class of contracts.'[718] As such, it is the 'political and policy-motivated denials of the powers involved in creating implied terms' which create confusion in distinguishing and applying the two types of implication methods.[719]

The Supreme Court recently had the opportunity to review the implication of terms in law in *Barton,* demonstrating the ongoing clash in the judiciary over a classical view of contracts and a more modern one.[720] The claimant was seeking to buy a high-value property owned by Foxpace Limited ('Foxpace') in 2012. The claimant attempted the purchase twice, failing to complete due to a lack of necessary financial resources. However, the claimant had expended £1.2 million deposits on the failed transactions, which were forfeited to Foxpace. To recover his loss, it was orally agreed that Foxpace would pay Barton the total amount of his loss, namely £1.2 million, if he introduced a buyer for the property and the property sold to that buyer for £6.5 million. The express term of the oral agreement was later determined by the trial judge at first instance, and this point was not appealed. The claimant found a potential buyer in 2013, Western UK (Acton) Limited ('Western') and the sale documents were drafted with the £6.5 million price tag. However, a reduced price of £6 million was later agreed between Foxpace and Western, due to the construction of HS2 potentially affecting the value of the property. The claimant was not paid a fee as the property was not sold for £6.5 million. He brought a claim for reasonable remuneration (namely a contractual quantum meruit) based on

[715] *Barton* (n 486) [732] (Lord Leggatt SCJ).
[716] ibid.
[717] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 309.
[718] ibid.
[719] ibid 307.
[720] *Barton* (n 486).

an implied term to this effect, whereas the defendant argued that they were under no obligation to pay anything. The majority judgment was handed down by Lady Rose SCJ (with whom Lord Briggs and Lord Stephens SCJJ agreed) and it was held that there was no implied term in regards to a reasonable remuneration. It was evident that there was no express term to that effect in the contract, the alternative being an implied term. Applying the conventional tests of implication of terms in fact, the court found that a reasonable remuneration term could not be implied. First, the 'business efficacy' test requires that the least onerous term must be implied to give effect to the parties' contract efficacy. Accordingly, a term could be implied that the defendant does not deliberately reduce the selling price, but that does not mean it is necessary to imply a reasonable remuneration term to make the contract efficient. Second, looking at the context of the transaction, the court considered that the fee of £1.2 million was more than reasonable remuneration for the claimant's introduction, rather the deal was envisaged as a gamble, it carried a risk that the claimant would not get any monies if he failed to make an introduction which resulted in a £6.5 million sale. Finally, in applying the 'officious bystander' test, there was no evidence to suggest that the parties would have said 'of course' had they been asked whether reasonable remuneration would be paid to the claimant if the sale was effected at less than £6.5 million.

A further interesting analysis was undertaken in regards to implying the term in law. The claimant argued that, based on s 15 of the Supply of Goods Act 1982, a term should be implied to the effect that the supplier of the service should be paid a reasonable charge. However, the court rejected this argument stating that s 15 only applied to a 'relevant contract' as defined in its s 12(1) as a contract under which the 'supplier agreed to carry out a service.' However, the claimant was under no obligation to introduce a buyer to the defendant, the contract was unilateral. Moreover, the court considered that remuneration was agreed in the contract; therefore, s 15 was not applicable. The question of whether a term in common law could be implied by necessity was also considered. The court held that such a term could only be implied in law by necessity if the contract fell within the categories of particular classes of contracts. The claimant relied on cases involving estate agents where a term was implied for a reasonable sum in exchange for services supplied. The court did not agree that the contract in question was an estate agent contract.[721] Also, the fact that the fee agreed was £1.2 million and not as determined by the appellate court, £435,000, was a strong indication that the claimant,

[721] ibid [69-76].

rather than looking for reasonable compensation, was taking a risk of not being paid anything with his introduction.[722]

Lord Leggatt and Lord Burrows SCJJ agreed with the majority that a term could not be implied in fact in the circumstances. However, they dissented in regards to a reasonable remuneration being implied in law. Lord Leggatt SCJ held that a statutory implication by operation of s 15(1) of the Supply of Goods Act 1982 was possible as there was no reason not to apply it to unilateral contracts. He stated that the common law rules developed default rules over time for the supply of goods, but also for the supply of services, one being that if no price is fixed for such supply, a reasonable charge is due to the supplier.[723] He argued that the later codification of the common law in s 15 of the Supply of Goods Act 1982 does not displace the common law, which remains applicable.[724] However, Lord Leggatt SCJ posited that regardless of the wording of s 12(1), which provides that the contract must be one where a person 'agrees to carry out a service,' agreements manifested and concluded by actually carrying out the service are also included in its definition. Therefore, he found that an implied term in law should operate in the circumstances and Barton should be allowed a reasonable remuneration for his introduction.[725] Consequently, the default position should be that Foxpace is obliged to pay Mr Barton a reasonable remuneration under an implied term at law unless it can be shown that the parties agreed otherwise, not that nothing was said by the parties, so nothing was payable.[726].

Similarly, Lord Burrows SCJ held that Barton had a contractual right to reasonable remuneration, not by way of a term implied in fact, as the conventional tests were not satisfied, but in law.[727] He discarded the argument of 15(1) of the Supply of Goods Act 1982 as not being applicable in the present case due to the wording of s12 (1) being confined to bilateral contracts. However, he also found that there was no contractual consideration determined for completing a sale for less than £6.5 million. Therefore, the gap could be filled by implication through 15(1) of the Supply of Goods Act 1982. In that regard, he stated that s 15(1) 'gives a strong steer to

[722] ibid.
[723] ibid [135-136], [154-155].
[724] ibid [154-155].
[725] ibid [154-155], in doing so, Lord Leggatt SCJ relied on Lord Kitchin SCJ's judgment in *Wells v Devani* [2019] UKSC 4, [2020] AC 129 [148] where the latter had stated that a term can be implied into a unilateral contract imposing a legal obligation once the contract becomes bilateral in the course of its performance, albeit in the context of implication of a term in fact.
[726] *Barton* (n 486) [136].
[727] Lord Burrows SCJ was also ready to hold that had there been no such implied term, Mr Barton would still be entitled to a reasonable remuneration on the basis of unjust enrichment, with the unjust factor being failure of basis (i.e. consideration) [241].

the courts that it is appropriate to imply a term as to reasonable remuneration into such a unilateral contract.'[728] This is because the statute has codified the common law, and as such, the close link between them cannot be denied. Therefore, 'in deciding on the common law, the courts can apply the statute by analogy.'[729] Where a term is implied in law at common law, the term has to be necessary to the type of contract in question. He characterised the contract in question as one of introduction or commission, and provided an analogy with estate agent contracts, concluding that the implied term in law of reasonable remuneration for estate agents can also apply to introduction or commission contracts, which is further justified by the presence of s 15(1), albeit being worded to cover bilateral contracts rather than unilateral ones. Turning to whether the implied term of reasonable remuneration has been excluded in the present case, he posited the agreement in question not to be an 'if, but only if agreement', where Barton would only be entitled to remuneration if the sale was completed for £6.5 million. Rather, the parties never thought or decided what should happen if the sale was completed for a lower price.[730] Therefore, the default common law rule should apply to fill in the parties' silence. The sum agreed for remuneration of £1.2 million was not a high incentivising rate of commission to encourage Barton to find a purchase, but rather reflected Barton's recoupment of what he had previously lost.[731] In sum, the majority view held that silence in the contract meant that there was no agreement on reasonable remuneration, whereas the minority viewed silence as not excluding reasonable remuneration in law if the property was sold for less than £6.5 million. The majority's view is a good example of a classical view of contract law limited by a literal view of the agreement, whereas the minority embraces a more modern view of contracts, which takes into account the commercial norms and expectations of the parties. The case highlights the difficulty of attributing the parties' reasonable expectations solely to implied terms, where express terms are found to be insufficient or ambiguous.[732] It is hereby suggested that determining the reasonable expectations of the parties would have been best achieved through the recognition of good faith duties in the contract, and not by way of an implication in fact or in law. This could have allowed an analysis not based on 'a reasonable sum' as suggested by the dissenting judges, but anchored in the contract at hand, which aimed

[728] *Barton* (n 486) [211-214].
[729] ibid.
[730] ibid [221-224].
[731] ibid.
[732] There is support in the doctrine that there should have been an implied term to pay for services rendered in the context of a commercial deal, see Paul S Davies, 'Implied Terms and Commission Agreements' (2023) 82(3) Cambridge Law Journal 385; Nicholas Strauss, 'Express Contract and Implied Quantum Meruit' (2023) 139 Law Quarterly Review 531.

to compensate the introducer in exchange for an introduction. Where the price sold for less than the agreed amount, then the compensation could have been proportionally reduced based on the final sales' price. Such an approach would have been based on the contract and on the reasonable expectations of the parties assessed from an objective basis.

3.2.3. How to Imply Good Faith?

3.2.3.1. Implication in Law

The debate as to whether good faith could be implied in fact or in law is ongoing. At first sight, it appears that good faith would be a suitable candidate for an implication in law, to operate akin to a general principle of good faith.[733] This, of course, brings us back to the debate on whether good faith should be an overarching principle in English law. If good faith is to be viewed as an overarching principle, then it would not be necessary to imply it in law.[734] However, a general principle of law and a term implied in law are two different conceptions. Sanctity of the bargain does not operate as an implied term in law in contracts; if a party frustrates the performance of the contract, there is no breach of an implied term in the contract to the effect that such party must have stayed loyal to its contractual commitment. Similarly, a party cannot exclude liability for deceit, but this is not because there is an implied obligation to be honest. Rather, the breach is due to a contravention of a specific doctrine, such as that of misrepresentation.[735]

The terms implied in law provide the courts with default rules helping them conform to previous decisions in relevant contracts. An efficient view of default rules requires that default rules be the most efficient ones.[736] The emphasis on the efficiency of default rules is particularly important in the context of the good faith debate. However, the efficiency criterion of a default rule should not go unchecked.[737] Rather, it should be balanced by considerations of fairness, which can manifest through the concept of reasonable expectations in the context of good

[733] Leggatt LJ in *Al Nehayan* (n 48) 174 also suggested that he would have reached the same decision if he had not implied good faith in fact into the contract which he considered to be relational, namely he would have implied a term of good faith into the contract in law. Later, in *Cathay Pacific* (n 644) [188] (John Kimbell QC), the court objected to an implication of good faith in law, stating that Leggatt LJ's comment in *Al Nehayan* on the matter was not the ratio of the case and was questionable.
[734] Elisabeth Peden, ''Implicit Good Faith' - or Do We Still Need an Implied Term of Good Faith?' (2009) 25 Journal of Contract Law, Legal Studies Research Paper 09/01 <http://ssrn.com/abstract=1326690> accessed 3 April 2025, 10.
[735] Michael Furmston, 'Universal Terms in Contract', in L Gullifer, S Vogenauer (eds), *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (Hart Publishing 2014) 152.
[736] See discussion on efficiency in chp 1.2.1.
[737] See discussion on fairness in chp 1.3.1.1.

faith.[738] As such, a standard of good faith would require that any rule derived from it conforms to the reasonable expectations of the parties 'by avoiding the potential risk of granting one or the other an unexpected advantage.'[739] The reasonable expectations would necessarily be determined against the context of the deal, including 'normal commercial practices, customs, usages, and an understanding of an appropriate commercial balance of obligations.'[740] This would require 'asking both what would be an efficient allocation of risk for this type of contract and what would conform to the reasonable expectations of honest men and women.'[741]

If good faith were to be implied in law, the relevant types of contracts for such a purpose would need to be ascertained. In the commercial context, this can be done based on whether the parties are dealing at arm's length, or whether they are in a 'symbiotic' relationship.[742] However, this would not be a straightforward classification. Commercial contracts are varied, and they cannot be grouped as employment or tenancy contracts under one umbrella where there would almost always be a disparity in the bargaining power. Rather, it could be the subsets of commercial contracts which would determine the 'type' in which a good faith principle could be implied. For instance, construction agreements, which are a type of commercial agreement, already include implied terms under the law.[743] It is possible to envisage that joint-venture agreements, supply agreements, distribution agreements, franchise agreements or licensing contracts would all have terms implied in law. As such, good faith could potentially be implied into such subsets of commercial contracts. This argument also finds support in the fact that the necessity criterion for implication in law is not absolute, and criteria of reasonableness and fairness are also increasingly relevant.[744]

Recognition of good faith in specific subsets of commercial contracts could incrementally spill into other subsets over time. Possibly, good faith can eventually elevate itself to a more general principle of contract law once it is implied into several various

[738] Chps 1.3.1.2 and 1.3.1.3.
[739] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 321.
[740] ibid.
[741] ibid 322-323; Collins gives the example of the implied term of mutual trust and confidence in the context of employment contracts. He posits that such an implied term serves to uphold the efficient operation of employment contracts, by preventing misuse of contractual powers by the employer and instead encouraging a cooperative model of human resources management in order to maximise productivity. This efficiency criterion is also supplemented by a good faith control, by meeting the expectations of the parties under modern employer-employee relationships. Consequently, the employees physical and financial wellbeing are balanced against the employers' interest to manage its business freely.
[742] As proposed by Chen-Wishart, see text to n 473 above.
[743] See for instance, *Young & Marten Ltd* (n 706).
[744] *Crossley* (n 719) [36] (Dyson LJ). Also, McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 331-332.

categories.[745] As such, it would not be necessary to morph the law of contract into law of contracts.[746] In this context, the distinction between relational and discrete contracts becomes less important for deciding whether to imply good faith or not, but rather simplifies the classification of contracts based on the subject matter of the contract rather than the standards imposed on the parties to achieve the aim of the contract. For instance, a distributorship agreement can concern the one-off distribution of a limited product within a short amount of time, where it resembles more of a discrete contract; but it can also manifest as a long-term contract involving extensive cooperation duties on both parties. The decision whether to imply good faith in law into distributorship contracts revolves around the fact that it is classified as a distribution contract, and not as a relational contract.[747] Yet, the increasing interest in the concept of relational contracts merits attention.[748] We now turn to issues afflicting relational contracts.

3.2.3.1.1. Relational Contracts

The categorisation of contracts as relational is problematic. Even Leggatt LJ's remarks in *Yam Seng* related to '*some* joint venture agreements, franchise agreements and long-term distributorship agreements.'[749] This seems to negate the idea that good faith might not be implied into all types of relational contracts.[750] Moreover, given that all contracts are relational to some extent, is it helpful to speak of relational contracts as a separate category?[751] It is

[745] Although it is proposed that statutory reform is more adequate than incremental adoption of good faith, see chp 6.4.1.
[746] See Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 17-20. McKendrick, *Contract Law* (n 1) 2 contends that contract law is moving slowly towards a law of contracts because the general principles are becoming less important.
[747] This approach also circumvents the criticism that relational contracts are not sufficiently definite to constitute a nominate category of contracts, see eg Paul S Davies, 'The Basis of Contractual Duties of Good Faith' (2019) 1 Journal of Commonwealth Law 1 <https://www.journalofcommonwealthlaw.org/article/8784-the-basis-of-contractual-duties-of-good-faith> accessed 3 April 2025, 24-25.
[748] Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (n 281) 528.
[749] *Yam Seng* (n 3**)** [143], emphasis added. In *Acer Investment Management Ltd and another v Mansion Group Ltd* [2014] EWHC 3011 (QB) [108-109], despite being a distribution agreement, the court refused to categorise the contract as a relational one, refusing to adopt a formalistic approach to relational contracts.
[750] See for instance, *TAQA Bratani Ltd* (n 577), where the court found that although the contract was relational, the clause relied upon provided for an absolute and unqualified power, therefore a duty of good faith could not be implied in the presence of an express clause to the contrary.
[751] Melvin A Eisenberg 'Why There is No Law of Relational Contracts' (2000) 94 Northwestern University Law Review 805, 813-817 argues all contracts are at least to some extent relational. Davies, *JC Smith's the Law of Contract* (n 56) 306, also refuses a relational contract categorisation expressing that '[t]hat type of contract must be readily discernible; otherwise, there is a risk of inconsistency, incoherency, and the courts' intruding into the parties' bargain where it is not necessary to do so.'

accepted that the relational contracts axis denotes various degrees of relationship, on the one end having discrete transactions and on the other highly cooperative agreements.

After *Yam Seng*, several cases referred to it and further focused on the notion of relational contracts. In *Bates v Post Office Ltd (No.3)*, the claimant, a sub-postmaster, had a contract with the Post Office in which the claimant was to be liable for all losses under the contract.[752] The Post Office had introduced a new computer system to record the actions of the sub-postmaster, such as accounting. Due to technical issues with the system, the sub-postmaster had to pay substantial amounts of money due to discrepancies in accounts, which were not correct. Many sub-postmasters were affected by the malfunctioning of the system, and many separate actions were brought against the Post Office, Mr Bates' being one of them. In the trial dealing with common issues, and in dealing with the concept of relational contract, Fraser J set out nine characteristics of such contracts for the implication of a good faith duty, without deciding whether it was an exhaustive list. These characteristics were enumerated as follows:

1. There must be no specific express terms in the contract that prevents a duty of good faith being implied into the contract.
2. The contract will be a long-term one, with the mutual intention of the parties being that there will be a long-term relationship.
3. The parties must intend that their respective roles be performed with integrity, and with fidelity to their bargain.
4. The parties will be committed to collaborating with one another in the performance of the contract.
5. The spirits and objectives of their venture may not be capable of being expressed exhaustively in a written contract.
6. They will each repose trust and confidence in one another, but of a different kind to that involved in fiduciary relationships.
7. The contract in question will involve a high degree of communication, co-operation and predictable performance based on mutual trust and confidence, and expectations of loyalty.

[752] *Bates* (n 48).

8. There may be a degree of significant investment by one party (or both) in the venture. This significant investment may be, in some cases, more accurately described as substantial financial commitment.
9. Exclusivity of the relationship may also be present.[753]

Without going through the specifics of each item on this long list, one can see that some of them are already problematic even before they are applied to a case. What is meant by a long-term relationship is unclear and cannot be categorically defined. In some cases, the long-term nature of the relationship will be obvious, whereas in others this may be problematic. The parties' intention to be loyal to the bargain and act with integrity relates to the debate as to whether it is possible to contract out of good faith, discussed further below.[754] In regard to the significant investment criteria, it is unclear what types of investment, other than financial, would be sufficient to qualify as such. Where the relationship is exclusive, it is also doubtful whether this adds anything further to the mutual dependence of the parties on each other where this is necessary to perform the contract as agreed. In deciding the matter, Fraser J concluded that the contracts between the Post Office and its sub-postmasters were relational 'which means that there is an implied duty of good faith in the agreement.'[755] Clearly, the court implied in law a duty of good faith into the contract as a consequence of categorising it as a relational contract. The court guarded against the possibility of such decision being wrong, by considering and finding in three out of four class of terms that good faith could be implied on grounds of business efficacy, in fact.[756]

In a more recent case, the court refused the categorisation of contracts between a mobile virtual network operator (P4U) and mobile network operators (EE, Vodaphone UK, O2) as relational.[757] After reviewing the case law on the matter, the court emphasised the carefully drafted and considered nature of the contracts to state that had the parties wished to impose a general obligation of good faith on themselves, they would have done so expressly.[758] Therefore, based on a literal interpretation of the contract, the court did not find that the general express clause which existed in the agreement applied to all the obligations in the contract, but

[753] ibid [725].
[754] See chp 4.5.
[755] *Bates* (n 48) [1113].
[756] ibid [755-757], the terms in issue related to the Post Office's exercise of its powers under the contracts.
[757] *Phones 4U Limited (In Administration) v EE Limited* [2023] EWHC 2826 (Ch) [663] (Roth J).
[758] ibid [653].

only to a few.[759] Also, the court found that the nature of the agreements was such that the parties were effectively competing with each other to supply connections to customers directly.[760] The court concluded that it would not matter if the contract was relational because of the lack of a general duty of good faith, which could be implied.[761]

Macneil's work on relational contracts is of particular importance.[762] His understanding of contracts derives from a sociological perspective, which posits contracts as instruments which cannot be dissociated from the social structures and norms within which they operate.[763] The relational contract concept appeared as a contrast to discrete transactions, creating the impression that a relational contract is easily identifiably, similar to a spot transaction. Categorisation as a relational contract would therefore require the contextual interpretation of the contract, to determine the intentions of the parties.[764] Such contextual interpretation might be more relevant where the contract is not a discrete contract, because longer, more complex transactions ascertaining the expectations of the parties would necessitate more than what a literal approach of interpretation could provide in understanding the reasonable expectations of the parties.[765] MacNeil does not propose that there be such a separate class of contracts which can be named as relational, but he contends that a literal approach to contract interpretation would be inappropriate in the case of contracts which are not discrete but rely on the parties' cooperation.[766] In short, Macneil's work falls short of conceptualising relational contracts in a pragmatic manner.[767]

[759] ibid.
[760] ibid [662].
[761] ibid.
[762] For an overview of MacNeil's work, see Collins, 'Is a Relational Contract a Legal Concept?' (n 75) 8-9. Also see Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (n 281) 533.
[763] Macneil, 'Contracts: Adjustment of Long-term Economic Relations Under Classical, Neoclassical and Relational Contract Law' (n 81).
[764] Collins, 'Is A Relational Contract a Legal Concept?' (n 75) 8-9.
[765] Ian R Macneil, 'Contracts: Adjustment of Long-term Economic Relations Under Classical, Neoclassical and Relational Contract Law' (n 81) 890.
[766] Collins, 'Is A Relational Contract a Legal Concept?' (n 75) 9.
[767] Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 186, argues that the relational contract 'as a distinct category recognised in law, mandating a specific response, is likely to disappear from the analysis [of implying terms in fact], with only the implied term of good faith remaining.'

A better attempt at defining relational contracts was made by Collins.[768] His reframing of the relational contract is through the lens of quasi-integrative systems.[769] He posits that an identified group of contracts called 'networks' share crucial relevant features in common, requiring 'intensified duties of loyalty and co-operation implied by law.'[770] By quasi-integration

> is meant the idea that though no single legal entity binds the parties together but rather the arrangement is formed by two or more separate organizations that retain their antagonistic interests, the agreement seeks to achieve many features of organizations for the purpose of establishing efficient relations of production.[771]

These networks are characterised by 'an intensified economic logic of both competition and co-operation that arises from their structure as a quasi-integrated production regime (...).'[772] The parties are seen as maintaining their antagonistic interest, all the while seeking to establish 'efficient relations of production.'[773] This is because they will have to play by the market rules to maximise their revenue, and compete with each other to maximise their own profit allocated from the sum of profits commonly generated by all parties.[774] The view adopted of such networks is an economic one which assumes that all parties would be in a better economic position through their joint efforts to increase the pot of profits to be later shared. The duties of loyalty and cooperation arise out of the economic logic of the structure rather that the length of the contract or the substantial investment of the parties in it as suggested by Fraser J in *Bates.*[775]

The issue with framing the categorisation of relational contracts as one relating to networks is that the networks, envisaged also as connected contracts, derive from social and economic sciences, and cannot be easily transposed into the legal field.[776] Indeed, in contract

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[768] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557**)** 301; Collins, 'Is A Relational Contract a Legal Concept?' (n 75**)** 12.
[769] The concept later also gained popularity in the fields of sociology and economics, see sample literature in Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557**)** 326 fn 90.
[770] ibid 301.
[771] ibid 326-327. The example given by Collins is that of franchise networks, where 'the franchisor and franchisee remain separate business entities, but they have to co-operate for the purpose of marketing a product or service. Both parties have an interest in maximizing retail sales, for which purpose they will need to co-operate intensively, yet both parties have an interest in maximizing their own returns on their investment by securing a greater share of the profits in the franchise agreement.'
[772] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 301.
[773] ibid 327.
[774] Collins, 'Is A Relational Contract a Legal Concept?' (n 75) 15, the author states that 'the underlying logic in these quasi-integration arrangements is driven both by the market and the organisation: parties must both compete and co-operate.'
[775] *Bates* (n 48)**.**
[776] Collins, 'Is A Relational Contract a Legal Concept?' (n 75) 8.

law, the will of the parties is the *raison d'être* of the contracts. Where the will is stretched so far beyond the scope of the specific contract, the other contracts in the network can no longer be justified to affect the rights and obligations of the parties to that specific contract. An individual franchisee owes no duty of loyalty to another franchisee in the same network.[777] The obligations of the franchisee solely arise out of its individual contract with the franchisor. Similarly, the distributor does not owe any duties to another distributor in the same network, but only to its manufacturer or vendor. The duties which arise out of individual contracts are the delimitations of the duties owed by these parties. However, it may be that in the performance of the individual contract, the franchisor, or the manufacturer or the vendor, might have to consider its business interests in a wider sense and seek to coordinate them in a way not to create conflicting obligations for the franchisor, or the manufacturer or the vendor, arising out of each individual contract with their contracting parties. English law does not yet recognise an explicit doctrine of connected contracts or similar for regulating business networks. Therefore, the network within which a party operates may be taken into account within the contextual interpretation of a contract, based on an assessment of the reasonable person, or when implying a term, by asking whether the reasonable expectation of honest people would be better served by taking into account such network.[778]

The duties which emanate from the classification of quasi-integrative contracts can be sectioned into three categories.[779] The first one relates to the duty to assist the other in its performance of the contract. This may include the efficient exchange of information, assistance, or any type of support to maximise the profitability of the contract. This duty has its limits because it does not extend to scenarios where assisting the other side would be harming the interests of that party in the apportionment of the profits. The second one is the duty not to harm the interests of the other party, which may cause a decrease in profitability. If harming the interests of the other party helps increase the harming party's share of the profits, this should not be allowed.[780] Otherwise, the harming party might be incentivised to avoid

[777] Hugh Collins, 'Introduction to Networks as Connected Contracts' in G Teubner, M Everson, *Networks as Connected Contracts* (Bloomsbury Publishing 2011) 14-15, this is also recognised by Collins, where for instance, in a franchising context, a franchisor fails to develop the network of franchisees by seeking out new ones, can be seen as a disloyal act towards the franchise operation as a whole, which in some jurisdictions can amount to a breach of a duty of good faith.
[778] Roger Brownsword, 'Networks as Connected Contracts by Gunther Teubner, Hugh Collins and Michelle Everson' (2012) 75 MLR 455, 460.
[779] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 328.
[780] ibid, in the context of connected networks, Collins argues that this would be allowed if there is a compensating interest in profit or benefit to oneself.

effectively maximising the overall profits. The third one relates to a duty of loyalty to the network to maximise the overall profits and prevent or defend against adverse interference by third parties. Where the interests of a party in maximising the overall profits or increasing its individual profits are at odds, the former must be preferred. If the second interest were to be preferred, this would inevitably affect the first one adversely. For example, in *Shell UK Ltd v Lostock Garage Ltd*, Shell, as the franchisor, discriminated between its franchisees in regards to rebates allowed to some franchisees and not to others.[781] This had the effect of negatively affecting the business of some of its franchisees. Bridge LJ, in the minority, found that an implied term operated in the franchise agreement to fetter Shell's power to discriminate between franchisees, by giving rebates to certain franchisees and not to others.[782] This implied term is said to have two aspects; first one is a negative one, preventing the franchisor from offering the franchisee's competitors terms which are more favourable than those available to the franchisee; and secondly it has a positive aspect, which imposes on the franchisor to provide the franchisee with terms that are not less favourable to it than those provided to its competitors.[783] Consequently, Shell's interest in maximising its individual profit was at odds with its interest in maximising the overall profits in the context of the individual contract. Therefore, Shell's choice of curbing the overall profits available in one franchising contract should be seen as violating the reasonable expectations of honest people by not fettering Shell's discretion in offering rebates.

By proposing a quasi-integrative contract classification, Collins sought to find a solution to the binary view of contracts, where if the contract is of a fiduciary nature, good faith duties can be implied, whereas all other contracts do not automatically attract such duties.[784] Although an invaluable contribution to academic literature, a quasi-integrative classification cannot overcome one crucial obstacle. Indeed, it is not possible to uphold a view of contracts which displaces the principle of autonomy so vehemently defended by the courts in favour of the network of the contract. In a network view of contracts, the duty of loyalty is envisaged as being owed to the organisational structure, rather than to the deal between the parties. His

[781] [1976] 1 WLR 1187 (CA).
[782] ibid 1204. Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 327 argued that the majority decision contravened to the 'underlying economic logic' in this quasi-integration deal which is 'driven both by the market and the organization: parties must both compete and co-operate.' He considered Shell's conduct to be 'only within a market frame of reference' where he granted concessionary rebates to franchisees with sufficient bargaining power to demand them, thereby breaching a 'duty of loyalty towards the franchise network.'.
[783] ibid 1206.
[784] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 324.

approach blends the line drawn between the market and the 'organization;' the market being where the parties interests are antagonistic, where they each seek to maximize their advantage at the cost of the other party,' and the 'organization' being a network of contracts that binds the parties together, where they must cooperate to 'maximize the profits of the organization itself, the profits then being distributed according to the formula set by the contracts.'[785] Therefore, the connected contracts, or network theory, should be shelved until further notice from the courts.

3.2.3.1.2. An Alternative to Relational Contracts: Revenue Generating and Sharing Contracts

A more pragmatic and realistic alternative to the above could be either to redefine what we mean by relational contracts by restricting it to a certain category of contracts, or completely cut the ties with the relational contracts theory in order to develop an alternative. In the context of construction contracts, the recent doctrinal suggestion indicates replacing a 'party-centric' approach with a 'project-centric' approach, albeit recognising that the vocabulary to describe a different approach does not yet exist.[786] This approach would 'place the parties' individual interest within the wider lens of their shared interests in achieving the agreed common purpose of the contract.'[787] The policy drive within the specific industry is notably important in characterising such an approach. However, another way of moving beyond any limitation imposed by any specific industry or contract type, is to recognise a revenue generating and sharing contract (RGSC) classification.[788] RGSCs, as envisaged herein, refer to contracts where the overall profits envisaged to be shared by the parties are generated through the contract. Other non-financial values that are intended to be generated or actually generated by the contract are directly dependent on the financial value generated by the contract therefore, such non-financial value is implied in the financial value. For instance, if two parties enter into a contract to set up a joint venture for the manufacturing of new electronic chips, it may be that the product they manufacture is novel and disrupts the industry by making all existing ones on the market obsolete. As such, the value created by the joint venture is not only financial but

[785] ibid 326.
[786] David Christie, Severine Saintier, Jessica Viven-Wilksch, 'Industry-Led Standards, Relational Contracts and Good Faith: Are the UK and Australia Setting the Pace in (Construction) Contract Law?' (2022) 43 Liverpool Law Review 287, 289.
[787] ibid.
[788] An alternative nomenclature could be revenue share contracts or revenue generating contracts, or value generating contracts.

also, for instance, reputational because the parties are more likely to draw new investment into the company from external funders. Similarly, they are more likely to obtain a higher valuation if they were to sell the joint venture, simply because the goodwill of the company might encompass more than the value of its assets.[789]

The ultimate reason for the existence of the contract is the sharing of profits generated by the performance of the contract.[790] The contract must create an economic value, which would not have existed but for the existence of the contract. The parties' main goal is to generate the maximum amount of revenue to be shared between them. As such, the interests of the parties are parallel in increasing the revenue to be shared, but antagonistic in that they have to compete with each other to get a bigger slice of the revenue cake. It is similar to the quasi-integrative contracts concept proposed by Collins described above, with an important difference, which is that the RGSCs do not need to refer to a network external to the contract.[791] In fact, they are to be interpreted according to the regular applicable rules to all contracts without creating any disruptions within the law. Another advantage of categorising RGSCs, rather than relational ones, is that the duties of cooperation and loyalty do not figure in the definition, but emanate from the categorisation as RGSCs.[792]

Ultimately, a RGSC is easily identifiable. Indeed, a franchise contract does have the ultimate goal of maximising the overall profits in the performance of the contract, and then maximising each party's share in the distribution of such overall profits. Similarly, manufacturers or vendors aim to maximise their presence in the market in terms of volume and reach, and the distributors aim to increase their business with the manufacturer or vendor,

[789] Goodwill is hard to define and quantify, its ordinary legal meaning and accounting meaning might differ depending on the circumstances. The ordinary legal meaning of goodwill is the good name and public reputation of the business concerned, see *Primus International Holding Company v Triumph Controls UK Ltd* [2020] EWCA Civ 1228 [29] (Coulson LJ). The court interpreted the contract and rejected an accounting definition of the word in the circumstances, which would have meant a portion of a purchase price that is higher than the net value of assets minus liabilities assumed [17].

[790] This view of RGSC excludes most contracts between commercial parties and public entities, because such contracts are guided by public interest rather than profitability. However, another categorisation, could be found for such contracts and relevant good faith duties be implied accordingly. For instance, in *Amey Birmingham Highways Ltd v Birmingham City Council* [2018] EWCA Civ 264, the Court of Appeal adopted a contextual approach to interpreting the duties of the parties, taking into account the relationality of a 25-year private finance initiative agreement contract for maintenance of Birmingham's road network. Similarly, the contract in *D&G Cars Ltd* (n 49), despite its classification as a relational one, is not a RGSC, due to the activities undertaken by D&G Cars Ltd providing essentially a public service. Therefore, this contract too would have benefited from a separate categorisation than the general umbrella term of relational contract as the courts do not seem to distinguish the relational contract concept and consider it equally relevant for both between private parties, and between private and public parties.

[791] For the discussion on quasi-integrative contracts, see text to n 769.

[792] For instance, see the list provided by Fraser J in *Bates* (n 48) 725 whereby duties of cooperation and loyalty figured amongst the classification criteria.

which ultimately aims to generate overall profits for both parties. In joint venture agreements, the logic is the same. The parties seek to maximise the profits of the joint venture to then maximise their individual portions out of the overall profits. One may also add commercial agents to this mix.[793] Conversely, for instance, sales contracts, construction contracts, license contracts, would usually not be RGSCs. Indeed, the purpose of these contracts is not to generate revenue to distribute the overall profit amongst the parties. Rather, the exchange of promises is well-defined and does not necessitate generating profit through the performance of the contract to achieve the aim of the contract. A seller and a buyer are not concerned with generating revenue through the contract between them. The seller will seek to maximise its profit by selling at the highest possible price, and the buyer will seek to buy at the lowest possible price. There is no recourse to money-generating activities to make the sale possible outside the individual sales contract. The contract does not allow for common profit-making, only for individual profit-making, which can only be off the back of each other; as such, the contract has a limiting function in the parties' common profit-making capacity.

In contrast, in a RGSC, the contract is the instrument which facilitates and allows the parties to make a common profit together, then compete to have a share of that profit. Any financing arrangements with third parties in non-share revenue contracts would help the parties to execute their obligations under the contract, for instance, to sell and to buy, but would not be revenue generated by the execution of their obligation under the contract to make an overall profit together. Rather, the profit to be made by the parties under the sale is the driving force of the contract, rather than any profits to be made commonly through money-generating activities under the contract, to then be allocated to each party under the contract. However, a RGSC is not restricted by the categorisation of the subsets of commercial contracts. Indeed, some sales contracts can also be classified as RGSCs if they fit into its description of value generation and sharing. For instance, if the contract is not simply a sale but also a sale and a manufacturing contract, akin to a joint venture, then a RGSC classification would be suitable. Therefore, a RGSC classification transcends any contract type and focuses on the object of the contract, namely, whether revenue generation and sharing are intended through the contract.

The commonality across RGSCs is that the ultimate aim of the contract is the understanding that the parties are entering into the contract with the expectation that the

[793] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 328. Although rather than the common law, Commercial Agents (Council Directive) Regulations 1993 (n 140) provides for the termination rights for failure to carry out the obligations of either party under the contract s16. Such obligations are provided for in s 3 and s 4 and require that they be performed in good faith.

performance of the contract would ideally lead to generating profit. Whether this is the actual intention of the parties is not relevant for categorising the contract; their aim might be simply to associate with a good brand, or to extend the territorial market reach but the underlying logic is that all commercial parties, as commercial actors on the market, act with an understanding that the purpose of all commercial activity is to generate profit. To achieve such an aim, the parties would need to cooperate or be loyal to the contract as agreed, but this will not be because their contract is relational or because they operate from within a network, but because, to generate profit, they have to cooperate or be loyal to the contract by design. The actual or intended length would not be indicative because both short-term and long-term revenue share contracts qualify as such, whereas the length of the contract is a factor taken into account when deciding on the relationality of a contract. The longer the duration, the more likely that cooperative and loyalty duties will be involved, but short-term revenue share contracts would also have such duties due to the ultimate aim of the profit-maximising aim of such contracts. As such, the length of the agreement is not to be viewed as a determining factor.[794] Such an economic or market rules-oriented view of contract provides a more pragmatic avenue for regulating the rights and obligations of the parties as commercial actors through the implication in law of good faith duties.

3.2.3.2. Implication in Fact

A less radical option is implying good faith in fact. This method would take into account the particularities of each case and the intention of the parties, rather than policy concerns. As such, the court would determine the extent of any obligation to be derived from good faith based on the relevant context surrounding the agreement. The party relying on an implied term would have to pass the threshold for either of the classical necessity tests. For instance, as set out in *The Moorcock* and reiterated in *Marks and Spencer*, it will be the least term which provides a minimum of efficacy in a business sense that the parties, as reasonable business people, would have intended to have.[795] The requirement that the implied term be capable of clear expression, and in particular be the least encompassing version sufficient to provide a

[794] A similar point was made by Collins, 'Is a Relational Contract a Legal Concept?' (n 75) 15-16.

[795] *The Moorcock* (n 674), *Marks and Spencer* (n 658); Paterson, 'Terms Implied in Fact: The Basis for Implication' (n 665) 10, the reasoning of the court was a cost-benefit analysis, where the '[t]he precaution of taking reasonable care to ascertain the safety of the berth would have reduced the risk of damage to the ship. The jetty owners' proximity to the site made them the best placed party to have taken that precaution and hence liability was assigned to them.'

minimum of efficacy, is problematic in this context. Where the obligation of good faith is not clearly ascertainable by the court, it will not be implied in fact. More crucially, it would be hard to imagine scenarios where a vague concept of good faith satisfies the necessity requirement of the classical tests. With the potential of having multiple meanings, the court cannot determine how such an abstract principle would translate into an implied term of the contract. A better view is to imply precise duties derived from good faith, such as a duty of reasonable skill and care in performing the contract.[796] For this, there would have to be an anchoring to legitimise the judicial basis of the decision. Rather than drawing it out of thin air, a preferable approach is to view good faith as an overarching principle of contract law, in the same way that party autonomy is seen as a general principle. If a court can refuse to imply a term in fact where the proposed term would contravene to the parties' freedom of contract, due to substantively restricting on either or both party's ability to contract, so should the court be able to hold that a general principle of good faith prevents it from implying a term in fact due to the proposed term being substantively against considerations of fairness, honesty or fair dealing in the given case. It is not hard to imagine that over time, as similar type subsets of commercial contracts have similar good faith derived obligations implied in fact, that a general duty can be implied in law restricted to such subsets.

The most extensive discussion of good faith in recent years is no doubt the decision of Leggatt J in *Yam Seng*.[797] The court's issue was whether it should imply two terms containing good faith principles into a sparsely drafted distribution agreement. The terms in question were whether International Trade Corp should not have knowingly provided Yam Seng with false information, and whether it could approve other sellers who could offer the product at lower prices than Yam Seng in the contractual territories. He held that the first implied term was breached, and justified the repudiation of the contract; whereas there was insufficient evidence to establish the breach of the second duty. Leggatt J undertook an extensive review of authorities on good faith and concluded that English law's hostility to recognising good faith as a default rule in the performance of contracts was 'misplaced.'[798] His understanding of the

[796] Although recently in *Re Compound Photonics Group Ltd; Faulkner v Vollin Holdings Ltd* [2022] EWCA Civ 1371, the Court of Appeal revisiting the content of an express duty of good faith in the context of an unfair prejudicial claim against majority shareholders, that a duty to act in good faith could be breached by dishonest behaviour but also behaviour which would not be regarded as commercially acceptable to reasonable and honest people, even if not dishonest [239] (Snowden LJ). Moreover, the Court held that any positive obligation which could arise under an express clause of a duty of good faith could only arise as a matter of interpretation or implication from the other terms of the contract, therefore refused 'derivative' obligations deriving from a good faith clause [243] (Snowden LJ).
[797] *Yam Seng* (n 3).
[798] ibid [154] (Leggatt J).

good faith concept included an appreciation of the specific contractual context. Indeed, he viewed the contract at hand as one requiring a mutual trust and loyalty, not to a high degree as much as required in fiduciary or employment contracts, but not as the bare minimum required in spot transactions. Thus, he adopted the relational contract theory terminology by classifying the distributorship contract as a relational contract.[799] Such categorisation necessarily implied that the parties' expectations would not entirely be captured in the express terms of the contract. Therefore, he noted that implication was necessary to give business efficacy to the contract.[800] He emphasised that although the construction of good faith necessitates a contextual approach, the test remains an objective one. It does not depend on the parties' perception of whether an act is improper. Rather, the question is whether 'in the particular context the conduct would be regarded as commercially unacceptable by reasonable and honest people.'[801] As such, the presumed intention of the parties is determined by 'attributing to them the purposes and values which reasonable people in their situation would have had.'[802] Arguably, Leggatt J could have arrived at the same conclusion through the conventional tests of implying the two duties in fact. The opponents of implying good faith into contracts argue that the contract can be deemed efficacious even without implying good faith, thereby failing to satisfy the business efficacy test.[803] Further, if an officious bystander were to ask the parties whether there is a term that the contract be performed in good faith, the parties would rather be confused as to what is meant by good faith, thereby failing to satisfy the officious bystander test.[804] Regardless of such criticisms, Leggatt J has seized the opportunity in *Yam Seng* to pave a way for good faith duties to be implied in fact in contract law when necessary for business efficacy. Fundamentally, Yam Seng did not change the status quo and is fundamentally uncontroversial.[805]

Shortly thereafter, Jackson LJ in the Court of Appeal, overturning Cranston J's decision in the High Court in *Medirest*, took a restrictive approach and prevented the development of good faith a general doctrine; rather, the court insisted that if the parties wish to have such duty regulate their relations, they must do so expressly.[806] Medirest and the Trust for Medirest had a contract for providing facilities management, including catering services, to the hospital. The

[799] ibid [143].
[800] ibid [165].
[801] ibid [145].
[802] ibid.
[803] Davies, 'The Basis of Contractual Duties of Good Faith' (n 747) 27.
[804] ibid.
[805] Simon Whittaker, Good Faith, Implied Terms and Commercial Contracts (2013) 129 Law Quarterly Review 463, 469.
[806] *Medirest* (n 97) [106] (Jackson LJ).

Trust would pay a contract price every year in exchange for such services provided in accordance with certain service-level benchmarks. However, from the early stages of the contract, the Trust took a difficult approach to how the contract was performed by Medirest. Each party separately terminated the contract within 18 months and claimed substantial post-termination losses. The issue was with clause 3.5, which provided that

> [t]he Trust and [Medirest] 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 and to enable the Trust or, as the case may be, any Beneficiary to derive the full benefit of the Contract.[807]

The court preferred the Trust's construction of the clause in which the general duty to cooperate was restricted to the two stated aims of the contract, namely the efficient transmission of information and instructions, and the enabling of the Trust or any beneficiary to derive the full benefit of the contract.[808] Again, the court adopted a contextual approach to good faith and concluded that the content of the duty to cooperate in good faith, as limited by those two aims, is that 'the parties will work together honestly endeavouring to achieve the two stated purposes.'[809] The court also emphasised that as the contract was a detailed one which attempted to provide for a number of eventualities, a duty to act in good faith or a duty to cooperate should not be construed to mean that they can override any specific duties and limitations in the contract.[810] The court held that while the Trust had erroneously made wrongful deductions in breach of the agreement, which they had later cured, such a breach would not have breached clause 3.5 in any event for two reasons.[811] First, there was no evidence that the Trust had acted dishonestly, and second, the deductions were irrelevant to the two aims of the contract, namely the transmission of information or instructions between the parties, or receipt by the Trust or any beneficiary to derive the full benefit of the contract.

Notwithstanding the decision in *Medirest*, the following year, the High Court in *Bristol Groundschool Ltd v Intelligent Data Capture Ltd* gave support to Leggatt J's above approach and an obligation to act in good faith was implied into a hybrid joint venture and distribution agreement relating to the development of computer-based training materials.[812] The parties

[807] ibid [14].
[808] ibid [106-107].
[809] ibid [112].
[810] ibid [154].
[811] ibid [114].
[812] *Bristol Groundschool* (n 49) (Richard Spearman QC).

were in business for about ten years between 1999 and 2009, where they collaborated on producing electronic training manuals for commercial airline pilots. The defendants created the artwork, and the claimant prepared the text, sold the manuals to students and paid the defendant a specific sum for each product sold. However, they fell out in 2009 and each started producing their own training manuals. The issue was whether the defendant had breached the agreement by failing to provide technical support and refusing to include new materials in the manuals. In a counterclaim, the issue was whether a duty of good faith should be implied, and whether it was breached by the claimant when they downloaded materials from the defendant's information technology systems without authorisation. In reliance on the methodology of *Yam Seng* for implying terms into relational contracts, the judge Richard Spearman QC emphasised the honesty element of good faith and posited the test for implication to be whether the conduct in question would be 'as commercially unacceptable' by reasonable and honest people in the particular context involved.[813] He concluded that the agreement did contain an implied duty of good faith.[814] The duty was breached because it was commercially unacceptable, and the conduct of the claimant did not accord with the 'normally accepted standards of honest conduct.'[815] However, the judge concluded that the breach was not repudiatory, because it did not 'strike at the heart of the trust which is vital to any long-term commercial relationship,' and there were extenuating circumstances.[816]

Similarly, in the High Court, *D&G Cars Ltd*, a duty of good faith was implied into a long-term vehicle recovery contract based on trust and integrity.[817] The contract provided a procedure for disposing of recovered vehicles, and some of these had to be crushed to ensure that no identifiable part could be then used on other vehicles. D&G failed to comply with the procedure in regards to one vehicle and instead used it as part of its own fleet for a training exercise for its apprentices. The contract provided the Essex Police Authority the right to terminate the agreement in the event of material breach, and the issue was whether they could exercise such right in the circumstances. The court concluded that D&G breached an express term of the contract, and therefore, the Authority could terminate. More importantly, the court found that there was a clear breach of an implied term to act with honesty and integrity. First Dove J, in reliance on the approach undertaken in *Yam Seng*, stated that the contract was for a

[813] ibid [196], in citing the dishonesty test formulated in *Royal Brunei Airlines Sdn v Tan* [1995] 2 AC 378, and used again by Beatson LJ in *Mid Essex* (n 97) [150].
[814] *Bristol Groundschool* (n 49) [196].
[815] ibid [218].
[816] ibid, citing *Yam Seng* (n 3) [172] (Leggatt J).
[817] *D&G Cars Ltd* (n 49).

relatively long period (initially 5 years), during which the parties were going to undertake a large number of individual transactions, and D&G's role involved acting on behalf of a law enforcement agency, by returning recovered property to the public or to be used as evidence in criminal investigations. Therefore, its role was not simply to provide simple storage space but to carry out an act of public service. The court concluded it was a ''relational' contract par *excellence.*'[818] Second, the court rather preferred to use 'integrity' rather than 'good faith', but was essentially in line with *Yam Seng*'s approach to implication of terms.[819] Although the judge concluded there was no dishonesty, he did find that D&G's conduct amounted to behaviour contrary to integrity, which the parties would have identified as acts inconsistent with the requirements of fair dealing had they been asked at the time of contracting.

In 2016, the Court of Appeal handed down two notable decisions, one showing support to Yam Seng, the other rejecting it. In *Globe Motors,* Beatson LJ endorsed that a duty of good faith may be implied into relational contracts.[820] However, the case was one for interpretation and not for implication therefore, the matter was not considered any further.[821] In *MSC Mediterranean Shipping Company S.A,* Moore-Bick LJ, on appeal against the decision of Leggatt J in the first instance, refused to endorse a general organising principle; rather, he insisted on 'developing the law along established lines.'[822]

Despite the Court of Appeal's seemingly wavering support, Lord Leggatt continued championing the implication of good faith in fact into contracts in a later case in the High Court in *Al Nehayan.*[823] The parties entered into a joint venture regarding luxury hotels and subsequently a travel business. The deal was not commercially successful, and Kent requested additional funding from Sheikh Tahnoon, who initially agreed but later refused. Leggatt LJ implied a duty of good faith into the contract and more precisely elucidated two duties which reflected the parties' reasonable expectations. First, the parties could not sell or enter into negotiations not to sell their interest in full or in part in the joint venture to a third party covertly and without informing the other party. Second, the parties could not use their position as shareholders of the companies to obtain a financial benefit for themselves at the expense of the other party. Although Leggatt LJ cited and followed the necessity tests upheld in *Marks and*

[818] ibid [176] (emphasis in text).
[819] ibid [175], [176].
[820] *Globe Motors* (n 644).
[821] ibid [68].
[822] *MSC Mediterranean Shipping Company S.A.* (n 49) [45].
[823] *Al Nehayan* (n 48).

Spencer, he did not consider in detail how they applied to the case at hand.[824] What is clear is that the implication was not made in law but in fact. This was also confirmed later by Fancourt J in *UTB LLC*.[825] This case concerned breaches of alleged requirements of good faith based on two alternative grounds; first was that the joint-venture company was a quasi-partnership, and the second was that the contract between the parties was a relational contract. The judge refused to imply on either of the grounds, stating that the relational character was only one factor to take into account when implying in fact, and the emphasis was on whether the implied term was, from the viewpoint of a reasonable reader of the contract, necessary to give business efficacy to the contract.[826]

Implying good faith in fact relieves the court of the burden which comes with its roles as a lawmaker. However, through the operation of the doctrine of precedent, decisions where a term is implied in fact are likely to be adopted as precedents. As such, the identification of the type of contract concerned is relevant. Characterisation of the type of contract will focus on the essence of the parties' deal, beyond their choice of form and label.[827] Where the term will be implied in law, the court will inevitably have to establish that such implication is necessary for that type of contract. The parties would have to enter into such defined type contracts, knowing that they will have to abide by good faith duties. Whereas, where the term is implied in fact, it is factors beyond the type of contract that determine whether the implication is justified. Implying good faith in fact is considered to be the least controversial approach as it does not seem to contravene to the freedom of contract.[828]

However, the tests for implication in fact are not without criticism as they focus on ascertaining an illusory common intention, serving a residual role in policing opportunistic gaps. Where a contextual approach to interpretation is progressively preferred over a standard

[824] ibid [218], [272].
[825] *UTB LLC* (n 644).
[826] ibid [202]-[203].
[827] For the distinction between characterisation and interpretation, see McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 19-22.
[828] Davies, 'The Basis of Contractual Duties of Good Faith' (n 747) 30, Andrews, *Contract Law* (n 207) 596, 598; Both Davies and Andrews submit that the implied terms methodology would be the most appropriate method for dispute adjudication, guided by commercial necessity and basic understanding of minimum levels of fair dealing. Austen-Baker, *Implied Terms in English Contract Law* (n 709) 58 further clarifies that the implication in fact is the preferred approach adopted by the courts, rather than in law. In contrast, Simon Crabtree, 'Incremental Steps Towards Clarity: Good Faith as an Organising Principle Behind the Implication of Terms in Fact' (2019) 1 Journal of Commonwealth 141, 155, 163, 172, argues that despite implied terms serving the protection of the reasonable expectations of the parties reasonably well, an explicit recognition of a highly contextual principle of good faith is still required in order to correct the inconsistencies in the law's development, notably in the context of contractual discretions. His understanding of a general principle of good faith is however derived from the parties' reasonable intentions, either through implication in fact or construction.

of commercial common sense, the role of implication will be reduced to a narrow safety-net role and may disappear altogether where good faith is recognised as a principle and positive duties can directly emanate from a contextual interpretation of the contract. If the parties have failed to accommodate for a foreseeable risk through an express term, the tests do not help in deciding whether it would be unjust to correct the allocation of risk or whether to leave the loss lie where it falls.[829] Interpretation, using a contextual lens, reveals what parties would have agreed as to risk allocation had they foreseen the scenario, decided against a commercial common-sense reading of the contract; while implication in fact can only supply a term where a genuine lacuna remains and that term reflects what parties obviously would have bargained for. As such, implied terms are not suitable for addressing all types of incompleteness in contracts, but only those where the silence prevents the contract's purpose from being realised. The implication of a term would be justified to address the issue of unfair advantage taking of the presence of a gap.[830] Such advantage is unfair only if one party had not expressly bargained for or paid for it. Consequently, where the contract contains a critical gap, it will not always be filled 'by asking solely whether a proposed implied term is necessary to give effect to what a reasonable person would understand the contract to mean, in circumstances when it was not expressly said.'[831] Indeed, it may be that 'nothing is to happen and that this is what the contract means.'[832]

3.3. Contractual Discretions

Where a contractual right is conferred upon a party in a contract, the motive behind exercising the right is generally regarded as irrelevant in English law. In *White and Carter (Councils) Ltd v McGregor*, Reid LJ famously said that 'it never has been the law that a person is only entitled to enforce his contractual rights in a reasonable way and that a court will not support an attempt to enforce them in an unreasonable way.'[833] This stems from English law's

[829] Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 319.
[830] ibid.
[831] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 473.
[832] ibid 474, citing Lord Hoffmann in *Attorney General of Belize* (n 687).
[833] [1962] AC 413 (HL) 1183; although a Scottish decision, the English courts' later stance has been to adopt the 'White & Carter principle', see Qiao Liu, 'White & Carter Principle: A Restatement' (2011) 74(2) MLR 171, 172. The case concerned a three-year contract for advertisement display between a company supplying litter bins to local councils and a business which required advertisement to be displayed on such bins. The latter cancelled the contract on the same day of contracting. The claimant proceeded to display the advertisements as contracted for and brought a claim for the contract price after the defendant defaulted in all of its initial payments. The court reiterated that in cases of anticipatory breach, the innocent party had an unfettered option as to whether to accept the breach or not. However, Lord Reid presented two exceptions to that rule. The first exception related to cases where the innocent party could not perform the contract without any cooperation from the other side (which did not apply here); the second exception was where the innocent party had no legitimate interest in performing the

utmost respect for the sanctity of the bargain and its desire for certainty in the adjudication of commercial dealings.[834] Yet, the courts have progressively developed limits on the exercise of contractual rights in the context of contractual discretions. Some contractual provisions might allow a party to use its discretion in performing the contract. Contractual discretions may be adopted for various reasons, including efficiency in adapting to future uncertainty; economic and reputational constraints on abuse; compensatory pricing; and in some cases, reciprocal allocations of discretion.[835] It is hard to imagine that parties would agree to an unfettered contractual discretion. Whether this discretion is subject to any restriction and, if so, its extent, have been the subject of case law and academic debate.

In *Equitable Life Assurance Society v Hyman*, the House of Lords gave an important decision on contractual discretions.[836] The case concerned the interpretation of the claimant company's standard form policies and its articles of association. The company had sought to exercise a principle of granting different final bonuses to their 'with-profits' retirement annuity policyholders, whose policies contained a provision for guaranteed annuity rates, the calculation of which depended on whether the policyholder elected to take the annuity at the higher guaranteed rate or the lower current rate. The company relied on their articles of association, which, they argued, conferred upon them the discretion to override the guaranteed annuity rate. The court held that the company could not exercise discretion in a way which was contradictory to the intention of the instrument conferring it, therefore, the company's practice was in breach of contract, and their articles of association should have been read as conferring discretion subject to the reasonable expectations of the policyholders.[837] Such expectations were that the policyholders would benefit from their choice of a guaranteed rate if the market fell.[838] The court considered that it was strictly necessary to imply a restriction in the company's articles of association to preclude the use of the directors' discretion in an unfettered way.[839] Consequently, the court took a contextual business common sense approach to implication, by

contract except to claim damages (which applied here, and resulted in a decision against the defendant who could not prove a legitimate interest in keeping the contract alive).

[834] See chp 1.2.1.

[835] These were identified by Collins, 'Discretionary Powers in Contracts' (n 565) 219, 226-231.

[836] 4 [2002] 1 AC 408 (HL).

[837] ibid 459 (Lord Steyn).

[838] ibid 449 (Lord Woolf MR).

[839] ibid 459 (Lord Steyn) in particular, Lord Steyn's approach to construction was to consider implication as a sub-category of construction, rather than make references to the traditional tests for implying terms in fact.

referring to the guaranteed annuity rates being a good selling point in the marketing of the policies.[840]

In a later case, in *Paragon Finance*, the Court of Appeal held that the lender's discretion to set rates was fettered in regard to two residential mortgages, stating that such rates 'should not be set dishonestly, for an improper purpose, capriciously or arbitrarily.'[841] An example of capricious reasoning is where a lender raises the rate of interest because its manager did not like the colour of the borrower's hair.[842] As to the fettering of the discretion with reference to a reasonableness criterion, the court referred to Leggatt LJ's decision in *Abu Dhabi National Tanker Co v Product Star Shipping Ltd (the Product Star)(No 2).*[843] The case concerned a charterparty contract under which the master and the owners had a discretion in determining whether any port to which the vessel was ordered was dangerous. Leggatt LJ had stated that 'not only must the discretion be exercised honestly and in good faith, but (...), it must not be exercised arbitrarily, capriciously or unreasonably.'[844] Usually, the concepts of arbitrariness, irrationality, perversity or capriciousness are deemed to be effectively the same in that they all defy reason one way or another.[845] In the circumstances, the owner had acted unreasonably in the way he had exercised his discretion. The court arrived at the decision not by implication in fact but by interpreting the contract, by 'having regard to the provisions of the contract by which [the power] is conferred.'[846] In *Paragon Finance*, Dyson LJ agreed with the reasoning of Leggatt LJ in *The Product Star* that the standard of reasonableness is that of the administrative law's *Associated Provincial Picture Houses Ltd v Wednesbury Corporation (Wednesbury)* unreasonableness.[847] However, the standard was then implied into the contract in *Paragon Finance,* rather than being adopted as a tool for interpretation as in *The Product*

[840] ibid.
[841] *Paragon Finance* (n 583) [36] (Dyson LJ).
[842] ibid [31].
[843] [1993] 1 Lloyd's Rep 397 (CA) 404.
[844] ibid; in *Socimer* (n 156) [66], this test was later referred to by Rix LJ as being one of 'rationality'. In borrowing from criminal law in the context of interpreting banking contracts in *Lehman Brothers International (Europe) (in administration) v Exxonmobil Financial Services BV* [2016] EWHC 2699 (Comm) [2016] 2 CLC 578 [277], Blair J relied on the distinction made between rationality and reasonableness in *Hayes v Willoughby* [2013] UKSC 17, [2013] 1 WLR 935, whereby reasonableness was deemed to be an objective standard applied to 'the outcome of a person's thoughts or intentions.' In contrast, rationality requires 'a minimum objective standard to the relevant person's mental process', and 'imports a requirement of good faith' to avoid arbitrariness, capriciousness or perversion in the decision-making process (Lord Sumption SCJ in *Hayes* himself referred to *Socimer* (n 156) [14]).
[845] Hooley (n 456) 77-78.
[846] *The Product Star* (n 843) 404.
[847] [1948] 1 KB 223 (CA). *Paragon Finance* (n 583).

Star.[848] The implication must be necessary to give effect to the reasonable expectations of the parties, and applying the officious bystander test the parties would have said, if asked at the time of contracting whether discretion could be exercised dishonestly, for an improper purpose, capriciously or arbitrarily, the parties would have said 'of course not.'[849] As such, the rates set could have been unreasonable, but not so unreasonable that no reasonable lender would charge as such.[850]

The Court of Appeal later took the opportunity in *Socimer* to revisit the law on contractual discretions.[851] The case concerned a dispute on the termination of a contract between two banks for the forward sale of securities. The contract expressly provided for the seller to value the portfolio of assets at the termination date and give credit for retained securities belonging to the buyer, which the seller failed to do. Instead, the defendant seller realised the assets over time and credited the claimant with the proceeds. The claimant buyer defaulted and went into liquidation owing money in respect of the forward sales securities which it had bought. The court held that an implied term to fetter the defendant's discretion on valuing the assets was not necessary or sufficiently certain and therefore could not be implied. This was because the contract was a carefully drafted one, and the claimant's own proposed implication could take two different forms. The first one was to restrict the defendant's discretion on valuation of the assets subject to requirements of good faith, and the second one to impose an independent and objective true price criterion for the valuation of the assets. In essence, the court's fettering of contractual discretion was made subject to a good faith criterion.[852] However, for good faith to operate, there must not be a binary choice. Indeed, in a

[848] *Paragon Finance* (n 583) [36]. Peden, 'When Common Law Trumps Equity: The Rise of Good Faith and Reasonableness and the Demise of Unconscionability' (n 455) 15. Although some authors contend that the implication in *Paragon Finance* was an application of the 'proper purpose test,' such test is usually restricted to the exercise of powers held by fiduciaries such as trustees or directors, see David Pollard, 'Exercising Powers: Proper Purposes rather than Best Interests: Fiduciaries and Eclairs' (2016) 30(2) Trust Law International 71, 73, and see Davies and Sales, 'Controlling Contract Discretions: Wednesbury Reasonableness, Good Faith and Proper Purposes' (n 663) 127, 128.

[849] *Paragon Finance* (n 583) [36].

[850] Jeannie M Paterson, 'Implied Fetters on the Exercise of Discretionary Contractual Powers' (2009) 35(1) Monash University Law Review 45, 60, argues that it is possible to distinguish between an implied duty not to exercise discretionary powers for an *improper purpose* and an implied duty not to exercise discretionary powers *unreasonably*. The latter would relate to instances where the subjective motives of the decision maker were made for a proper purpose but the decision was objectively unreasonable (that no reasonable person would have made the decision). In practice, this would only arise where an egregious decision was motivated by an improper purpose but the evidence of the motive is not available.

[851] *Socimer* (n 156). *Socimer* was also later applied in the banking context of interpreting repurchase transactions in *LBI EHF v Raiffeisen Bank International AG* [2018] EWCA Civ 719, [2018] 1 CLC 548, [38] (Flaux LJ), where the Court of Appeal held that in the absence of an express or implied limitation in the exercise of a discretion, the only limitation would be that 'the decision-maker must have acted rationally and not arbitrarily or perversely.'

[852] *Socimer* (n 156) [116] (Rix LJ).

later case, in *Medirest,* the Court of Appeal distinguished *Socimer* and held that where a contractual discretion amounts to a binary decision as to whether or not to exercise an 'absolute contractual right', then there would be no implied term that the party must take that decision not in an 'arbitrary, irrational or capricious manner'.[853] In contrast, the court's approach in *Socimer* was to view good faith as implicit to all commercial contracts, the use of express language requiring it being rare.[854] There is no indication that Rix LJ in *Socimer* was referring to an implication of good faith under the traditional tests; rather, good faith is seen to be inherent in the standard of behaviour of contracting parties, safeguarding against 'abuse caused by self-interest.'[855] A distinction was made with 'objective' reasonableness, in contrast to a *Wednesbury* unreasonableness. The 'objective' one would arise in instances where a term was to be implied under the traditional tests requiring the fixing of a reasonable price or a reasonable time.[856] The reference to objectivity is confusing; the assessment of the reasonableness of a party's exercise of its discretion assumes that the courts would fetter the exercise where the party's decision is outside of the range of reasonable responses in the circumstances of the parties, which can only be assessed against an objective criterion. In the commercial law context, the standard of *Wednesbury* reasonableness should in fact refer to an objective formula encompassing the reasonable expectations of the parties.[857]

Where reasonableness is in issue, it may be hard to determine what will constitute what is reasonable in the circumstances. In *Barclays Bank plc v Unicredit Bank AG (formerly known as Bayerische Hypo-und Vereinsband AG),* the court had to interpret an express term requiring the exercise of a right to be made in a 'commercially reasonable manner.'[858] The court had to determine whether a party's refusal to consent to the early termination of guarantees it had given for loan portfolios had been 'commercially reasonable' under the contract. In interpreting the clause, the court said that the result did not have to be commercially reasonable, 'although, if it is not, that would no doubt cause one to look critically at the manner of the

[853] *Medirest* (n 97**)** [91], [92]. *Socimer* (n 156) was distinguished on the basis that the contract permitted one party to value a portfolio of securities, which was a decision that affected both parties and was not a binary decision as to whether or not to value the porfolio [83].
[854] *Socimer* (n 156) [116].
[855] ibid. Campbell, *Contractual Relations: A Contribution to the Critique of the Classical Law of Contract* (n 352) 148, also considers that '[a]s a general concept of an implied undertaking not to take opportunistic advantage in ways that could not have been contemplated, and therefore provided for, at the time of negotiation, good faith is inherent in contract as such.'
[856] *Socimer* (n 156), the implication was not found to be necessary in the case, [121] (Rix LJ), [157] (Lloyd LJ), [158] (Laws LJ).
[857] Steyn (n 4) 433-434; Cora Chan, Ernest Lim, 'Problems with *Wednesbury* Unreasonableness in Contract Law: Lessons from Public Law' (2019) 135 LQR 88 , 97.
[858] [2014] EWCA Civ 302, [2014] 1 CLC 342.

determination.'[859] Further, the court's test for commercial reasonableness was that 'the party who has to make the relevant determination will not be acting in a commercially reasonable manner if he demands a price which is way above what he can reasonably anticipate would have been a reasonable return from the contract into which he has entered and which it is sought to terminate at an early date.'[860] The court conceded that the party exercising the discretion was entitled to look after its own interest.[861] Although no references were made to good faith in the case, the fettering of the discretion followed the reasoning of the decisions in *Paragon Finance* and *Socimer*.[862]

Although in the employment law context, the court in *Braganza*, considered the reasonableness requirement in contractual decision-making.[863] An employee of the defendant had disappeared from a vessel in the course of his employment, and the cause was unknown; the most plausible explanations being accident or suicide. The employer refused to pay the widow death benefits under the employee's contract of employment. In refusing, the employer relied on an express clause in the contract which provided the employer discretion to refuse a payout if it deemed that the death had resulted from the employee's 'wilful act, default or misconduct.'[864] The court implied a fetter on how the right of the defendant was to be exercised under the contract. However, the basis for implication was not identified.[865] The court equated the standard of the exercise of a discretion conferred under a contract to be that of *Wednesbury* unreasonableness.[866] As such, the decision did not have to be objectively reasonable. Reasonableness was said to apply both to the 'decision-making process' and the 'outcome.' The defendant was held to have failed on the former limb of the test. The decision must not have been so unreasonable that no reasonable decision-maker could have reached it. This does not mean that the party should not take its own commercial interests into account. The courts have indicated that the fettering of the discretion does not apply to the exercise (or not) of contractual rights, such as to terminate a contract, where the choice is binary, but only to instances where the party makes 'an assessment or choos[es] from a range of options, taking into account the interest of both parties.'[867] However, the adoption of a full *Wednesbury*

[859] ibid [15].
[860] ibid [19].
[861] ibid [22].
[862] *Paragon Finance* (n 583), *Socimer* (n 156).
[863] *Braganza* (n 583) [17].
[864] ibid [1].
[865] Chan and Lim (n 857) 19-20 contend that the implication was not in law, but rather was made on the basis of the parties' reasonable expectations which were objectively assessed in order to control abuse of power.
[866] ibid 37, 103.
[867] *Medirest* (n 97) [83] (Jackson LJ).

unreasonableness test in the exercise of contractual discretions has not been generalised in application to all contracts.[868] It has been criticised that contract law should not rely on public law concepts; instead, it should develop and use its own doctrines, such as that of the equitable principle of 'fraud on power,' also known as the 'proper purpose rule.'[869] The issue, of course with the application of such doctrine, is that it is borrowed trust and company law, where the control of the discretion relates to a fiduciary, such as that of a company director; whereas commercial parties do not operate as each other's fiduciary in the context of arm's length contracts.[870]

The courts' references to reasonableness alongside their assessment of good faith are confusing and ill-informed. Indeed, where reasonableness is equated to *Wednesbury* reasonableness, the courts assessment of the standard of conduct should be made exclusively on an objective basis. In *SNCB Holding v UBS AG*, Cooke J had clearly stated that a duty of good faith is understood as implying 'subjective honesty, genuineness and integrity, not an objective standard of any kind, whether reasonableness, care or objective fair dealing.'[871] The defendant had exercised a contractual right in a funding agreement to replace higher-value bonds held in a collateral account with lower-value ones. Although this was advantageous to the defendant, it was against the interests of the claimant. The claimant argued that when the reasonable expectations of the parties are taken into account, there would operate an implied term to prevent the defendant from acting in the way it did. The court refused such reasoning and provided that no such term could be implied, the good faith being restricted to an honest belief in an entitlement to exercise the contractual right.[872] As such, the court's reasoning was restricted to a subjective assessment of the defendant's state of mind. Dyson LJ's line of questioning in *Paragon Finance* clearly reflected the courts' general distinction drawn between a subjective good faith and an objective standard of reasonableness:

> [i]t is one thing to imply a term that a lender will not exercise his discretion in a way that no reasonable lender, acting reasonably, would do. It is unlikely that a

[868] Wayne Courtney, 'Reasonableness in Contractual Decision-Making' (2015) 131 LQR 552, 555; Hooley (n 456) 73.
[869] Davies, 'Excluding Good Faith and Restricting Discretion' (n 585) 105.
[870] *Eclairs Group Ltd v JKX Oil & Gas Plc* [2015] UKSC 71, [2016] 3 All ER 641 [30] (Lord Sumption SCJ) stated that '[t]he proper purpose rule is a principle by which equity controls the exercise of a fiduciary's powers in respects which are not, or not necessarily, determined by the instrument.'
[871] [2012] EWHC 2044 (Comm) [72], in this context, the court refers to 'utmost good faith' being specific to insurance law and encompassing objective standards of conduct in contrast to 'good faith' in commercial contracts.
[872] ibid [112], there was no evidence of dishonest behavior in the circumstances.

> lender who was acting in that way would not also be acting either dishonestly, for an improper purpose, capriciously or arbitrarily. It is quite another matter to imply a term that the lender would not impose unreasonable rates.[873]

The court's decision was informed by the necessity to give effect to the reasonable expectations of the parties; there was an implied term that 'the claimant would not set rates of interest unreasonably in the limited sense (...) described.'[874] However, it is argued that the distinction the courts draw between a restrictive subjective good faith and an objective reasonableness is confusing and unwarranted.[875] The honesty element of good faith, which is recognised by the courts, relates to the belief of the party that he acted in a proper way. The assessment necessarily is made against an objective criterion of honesty, and does not involve an assessment in a vacuum. The belief may well be honest, however the materialisation of it in the external world may be contrary to an objective criterion of honesty, and it is argued that it is the latter assessment which should be relevant for good faith in contractual performance as an inquiry into the mind of the party is not reliable. Furthermore, the separation of reasonableness from the assessment of good faith is unnecessary where good faith is stripped from its subjective nature and only an objective good faith remains. This would also alleviate any concerns in regards to subjective and objective debate which in essence seeks to address abusive exercise of contractual discretions. Such an approach would also be in line with an understanding of good faith as a normative concept, as argued herein, which already encompasses adherence to the reasonable expectations of the parties.[876] Where the courts already make a reference to decisions being reasonable because they are made for instance for genuine commercial reasons, or where it is commercially necessary, these evaluations inevitably touch on the contractual expectations of the parties, and anything which betrays the reasonable expectations of the parties would also be 'unreasonable' in the objective sense as envisaged by the courts.[877]

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[873] *Paragon Finance* (n 583) [41].
[874] ibid [42].
[875] Indeed, Dyson LJ's analogy with the *Wednesbury* reasonableness in earlier cases such as that of *Paragon Finance* was criticised as being questionable for providing necessary authority; rather it was argued that the correct approach would have been to adopt a purposive interpretation of the contract to prevent abuse of discretionary rights for an improper purpose, see VK Sims, RJ Goddard, Controlling Contractual Discretion (2002) 61(2) The Cambridge Law Journal 268, 270-271.
[876] Hesselink (n 250) 620 argues that '[i]n all systems objective good faith is usually regarded as a normative concept. Indeed, good faith is often seen as the highest norm of contract law, or of the law of obligations or even of all private law.'
[877] Collins, 'Discretionary Powers in Contracts' (n 565) 245, 'what is regarded as irrational or perverse is an exercise of discretion that falls outside the reasonable expectations of the subject of the power (...).'

In sum, courts seek to prevent unfettered discretionary contractual powers that are inconsistent with the reasonable expectations of the parties. Such expectation is presumed to be that rational parties would not have consented to a discretionary contractual power being exercised for reasons contrary to the purposes for which the power was granted or in an unreasonable and arbitrary manner.[878] Although the principles on the restriction of discretions have been implied in fact or through interpretation of the contract, it may be said that they have become terms implied in law.[879] As such, even where the contract does not provide for an express duty of good faith, the court is likely to subject the exercise of a discretion provided in the contract to a good faith check. Lord Leggatt SCJ is correct in arguing that there is no difference between the exercise of an express contractual power and that of a freedom which exists because the contract does not exclude it.[880] Where the courts are open to subjecting the exercise of express contractual discretions to a requirement of good faith, by the same token it would not be a big step to subject the freedoms of the parties in exercising their contractual rights to the same good faith requirement. If express contractual powers are subject to a good faith requirement, it would be illogical not to extend such requirement to the rest of the powers in the contract, even where the parties have not expressly provided for it. For instance, if the court considers a term must be implied by necessity, the same requirement of good faith would be imposed upon exercise of the term. It would not mean that a good faith duty has been implied into the contract, but rather that the implication of the term necessary for the contract to make business sense has been subjected to a good faith check which applies by default to the exercise of rights in the contract. This is because, in the long term, it is likely that the category of contractual discretions is bound to expand by case law.[881]

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[878] Paterson, 'Implied Fetters on the Exercise of Discretionary Contractual Powers' (n 850) 52. See further discussion on rational choice theory in chp 4.2.

[879] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 18, 333, 353-354; Leggatt, 'Contractual Duties of Good Faith' (n 248) 14-15, suggests that 'implication has now hardened into one of law' and the good faith restriction on the exercise of contractual discretions has indeed become a 'general default rule.' For an opposite view, see Davies and Sales, 'Controlling Contract Discretions: Wednesbury Reasonableness, Good Faith and Proper Purposes' (n 663) 125, who argue that good faith should not be implied in law to all contracts where one party has a discretionary power over the other. They contend that 'this is so broad that it is unhelpful, and it is inappropriate to imply at law duties of good faith in circumstances where such a term could not be implied in fact.'

[880] Leggatt, 'Contractual Duties of Good Faith' (n 248) 16.

[881] This approach would also bring a more coherent explanation to the law on repudiatory breach which struggles with a rationale based on reasonableness and legitimate interest. See for instance the different reasoning used by Leggatt J in the High Court, and the Court of Appeal in *MSC Mediterranean Shipping Co S.A.* (n 49), Leggatt J preferring an approach where he held that the innocent party could not exercise its power to keep the contract alive if to do so would be 'wholly unreasonable,' applying the 'legitimate interest' test in *White & Carter (Councils) Ltd v McGregor* [1962] AC 413.Whereas the Court of Appeal decided that the right to keep the contract alive was not fettered despite the innocent party's repudiatory breach, the contract had come to an end automatically by the innocent party's repudiatory breach, due to the commercial purpose of the contract having

On an alternative view, it can be argued that the recourse to implied terms for fettering the exercise of contractual discretions in contracts is an artificial construct.[882] Rather, the fettering should be done through the interpretation of the contract, with an understanding that good faith is implicit in contract law. This would also bypass the requirement for implied terms of being necessary in the relevant type of contract. If good faith is implied in law to all contracts, the criticism might be that each type of contract has different policy considerations; therefore, it would not be possible to hold that all contracts, or commercial contracts, are implied to have a good faith requirement.[883] Indeed, a contextual interpretation of the contract would be able to take into account the parallel frameworks in which contracting parties operate as identified by Collins.[884] The first framework relates to the written contract itself, the second framework is the economic relation within which the contract is grounded and provides the 'wealth-enhancing reasons' to the contract. The second framework posits the parties as rational parties driven by self-interest. The third framework is the trust between the parties which emanates from the social interactions in respect of the trade 'including personal contacts and the history of the connection between the parties.' Moving from the premise that parties are rational actors, they are deemed to want to preserve the trust and avoid being regarded as acting in bad faith. It is the second and the third framework which inform the decisions undertaken in regards to the execution and performance of the first framework, which is the binding contract. The frameworks are useful in our understanding of contracts in that written contracts in themselves are not sufficient in gauging the motivations and expectations of the parties. The fettering on the exercise of contractual discretions, viewed with the frameworks in mind, can be understood as legal responses to the presence of such frameworks; even though, as Collins admits himself, this view is not entirely in the legal practice of the courts.[885] The task of weaving together all three frameworks is best accomplished by reference to the reasonable expectations of the parties, which cannot be entirely reflected in a written document. The multidimensional nature of such expectations requires that a document, written mainly as a guarantee that the parties' deal will have legal force in case the contract is not performed as

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been frustrated. The Court of Appeal accepted (in obiter) that even if it were possible for the innocent party to affirm the contract, it would have had no 'legitimate interest' in going so. However, the Court of Appeal declined recognising a duty of good faith in fettering the parties' exercise of their rights.

[882] Peden, 'When Common Law Trumps Equity: The Rise of Good Faith and Reasonableness and the Demise of Unconscionability' (n 455) 16 argues that the standard of fettering required by good faith would be 'be honesty, loyalty to the contract and a requirement to consider the interests of the other party.'

[883] Elisabeth Peden, 'Incorporating Terms of Good Faith in Contract Law in Australia' (2001) 23(2) Sydney Law Review 222, 230.

[884] Collins, 'Discretionary Powers in Contracts' (n 565) 250-251.

[885] ibid 252-253.

agreed, cannot possibly address all the questions which may arise in regards to performance. Good faith, as a flexible concept, can provide the gateway to claw back the relevant and necessary elements from such frameworks by reference to the parties' reasonable expectations.

3.4. Conclusion

The issue with the classification of contracts for implying good faith duties in law is that, outside of those categories, where good faith duties are automatically implied, there would have to be recourse to the restrictive device of implication of good faith duties in fact, depending on the circumstances of each case. Clearly, rather than a cohesive approach to the regulation of unfairness, this approach continues to contribute to the fragmented state of affairs. Even if the implication in law to certain categories were to be adopted, whether relational contracts, networks of contracts, or RGSCs, any contract falling outside of such categories would be at the mercy of existing ways of curbing opportunistic behaviour in contractual performance. The same criticism can be made of the application of good faith duties to the exercise of contractual discretion. Where the case does not relate to contractual discretions, then again, there may potentially be a vacuum in the regulation of unfair behaviour. Another way in which a more comprehensive application of good faith in contract performance could be adopted is if good faith were to operate as an interpretative principle, as suggested by case law and doctrine in the case of contractual discretions. We shall now investigate such a claim.

CHAPTER 4: GOOD FAITH AS A RULE OF CONSTRUCTION

4.1. Introduction

Where the implication of good faith is restricted in English law as discussed in the previous section, the construction of contracts can be better suited to overcoming the severe limitations of classical contract law theory. Relational contract theory provides that a contextual understanding of the contract is necessary to justify the legal force enjoyed by contracts.[886] The classical contract theory's view of the contracting parties as adversaries is not in fact incompatible with the tenets of relational theory. Parties are understood as self-interested in either theory because the institution of contracting would not operate without the fundamental underlying norms of honesty and reciprocity, where both parties expect to obtain a benefit out of the contract in exchange for sacrificing something of value.[887] Promoting fair dealing and deterring opportunistic behaviour in contract performance is another way of expressing Steyn's proposal for contract law to uphold 'the reasonable expectation of honest men.'[888] Ignoring the context of the contract severely restricts such an endeavour. However, fully embracing a relational approach without reference to objective criteria can lead to arbitrary and inconsistent decisions.[889] Instead, the framing of contractual parties as rational actors should be the basis upon which the pursuit of their self-interest in contracts must be understood. This would allow an objective interpretation of the surrounding context of the contract without succumbing to the criticisms of a subjective and haphazard process of the relational contract theory, nor to the harsh outcomes which may arise out of the strict application of classical contract theory.[890]

4.2. Good Faith as a Rule of Construction?

[886] Zoe Gounari, 'Developing a Relational Law of Contracts: Striking a Balance between Abstraction and Contextualism' (2021) 41 Legal Studies 177, 182.
[887] Honesty underlies doctrines such as misrepresentation or mistake, whereas reciprocity underlies the doctrine of consideration, see Macneil, Values in Contract: Internal and External (1983) 78 Northwestern University Law Review 340.
[888] Steyn (n 4).
[889] Gounari (n 886) 184 gives the examples of *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 WLR 896 (HL) and *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 (HL), where the courts have used a different framework for assessing context when interpreting the contract, where in the former case, the relevant context was that of business common sense, and in the latter it was the industry practice.
[890] See eg *Arcos Ltd v EA Ronaasen & Son* [1933] AC 470 (HL) where the House of Lords upheld the buyer's strict right to reject goods for not complying precisely with their description in the contract, despite being of merchantable quality and fit for purpose.

Implication vs Interpretation

The process of implying a term and the construction of a term are not the same.[891] The first one relates to issues which may not have been thought out by the parties at the time of contracting, and completes the contract as an extension of the parties' presumed intention.[892] The process of construction revolves around terms set out in writing, which seek to clarify ambiguities in their meaning. The parties have put their minds to the issue at the time of contracting, but failed to properly reflect their intention in the contract. If need be, the court can even order rectification to correct an error in the document.[893] The methodology used is acknowledged to be that the courts first start with determining the express terms, before moving on to finding any implied terms.[894] However, there is no obligation upon the parties to provide for all eventualities in express terms. If there were, 'there would be very little to the law of contract.'[895] Indeed, '[a] principal function of contract law is to provide a framework of rules which apply to contractual relationships unless the parties expressly opt out of them.'[896] There may be communalities between implication and interpretation but as Lady Hale stated in *Byron v Eastern Caribbean Amalgamated Bank*, construction 'involves deciding what the parties meant by what they did say' while implication 'involves deciding whether they would have said something that they did not in fact say had the matter occurred to them.' [897] In any case, a term cannot be implied if it is inconsistent with an express term.[898] The inconsistency can be explicit, where linguistically the proposed implied term clashes with the meaning of the express term. The inconsistency can also be implicit, where the proposed implied term contradicts the

[891] The terms construction and interpretation are used interchangeably in this thesis, and the process of implication is seen as separate to that of construction or interpretation.
[892] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 459, contends that freedom of contract and party autonomy ultimately underlie the process of contract interpretation, implying that the shift has been at the expense of other normative considerations such as fairness.
[893] The requirements for rectification were succinctly summarised by Peter Gibson LJ in *Swainland Builders Ltd v Freehold Properties Ltd* [2002] EWCA Civ 560, [2002] 2 EGLR 71 [74] as being '(1) the parties had a common continuing intention, whether or not amounting to an agreement, in respect of a particular matter in the instrument to be rectified; (2) there was an outward expression of accord; (3) the intention continued at the time of the execution of the instrument sought to be rectified; (4) by mistake, the instrument did not reflect that common intention.'
[894] This is sometimes referred to as the sequential approach, see for instance *Marks and Spencer* (n 658) [28] (Lord Neuberger SCJ), and *Trump International Golf Club Scotland Ltd v The Scottish Ministers* [2015] UKSC 74, [2016] 1 WLR 85 [35] (Lord Hodge SCJ). The opposite is an iterative approach where the processes of construction and implication are carried out together, as an objective interpretation of the contract as a whole, see McKendrick, *Contract Law* (n 1) 198. For an overview, also see Hogg (n 697) 1672-1673.
[895] *Barton* (n 486) [126] (Lord Leggatt SCJ).
[896] ibid.
[897] [2019] UKPC 16 [22].
[898] *Carewatch* (n 3) [110].

substance of the express terms of the contract without necessarily being linguistically inconsistent.

What is clear is that the process of interpretation concerns the parties' manifested intention in a contractual document. The objective theory of contractual interpretation dominates judicial interpretation of contractual documents.[899] While at times this may also correspond with the parties' actual intention, the law of contract will always be concerned with the incarnation of intention in the contract. Even where the parties' subjective mindset would be relevant, for instance in cases of mistake, fraud, or duress, the court will be limited in its inquiry to the evidence presented by the parties and its objective assessment. The more unreasonable the meaning arrived at through interpretation, the less likely that the parties will be held to have meant it. This approach admittedly seeks to arrive at a fair decision, without claiming good faith as its legal basis, but it should. In short, the parties will do best to spell out any unreasonable deviation from the natural and ordinary meaning of words.[900]

The Paradox of Objectivity in Contractual Interpretation and Rational Choice Theory

The reasonable person, a legal fiction, is the cornerstone of contractual interpretation.[901] The reasonable person's understanding of the contract is conclusive, and in the context of commercial contracts, the reasonable person is a business person.[902] It may be subject to criticism that such standard is not objective enough. Indeed, Leggatt, writing extra-judicially, presents a paradox which is that on one hand the court must figure out the parties' intentions objectively, but on the other the court must do so without inquiring into their subjective states of mind. [903] The first solution may be to say that English law restricts admissible evidence from which the court can infer the parties' intention, and as such, only external manifestations of the

[899] Richard Calnan, *Principles of Contractual Interpretation* (3rd edn, Oxford University Press 2017) 16-19.
[900] *Carewatch* (n 3) [91] the court rejected the defendants' understanding of 'business' and 'services' provided for in the contract as to mean only those as developed and in existence at the time of contracting, stating that such an interpretation, although linguistically possible, would 'fly in the face of commercial common sense.' The court considered there was no 'sensible reason' why the parties would adopt such a rigid approach where the agreement was for a minimum of seven years, and the provision of care and support services were inherently of an ongoing nature which might need to be adapted to changing circumstances. The takeaway of this conclusion is that had the parties wished for a rigid clause, they should have made it clear in the contract.
[901] Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 28.
[902] ibid 38.
[903] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 454.

parties' intent can be taken into account.[904] On this view of interpretation, the contract is seen as a psychological evaluation of the parties' intent.[905]

A distinction is drawn between words, as would be conventionally defined in a dictionary, and words understood against the relevant background to the parties' deal, the latter inevitably calling on the assessment of a reasonable person.[906] The reasonable person's assessment would be limited to the information available to the parties when they entered into the contract.[907] The issue with this first solution is argued to be that there is no common intention of the parties; there may be as many intentions as the number of parties to a contract. It would thus be crucial to focus the investigation on the shared intention rather than coincident intentions.[908] Shared intention would entail a mutual understanding each other's intention which has been communicated to the other confirming that they share the same intention. Express terms would usually reflect such shared intentions. However, the ascertaining of the shared intention involves the risk that different interpretations would be advanced by the parties in litigation, each disputing the other's suggested meaning.[909] This may be because the parties may not have actually read the contract, and even if they had, they may not have entirely understood it in cases where the contract was drafted by their legal representative. The issue would be even more pronounced in cases of standard form contracts. Further, the parties are unlikely to have considered the full extent of eventualities, and even a detailed and well-thought-out contract would fail to provide for all eventualities in most circumstances. Regardless, effect will have to be given to contracts even where the language used by the parties did not reflect their intention. To argue otherwise would make a limited number of contracts enforceable in which the parties' actual intention was accurately reflected in the contract language. Consequently, interpretation should not be dependent on the parties' meaning of the language used due to the difficulty of ascertaining a shared intention.

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[904] ibid 456.
[905] This is sometimes referred to as the 'psychological theory' of contract interpretation, see David McLauchlan, 'A Better Way of Making Sense of Contracts?' 132 (2016) Law Quarterly Review 577, 579.
[906] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 458.
[907] Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 39, the reasonable person is said to be attributed the common knowledge of the parties, including knowledge of background and purpose; it is 'the reasonable interpreter of the bargain or agreement.'
[908] ibid 461; the latter are defined as the intention of each party which happens by chance to correspond to the intention of the other party. Mounting legal rights and obligations on such an understanding of 'intentions' would necessarily undermine the certainty of contract law.
[909] ibid 462.

Another solution could be to say that the court is concerned with ascertaining the parties' presumed intention, not their actual intention.[910] This is proposed by Leggatt as the rational choice theory.[911] The theory assumes that 'the parties deliberately chose the words of the contract to express a shared intention and that the parties are rational and reasonable people.'[912] It rests on two assumptions. The first is that the language of the contract is deliberately chosen by the parties to express a particular meaning. The intention is presumed to be a condition of the interpretative process, not a result of it.[913] The second assumption is that the contracting parties are rational and reasonable people.[914] As such, the reasonable person's viewpoint is that of the authors of the contract, not the reader of the contract; indeed '(...), I suggest, what English lawyers in fact do when they interpret contractual documents is to assume that the parties themselves, rather than a hypothetical interpreter of their language, were reasonable people.'[915] This topic is further discussed below.[916]

Extrinsic Evidence

The courts have recourse to construction rules or presumptions when interpreting contracts.[917] One of them is the parol evidence rule to deny evidence outside the four corners of the contract. It prohibits adducing evidence to contradict, vary, add to, or subtract from the terms of a written contract.[918] The parol evidence rule relates to the interpretation of the

[910] ibid 456; also noted by Lord Neuberger SCJ in *Marks and Spencer* (n 658) [21] in reference to Lord Steyn's remarks in *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408 that the implication of a term is 'not critically dependent on proof of an actual intention of the parties when negotiating the contract,' but the relevant question is to determine a presumed intention based on what the view of the 'notional reasonable people in the position of the parties at the time which they were contracting.'

[911] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 454.

[912] Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 49.

[913] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 467.

[914] Some commentators make a distinction between a 'reasonable' and a 'rational' person, arguing that rationality is limited to regard for one's own interests, without any for the other party's interests, whereas reasonability involves an outward look beyond one's selfish interests, based on reciprocity and an understanding that they exist in a social world where they the person they engage with also seeks to benefit from the deal, see Han (n 327) 48. However, such a distinction is confusing, unnecessary in contract law because an understanding of the parties as rational necessarily involves an objective appreciation of their presumed intention which an objective 'reasonableness' test is bound to repeat, Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 468.

[915] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 468.

[916] See chp 4.2 '*Reasonableness and Contextual Interpretation*.'

[917] For a list of presumptions of construction which operate across all contracts, see McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657**)** 279-309 (the presumption that a contracting party cannot take advantage of its own wrong, the presumption that clear words are required to exclude or modify remedies that arise by operation of law, the presumption of legality, the presumption against impossibility, the presumption of technical legal usage in document drafted by lawyers, presumption in favour of one-stop dispute resolution).

[918] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 450.

contract. As such it is concerned not with the implication of terms, but with ascertaining the meaning of what is already contained in the document, where the agreement has been reduced to writing. There are certain exceptions to soften the harshness of the rule.[919] For instance, there is a presumption that when a contract is reduced to writing, the parties' intention was to set out their whole agreement in the document. Where the parties use an entire agreement clause, this purports to strengthen such presumption. However, it is accepted that an entire agreement clause is usually inapt at excluding various statutory implied terms or those terms which are necessary to make the contract work.[920] As with all presumptions, this one is also rebuttable. However, to rebut, the party will have to adduce extrinsic evidence. This would only be acceptable where the party sought to evidence terms which were intended to be part of the agreement at the time of contracting, where rectification may be sought. However, most disputes arise because the parties do not agree on a common intention looking retrospectively back to the time of contracting when the term was agreed. The court will then be tasked to resolve the dispute through an objective lens.[921] Where the contract appears complete, it will be for the party seeking to disprove the completeness of the contract to rebut the presumption that the contract is complete. Whether the document looks complete or not will ultimately depend on ascertaining the intentions of the parties, which will be problematic where the parties are arguing opposing views on the completeness of the contract. The courts resort to the viewpoint of the reasonable person to arrive at a decision. Lord Hoffmann's restatement of the law on interpretation is useful in that he confirmed the current approach towards the admissibility of extrinsic evidence to help the interpretation process.[922] Rather than having an ambiguity as a precondition to justify having recourse to extrinsic evidence, the court was of the view that extrinsic evidence is generally admissible in aiding interpretation. As such, '[t]he exclusion of background material from the process of interpretation should be the exception

[919] ibid 451-457, exceptions such as where the document is not intended to be the whole document or in collateral contracts and warranties,
[920] ibid 775.
[921] John W Carter, Michael Furmston, in M Furmston (ed), *The Future of the Law of Contract* (Informa Law from Routledge 2020) 72, 92, this is in contrast to the subjective approach adopted in most civil law jurisdictions where the common intention of the parties is determined subjectively, and only when this cannot be determined, the assessment will be made on the basis of the reasonable person's view. However, the common law also uses a 'subjective indicia of intention' but they 'remain faithful to the purpose of the process' which is an objective one.
[922] See text to n 933 below.

rather than the rule.'[923] Even where an entire agreement clause is used, extrinsic evidence will be admissible.[924]

Reasonableness and Contextual Interpretation

In interpreting contracts, courts usually refer to the natural and ordinary meaning of the words. This rests on the assumption that the parties would have used the words in their conventional sense. Where they make a mistake in the language, or one uses a meaning which is not known to the other, the court may seek to depart from the natural and ordinary meaning, and instead interpret the contract against the background of the parties' dealings. The background to take into account would be limited to what the parties knew or may be taken to have known. However, where it is assumed that the contracting parties are reasonable people, the interpretation may not turn on the actual intention but on the values which the reasonable people in the position of the parties would share.[925] In *Investors Compensation Scheme Ltd v West Bromwich Building Society ('ICS')*, the principles of interpretation were succinctly restated by the House of Lords.[926] Importantly, the court emphasised that interpretation involved ascertaining the meaning of a document from the viewpoint of a reasonable person having all the background knowledge, previous negotiations and subjective intent being excluded from such background knowledge.[927] Rather than being concerned with identifying a fictional common intention of the parties, interpretation is to become concerned with ascertaining the meaning of the words understood by a reasonable person.[928] The object of inquiry is understood to be the objective meaning of the contract, rather than the parties' intentions.[929] The fundamental question was, however the ascertainment of the standard of fair dealing that should apply, namely whether the reasonable person standard was to be dependent or independent from those set by the parties in their contract, expressly or impliedly.[930] The

[923] *Cherry Tree Investments Ltd v Landmain Ltd* [2012] EWCA Civ 736, [2013] Ch 305 [38] (Arden LJ, relying on the approach of the court in *Investors Compensation Scheme Ltd v West Bromwich Building Society* (*ICS*) [1998] 1 WLR 896 (HL)).

[924]*Barclays Bank Plc* (n 858) [27] (Longmore LJ), the entire agreements clauses do not exclude admissible evidence 'about the way in which parties exercise rights given to them by the terms of the contract.' Rather, the exclusion relates to evidence to the effect that 'the terms of the contract are to include any mutual understanding that is not recorded in the contract.'

[925] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 473.

[926] *ICS* (n 923) 912-913 (Lord Hoffmann). These were later relied upon again in *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38, [2009] 1 AC 1101 [14] (Lord Hope).

[927] *ICS* (n 923) 913 (Lord Hoffmann).

[928] Andrew Robertson, 'Purposive contractual interpretation' (2019) 39 Legal Studies 230, 232.

[929] ibid.

[930] Brownsword, 'After Investors, Interpretation, Expectation and the Implicit Dimension of the 'New Contextualism''(n 321) 105, 107, the author contended that 'new contextualism' requires a determination on the reasonableness standards on whether the parties should be acting in an adversarial or a cooperative way, however

court also stated that the referring to the natural and ordinary meaning of the words simply means that the court does not easily assume a linguistic mistake; the departure from the natural and ordinary meaning of the words is justified where it is evident from the background that 'something must have gone wrong with the language.'[931] Lord Hoffmann alluded to a 'fundamental change' taking place in contract law, meaning a move towards common sense principles of interpretation in ordinary life. In the commercial context, this would equate to 'business common sense' with which the reasonable person, having at its disposal all the background knowledge available to the parties generally, would interpret the meaning of the contract.[932]

In *Homburg Houtimport BV v Agrosin Private Ltd (The Starsin)*, Lord Hoffmann refined his restatement of the rule on interpretation of contracts stating that the reasonable person is a 'reasonable person having all the background knowledge which is reasonably available to the person or class of persons to whom the document is addressed.'[933] In further defining the reasonable person, Lord Hoffmann writing extra-judicially, stated that

> 'the reasonable person' is the notional audience, not the notional parties. The reasonable audience will expect parties to a legal document to have said something which, against the available background, makes rational sense, but will not necessarily expect them to have been reasonable in the sense of being fair to each other. It does not matter whether that meaning would have been in some commercial sense 'reasonable' or not.[934]

In a later case, a similar approach was followed where a reasonable reading of the contract was carried out. The case was that of *Chartbrook Ltd v Persimmon Homes Ltd*.[935] Persimmon, bought land from Chartbrook to build flats. They agreed on a fixed price for the land and an additional sum which might or might not be payable contingently upon the price at which Persimmon actually sold the flats. The additional sum would have been payable if the actual price of sold flats exceeded a base figure. The issue was ascertaining the base figure. A literal interpretation of the contract meant that the base price would be the land price, and

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the decision in *ICS* indicated a preference of the court for a 'practice-based' reasonableness standard where the standard was dependent on the contractual dealing, rather than being independent from it.

[931] *ICS* (n 928) 913.

[932] *ICS* (n 928) 912-913. However, over-reliance on 'business common sense' is discouraged as judicial perceptions of it vary, see Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 63.

[933] [2003] UKHL 12, [2004] 1 AC 715 [73] (Lord Hoffmann).

[934] Lennie Hoffmann, 'Language and Lawyers' (2018) 134 LQR 553, 569.

[935] *Chartbrook* (n 935)**.**

Chartbrook would be entitled to payment of an additional sum of the difference between sum received for the land and the price for which the flat was actually sold.[936] From the standpoint of a reasonable reader, this was not a reasonable reading of the contract, because the land price would be an altogether independent price from calculating the actual sales price of the flats. The reasonable reading would be to understand the additional sum to be paid as taking into account the possibility of the rising market of the day where the flats could have been sold for more than the parties' expectation.[937] As such, the interpretation which was adopted was contextual, viewing the words used in a rational way:

> [w]hen the language used in an instrument gives rise to difficulties of construction, the process of interpretation does not require one to formulate some alternative form of words which approximates as closely as possible to that of the parties. It is to decide what a reasonable person would have understood the parties to have meant by using the language which they did.[938]

The contextual approach stresses the idea that words do not have autonomous meanings independent from context; consequently, words' conventional meanings can only be understood given the background context.[939]

Consequently, the context of the deal lies inevitably at the heart of the interpretative exercise.[940] The context includes 'absolutely anything which would have affected how the language of the document would have been understood by a reasonable man.'[941] In *Rainy Sky SA v Kookmin Bank*, the Supreme Court had emphasised that interpretation was a 'unitary exercise,' meaning that the court should look at both the language used and the context of the contract together, not in a preferential manner:

> the exercise of construction is essentially one unitary exercise in which the court must consider the language used and ascertain what a reasonable person (...) would

[936] ibid [8]-[13] (Lord Hoffmann)
[937] Hoffmann, 'Language and Lawyers' (n 934) 570.
[938] *Chartbrook* (n 935) [21] (Lord Hoffmann).
[939] Hoffmann, 'Language and Lawyers' (n 934) 570.
[940] The context is sometimes referred to as 'the matrix of facts' as coined by Lord Wilberforce in *Prenn v Simmonds* [1971] 1 WLR 1382 (HL). He had explained that it is necessary to 'inquire beyond the language and see what the circumstances were with reference to which the words were used, and the object, appearing from those circumstances, which the person using them had in view' (1384). Later in *Reardon Smith Line Ltd v Hansen-Tangen (The Diana Prosperity)* [1976] 1 WLR 989 (HL) 995-996, he further elaborated on the topic by stating that '[i]n a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposed knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.'
[941] *ICS* (n 928) 912–913, the two exceptions being the parties' subjective intent, and evidence of negotiations.

> have understood the parties to have meant. In doing so, the court must have regard to all the relevant surrounding circumstances. If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other.[942]

This was later confirmed by Lord Hodge SCJ in *Wood v Capita Insurance Services Ltd* where the court confirmed that the process was iterative and therefore 'it does not matter whether the more detailed analysis commences with the factual background and the implications of rival constructions or a close examination of the relevant language in the contract' as long as the court takes into account each factor.[943] Regardless of the order of consideration of the terms of the contract and the background information, this still leaves the question of the weight to be given to different outcomes produced by the use of a literal or a contextual approach. The quality of the drafting is sometimes taken into account as a factor in swaying the balance. Where the drafting is not good, the court should be able to depart from the natural meaning of the words:

> the clearer the natural meaning the more difficult it is to justify departing from it. However, that does not justify the court embarking on an exercise of searching for, let alone constructing, drafting infelicities in order to facilitate a departure from the natural meaning. If there is a specific error in the drafting, it may often have no relevance to the issue of interpretation which the court has to resolve.[944]

Although there are no special rules of interpretation applicable to different types of commercial contracts, long-term contracts are recognised as necessitating a flexible interpretative approach to 'best match the reasonable expectations of the parties.'[945]

Regrettably, the Supreme Court's decision in *Arnold*, seemed to move away from the contextual method preferred in *ICS*.[946] Instead, the court insisted on a natural and ordinary meaning approach to interpreting the contractual language, downplaying the significance of

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[942] [2011] UKSC 50, [2011] 1 WLR 2900 [21] (Lord Clarke SCJ).
[943] [2017] UKSC 24, [2017] AC 1173 [12] (Lord Hodge SCJ), discussed further below at text to n 964.
[944] *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619 [18] (Lord Neuberger SCJ). Similarly, in *ICS* (n 928) 913, Lord Hoffmann had stated that an apparent ambiguity in light of the background cannot be resolved by 'attributing to the parties an intention which they plainly could not have had.'
[945] See eg *Total Gas Marketing Ltd* (n 330) 1286 (Lord Steyn). In *Excelsior Group Productions Ltd v Yorkshire Television Ltd* [2009] EWHC 1751 (Comm) 14, Flaux J defended a flexible approach to interpretation for long-term contracts but emphasised that the words must be interpreted objectively at the time of contracting.
[946] *Arnold* (n 944).

the background in the interpretative process.[947] Although the iterative process was not rejected, the court restricted the role of the 'reasonable person' construct to 'ascertain objectively, and with the benefit of the relevant background knowledge, the meaning of the words which the parties used.'[948] The court's understanding of the role of this construct did not extend to an understanding of the contract, where the court would be effectively rewriting the contract.[949] The case concerned the interpretation of a service charge clause in a long lease of a holiday chalet. It was agreed that the charge would be £90 in the first year, rising by 10% per year thereafter. After several years, the charge significantly exceeded the cost of providing the services. On a literal interpretation, the lessee was to pay the increased service charge, regardless of the actual cost of the service. On an alternative reading, the lessee would be required only to pay a fair proportion of the cost of providing the services, up to a maximum of £90 in the first year, that maximum figure rising by 10% each year thereafter. Although it was accepted that interpretation was to be made from the viewpoint of a reasonable reader of the document at the time of contracting, the focus was to be on the natural meaning of the clause. As such, 'the question for the court is not whether a reasonable and properly informed tenant would enter into such an undertaking.'[950] This would risk the rewriting of the contract by the court. Commercial common sense was also underlined, but the court stated that the assessment of it must not be made retrospectively; when the parties make a bad deal, the court is not bound to correct it but to uphold it.[951]

Subsequently, in *Wood v Capita,* the Supreme Court sought to reconcile previous case law.[952] The case dealt with the interpretation of an indemnity clause in a sale of a company contract. After the sale, the purchaser had to pay out monies to customers due to the misselling of products before the sale of the company. The seller of the company refused to indemnify the buyer, arguing that the indemnity clause was triggered only if the customers had lodged a claim with the Financial Services Authority (FSA), which they had not. The buyer itself had contacted the FSA and was told to pay out. The judgment was handed down by Lord Hodge SCJ, with whom Lord Neuberger, Lord Mance, Lord Clarke and Lord Sumption SCJJ agreed.

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[947] ibid [77] (Lord Hodge SCJ) stating that '[t]he purpose of interpretation is to identify what the parties have agreed, not what the court thinks that they should have agreed.' Also see McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 26-28, who suggests that literalism is progressively making way for a more common-sense liberal approach.
[948] *Arnold* (n 944) [77] (Lord Hodge SCJ).
[949] ibid.
[950] ibid.
[951] *Arnold* (n 944) [29], [32] (Lord Neuberger SJC).
[952] *Wood v Capita* (n 943); the general principles of construction as summarised by Lord Hodge SCJ in *Wood v Capita* (n 943) were recently followed in *Phones 4U Limited* (n 757) [651] (Roth J).

The court held that ascertaining the objective meaning of the clause required considering the contract as a whole, 'depending on its nature, formality and quality of drafting, give more or less weight to elements of the wider context in reaching its view as to that objective meaning.'[953] The business common sense was used where there could be rival meanings of the clause. As such, the court would have to refuse a contextual analysis where a document was, for instance, negotiated and prepared with the assistance of skilled professionals. In considering the warranties provided in the same contract by the seller of compliance with regulatory requirements, the court stated that the seller might have had an interest in minimising their exposure to liability by preferring to indemnify claims lodged by customers.[954] The court indicated that:

> [b]usiness common sense is useful to ascertain the purpose of a provision and how it might operate in practice. But in the tug o' war of commercial negotiation, business common sense can rarely assist the court in ascertaining on which side of the line the centre line marking on the tug o' war rope lay, when the negotiations ended.[955]

The issue with such an approach is that it conflates ascertaining the intention of the parties through a subjective lens, whereby the individual considerations of each party would become relevant. Instead, it is the business common sense of the reasonable person which should be adopted. Despite an insistence on a literal approach, the court's taking into account the sophistication of the parties and the presence of warranty clauses in the contract is an indication of a contextual approach. Where the court has seemingly adopted a combined approach to literal and contextual interpretation, its selectiveness in the choice of factors can be criticised. The court explicitly pushed aside any consideration of business common sense. This caused a result which differed from the one which could have been achieved through the lens of the reasonable person looking at the contract with the same background information available to the parties at the time of contracting.[956] The court's view was that '[t]extualism and contextualism are not conflicting paradigms in a battle for exclusive occupation of the field

[953] *Wood v Capita* (n 943) [10] (Lord Hodge SCJ).
[954] ibid [28] (Lord Hodge SCJ).
[955] ibid.
[956] Indeed, in the first instance, Popplewell J had decided in favor of the buyer, *Wood v Sureterm Direct Ltd* [2014] EWHC 3240 (Comm). Popplewell J's approach was contextual in the sense that he considered the purpose of the clause against the background in which the parties operated, namely the regulatory environment in which the buyer had to operate, with potential liabilities arising towards the FSA. The purpose behind the clause was held to be that it was to protect the buyer against such liabilities arising regardless of how they arose [17]. Ultimately, his decision was in line with what made business common sense.

of contractual interpretation.'[957] However, a selective contextualism can be said not to be contextualism at all.

Notwithstanding cases like *Arnold* and *Wood v Capita*, it is likely that a contextual modern approach will become more prevalent in commercial contracts where the courts will identify the intention of the parties from the standpoint of an objective reasonable person, preferring a common-sense reading of the document, and taking into account all the admissible surrounding circumstances regardless of any ambiguity in the wording.[958] This argument may further find support in the fact that the courts' approach to implication to give effect to the presumed intentions of the parties is 'an early form of contextualism.'[959] Arguably, the risk may be that the courts seek to engage in rewriting the contract rather than interpreting it, albeit liberally. The criticism which may be levied against Leggatt's rational choice approach may be that, practically, the outcome does not differ. In *Marks and Spencer*, Lord Neuberger SCJ opined that '[t]he difference between what the reasonable reader would understand and what the parties, acting reasonably, would agree, appears to me to be a notional distinction without a practical difference.'[960] As such, one may argue that there is no difference between on the one hand determining what intention would reasonable parties would have had, and on the other determining what assessment would a reasonable observer would have made of the contract terms.[961]

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[957] *Wood v Capita* (n 943) [13].

[958] *Arnold* (n 944), *Wood v Capita* (n 943). McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 31-32, 52, 68-69. For an opposing view, see Peel (n 672) 6-049 who argues that although Lord Hoffmann's approach was commendable, the primacy of the language will continue to rule contract interpretation. He reserves the contextual approach to cases where the background leads to an irrational literal interpretation, not simply an unreasonable one. Also see Geoff Hall, 'Customs and Usages in England: Achieving Interpretive Accuracy by Giving Effect to Unexpressed Intent', in F Gelinas (ed) *Trade Usages and Implied Terms in the Age of Arbitration* (Oxford University Press 2016) 3, who contends that the courts are moving from a textualist to a contextualist interpretation of contracts. For a similar analysis, see Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 470. Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 40 opines that the debate is relevant for understanding interpretation however it doesn't explain why a case is decided in line with the literal method rather than contextual, or vice versa. He claims that the method is ultimately selected depending on '[t]he interpretation that is established to the highest degree of probability, as a matter of objective intention (...).'

[959] Hall, 'Customs and Usages in England: Achieving Interpretive Accuracy by Giving Effect to Unexpressed Intent' (n 958) 13. The author further argues that another form of earlier contextualism is drawing upon customs and usages to interpret a contract.

[960] *Marks and Spencer* (n 658**) [**23] (Lord Neuberger SCJ).

[961] McLauchlan (n 905) 584, 589, the author contends that the 'whole debate is much ado about nothing!' and effectively argues that there is no difference between the determining the intention of reasonable contracting parties with the background information that reasonable people in their situation would have had, and, the intention of a reasonable observer with the background information reasonably available to the parties in the circumstances.

Yet, the 'more strongly objective theory' of rational choice advocated by Leggatt remains a compelling one.[962] The dissociation of the interpretative process from the parties' actual intention is liberating for the court and promotes certainty more so than the current orthodox approach adopted in the above cases. As such, it also fits into the purpose of contract law as an institution which upholds the reasonable expectations of honest people.[963] The contract makers are deemed to be reasonable people, and what better way to uphold their expectations than by protecting the shared intention. The shared intention can depart from that of reasonable people in the parties' situation, in which case, doctrines such as rectification remain available.[964] However, where shared intention is fictitious or ambiguous, and it will be so where the court must interpret the contract to determine how it applies, it is this strongly objective standard which should apply in the name of fairness and certainty.[965] Had the parties, at the beginning of the contract, told each other that if a dispute were to arise under the contract that each would want it to be adjudicated only to its own advantage, it is unlikely that they would enter into the contract in the first place. Another way of saying this is to presume that the parties intended to act rationally, meaning 'they had properly reflected on what their self-interest requires in circumstances where their choices are dependent on the choices of another equally self-interested agent.'[966] This view presupposes that 'each party must be presumed to have made such concession as would represent the least amount of sacrifice, but would return the highest possible benefit in the circumstances.'[967] This would be the baseline for understanding all contracts, regardless of their nature. The rationale of contract law has to be upheld in the context of dispute adjudication, because it is the legally binding and enforceable character of contracts which distinguishes it from any other instruments of social connection and drives market forces. Consequently, the institution of contract, namely contract law, must proceed on the basis that the actors are presumed to be rational and if a dispute is to arise, that it would be adjudicated on a rational and fair basis.[968]

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[962] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 454. See discussion in chp 4.2 *'The Paradox of Objectivity in Contractual Interpretation and Rational Choice Theory'* above.
[963] See chp 1.3.1.2.
[964] For the requirements of rectification, see n 893 above.
[965] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 474.
[966] Gounari (n 886) 193, ('for presumed rational agents to agree to a bargain, the bargaining process itself must be presumed to be rational,' [191]).
[967] ibid 191.
[968] Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 49, states that although this theory has not had explicit judicial support, Lord Hodge SCJ's judgement in *Wood v Capita* (n 943) [10] echoes the rational choice theory when he stated that 'the court's task [is] to ascertain the objective meaning of the language *which the parties have chosen* to express their agreement.'

The novelty of Leggatt's approach is that it presupposes that the parties are rational actors and that their choice of language is deliberate in conveying a shared intention.[969] Indeed, he recognises that 'parties intend things without them crossing their mind, intend a single meaning although the parties have multiple minds, and intend their contract to have a life of its own and to cover situations they have not foreseen.'[970] The interpreter, assuming as such, makes a judgment about their intention through the language used to determine a shared intention, even if such a shared intention did not exist. The intention is presumed not as a result of the interpretation process, but as an essential component of such a process. The parties are deemed to want to 'maximize their joint surplus' as rational actors. [971] The departure from the orthodox approach is necessary on the basis that the traditional test asks 'what a reasonable person with the background knowledge available to the parties would have understood them to be using the words of the contract to mean.'[972] However, searching for the actual intentions of the parties is a defective process because either 'at least one of them had no relevant intention at all or in any event because they had no shared intention (...).'[973] Why then does the interpretative exercise focus on searching for the intention of the fictitious reasonable person? Admittedly, the reasonable person would have concluded that there was no intention individually or shared intention commonly between the parties. This is why Leggatt's approach is attractive as it departs from the lesser objective interpretation of the *ICS* test; it focuses on an interpretation of contractual documents 'as having the meaning which best explains why rational parties who were using the language of the contract to express a shared intention would have chosen that language.'[974] The parties, assumed to be rational actors, the public manifestation of their intention could only be viewed as acts of rational people. Consequently, the interpretative process no longer depends on the parties' intentions, but on the meaning conveyed by rational contractors to a reasonable person with the background knowledge

[969] Campbell, *Contractual Relations: A Contribution to the Critique of the Classical Law of Contract* (n 352) 147, also confirms that '[i]t is not an attempt to impose an exogenous standard; it is an attempt to elucidate the endogenous standard.'
[970] Adam Kramer, 'Contractual Interpretation: Meaning, Intention, and Disembodied Spirits' in E Peel and R Probert (eds), *Shaping the Law of Obligations: Essays in Honour of Professor Ewan McKendrick KC* (1st edn, Oxford University Press 2023) 148.
[971] Brooks (n 3) 507, 508 the rational actor approach is posited as one which is suggested by the conventional economics approach which draws on considerations beyond the parties' actual agreement and intent. As such the 'rationality' referred to by Leggatt is more akin to the 'contractual morality' reasoning than 'consensual rationality' (chp 1.2.3).
[972] Leggatt, 'Making Sense of Contracts: The Rational Choice Theory' (n 421) 463.
[973] ibid.
[974] ibid 475.

available to the parties.[975] The intended meaning and the one conveyed to a reasonable person are expected to coincide, but the latter takes into account a wider range of factors and background information. This is understood as 'institutionalising the relational treatment of contracts' to ascertain the parties' intentions 'not by reference to each party's unique intentions' but by reference 'to the common basis upon which the parties agreed as presumed rational agents', to have 'calculated their respective concessions to make the contract possible in the first place.'[976] Where the contract is incomplete, the courts would be able to complete the contract without rewriting it.[977]

The debate is still ongoing as to whether the courts will adopt the contextual method adopted in *ICS*, or whether they will stay loyal to the literalist approach.[978] What is clear is that the rules of construction are not rigid; they are broad principles, capable of change.[979] It is submitted that good faith can add clarity to the above debate between the literal and contextual interpretation. This is because the process of interpretation can be 'stretched beyond its capacity to justify outcomes,' in the sense where contract is taken to be the primary, if not only, source for contractual liability.[980] However, as we have argued herein, contracts do not exist in a vacuum, and normative considerations governing contract law acknowledge such reality.[981] The competing fairness consideration, to that of freedom of contract, crystallises in good faith.[982] As such, consent of one party is 'tempered by the reasonable expectation of the other party, (...). It is also tempered by a principle of fairness between the parties.'[983] This is because

[975] Gounari (n 886) advocates for institutionalising the relational treatment of contracts in order to ascertain the parties' intentions not by reference to each party's unique intention but by reference to the common basis upon which the parties agreed as rational agents.
[976] ibid 192.
[977] As such, contextualism would not have helped the court find a contract in *Baird* (n 330), because the parties did not share a common business intention, namely one party's view of the relationship was a 'discrete' one, whereas the other one's was of a partnership, Gounari (n 886) 193.
[978] Brownsword, 'After Investors, Interpretation, Expectation and the Implicit Dimension of the 'New Contextualism'' (n 321) 103.
[979] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 35.
[980] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 459.
[981] ibid 479-480, where the author posits that the role given to interpretation necessarily is reflected in the role of contract law itself. Therefore, interpretation must reflect the substantive normativity which the contract law's framework rests upon, including morality considerations. For instance, in regards to the doctrine of fundamental breach, she posits that the underlying substantive norm is that a 'a promise to render performance could not be emptied of all content and the obligation rendered largely illusory through the formal operation of contract terms.'
[982] Catterwell, *A Unified Approach to Contract Interpretation* (n 290) 63 who considers that 'fairness is rarely overtly relied upon in construction and it is not generally regarded as a universal guiding factor. Instead, it underlies a number of discrete rules and principles, such as the contra proferentem rule. More broadly, fairness is embodied in the duty of good faith.'
[983] Philip Sales, 'Contractual Interpretation: Antinomies and Boundaries' in E Peel and R Probert (eds), *Shaping the Law of Obligations: Essays in Honour of Professor Ewan McKendrick KC* (1st edn, Oxford University Press 2023) 154.

'each party is subject to obligations owed to the other, neither can claim that their own subjective beliefs as to the meaning of a promise (whether given by them or to them) should govern in a dispute about that meaning.'[984] Thus, such a view of good faith also alleviates concerns that 'a law that merely interprets, rather than directs, can appear seriously impoverished.'[985]

Undoubtedly, good faith is apt to operate in its own right as an independent rule of construction.[986] However, this does not make a principle of good faith redundant. Indeed, 'we don't throw out a new chocolate bar because it duplicates one we already have. (...) Redundancy can be a good thing in complicated systems in the law.'[987] A principle of good faith cannot simply be packaged as an interpretative tool precisely because as a principle, it 'enables a court to find unusual misconduct in performance to be a breach of contract without having to pretend to justify the decision by reference to intent or to custom.'[988] More precisely, the process of interpretation and the process of applying an external rule, regardless of whether the outcome would be the same, are entirely different.[989] The former draws its authority from the parties and the agreement in question, and the latter draws it from the external rule. In other words, '[t]o interpret a set of circumstances to reach a conclusion on liability is not the same as applying an external rule to reach the same end.'[990] In sum, good faith cannot be restrained to an interpretative tool, however its recognition as an overarching principle would undoubtedly facilitate an interpretation of contracts which is geared towards implementing good faith duties rather than denying them. The evidence to support such claim can be found in the courts' approach to contractual disputes where cooperation is in issue.

4.3. Duty to Cooperate

The duty to cooperate can be considered as a manifestation of the reasonable expectations of the parties based on the principle of good faith.[991] Duties of cooperation

[984] ibid.
[985] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 488.
[986] For an opposing view, see Davies, 'The Basis of Contractual Duties of Good Faith' (n 747) 30-31 who argues that such an approach would undermine the certainty in contracts, and instead implication in fact should be preferred.
[987] Melvin A Eisenberg, 'The Principle of Good Faith in Contract Law' in MA Eisenberg (ed), Foundational Principles of Contract Law (Oxford University Press 2018) 709.
[988] ibid 710.
[989] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 480.
[990] ibid.
[991] A view of good faith posits good faith on a spectrum. At the one end, good faith simply requires honesty and at the other, it requires a more extensive set of duties. See eg Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 314. Brooks (n 3) 505, claims mutual cooperation to be the 'touchstone of good

currently find their way into contracts through the process of implication rather than as applications of a principle of good faith or as principles of construction. However, there is precedent for using good faith under the latter method. In the Scottish case of *Mackay v Dick*, Blackburn LJ famously stated

> as a general rule, that where in a written contract it appears that both parties have agreed that something shall be done, which cannot effectually be done unless both concur in doing it, the construction of the contract is that each agrees to do all that is necessary to be done on his part for the carrying out of that thing, though there may be no express words to that effect. [992]

Seemingly, the court provided that there is a general obligation to cooperate or do all that is reasonably necessary to facilitate the performance of the contract.[993] The court did not imply such an obligation but rather arrived at it through the interpretation of the contract. The case concerned a contract for the sale of a custom-made digging machine. The contract provided expressly for the testing of the machine before payment was due. It was a clause to the advantage of the defendant. However, the defendant did not allow the testing and refused to pay for it. The court construed the contract as imposing an obligation on the defendant to cooperate to allow the machine to be tested. It was held that the defendant, having breached such obligation, could not complain and was required to pay.

In later cases, the decision in *Mackay* has been considered and relied on many times in various contexts.[994] Until the recent decision of the Court of Appeal in *King Crude Carriers SA & Ors v Ridgebury November LLC & Ors*, the English courts have preferred an implied terms approach to the duty of cooperation rather than one of construction as suggested in

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faith,' the degree of such cooperation varies depending on whether a 'consensual rationality' or a 'contractual morality' view is held of the concept (see chp 1.2.3 above).

[992] (1881) 6 App Cas 251, 263. A term was implied that each party undertook to do all that was necessary for the carrying out of matters which could only be achieved with the cooperation of both parties.

[993] In *Luxor (Eastbourne) Ltd v Cooper* [1941] AC 108 (HL), the leading authority on an estate agent's right to commission, the court found that there was no duty to cooperate because it was not necessary to imply such term to make the contract work in the context of the agency agreement where the work of the agent, which was to produce an offer for the property, did not require the other party's cooperation, except to provide access to the property for viewing by prospective buyers. There was no implied term to the effect that the principal would not dispose of the property himself or otherwise act so as to prevent the agent from earning the commission. The court therefore refused to imply a term to the effect that the owner was under an obligation to accept the prospective buyer introduced by the agent [118]. However, the court accepted that in certain cases the implication of a term of cooperation could be possible, resulting in the principal to be under a duty to do nothing to prevent the agent from doing the work which he was contractually bound to so.

[994] *Mackay* (n 992). See eg, *Swallowfalls Ltd v Monaco Yachting and Technologies SAM* [2014] EWCA Civ 186 [32] (Longmore LJ) (in the context of a shipbuilding loan agreement); *Quadrangle Development and Construction Co Ltd v Jenner* [1974] 1 WLR 68 (CA) 71 (Russell LJ) (in the context of conveyancing).

Mackay.[995] For instance, *Mona Oil Equipment & Supply Co Ltd v Rhodesia Railways Ltd* concerned a claim for breach of contract for the sale of oil tanks by the claimant to the defendant.[996] There was a dispute about whether the claimant was entitled to payment against a signed confirmation by the defendant's shipping agents that the tanks were at the defendant's disposal. The agents initially refused to give confirmation, awaiting instructions from the defendant. Even though the defendant later issued instructions, it did not inform the claimant it had done so, and the claimant did not ask the agents again for the confirmation. The claimant argued that the defendant breached an implied term that they would procure their agents to take all reasonable steps to ascertain whether the tanks were at the disposal of the defendants and not to do anything to prevent the fulfilment of the condition of payment. The court refused to find an implied term to such effect.[997] Devlin J concluded that where the wrongful act was a breach of contract in its own right, then it was unnecessary to rely on an implied term, thereby failing the test of necessity under the traditional tests.[998]

Similarly, in *James E McCabe Limited v Scottish Courage Limited,* the court had to consider whether there was an implied term of cooperation under the terms of a beer distribution agreement to decide whether there was wrongful termination.[999] The claimant claimed that there was an implied duty to cooperate 'so as not to prevent or in any way inhibit the fulfilment of the minimum purchase requirements.'[1000] The court stated that any term of cooperation or prevention from performance can only be imposed in light of the express terms of the contract.[1001] As such, to enforce a duty to cooperate, it must be necessary to make the contract work. This refers to an operation of the duty by way of implication under the traditional test of business efficacy. Cooke J refused to recognise a duty of cooperation which could operate independently from the contract:

> [t]he court cannot, by implication of such a duty, exact a higher degree of co-operation than that which could be defined by reference to the necessities of the contract. The duty of co-operation or prevention/inhibition of performance is

[995] [2024] EWCA Civ 719, [2025] 2 WLR 181. See text to n 992 above.
[996] [1949] 2 All ER 1014 (HC).
[997] ibid 1018 (Devlin J).
[998] ibid 1017-1018 (Devlin J).
[999] [2006] EWHC 538 (Comm).
[1000] ibid [14] (Cooke J).
[1001] ibid [17] (Cooke J).

> required to be determined, not by what might appear reasonable, but by the obligations imposed upon each party by the agreement itself.[1002]

More recently, in *Odyssey Aviation Ltd v GFG 737 Limited*, the court had to consider whether there was an implied term of cooperation.[1003] The case concerned an aircraft sale and purchase agreement. The buyer had paid a refundable holding deposit into an escrow account. The agreement contained conditions precedent which related to the receipt by the buyer of documents that could only be obtained from the seller. The buyer sought to terminate the agreement for breach of the conditions precedents and requested the return of the deposit. The seller also purported to terminate and requested the remainder of the deposit. It was held that there was an implied term that the buyer should have taken reasonable steps to request such documents and notify the seller if it had been unable to obtain them reasonably in advance of the scheduled delivery date. The duty of cooperation was not implied in law, but was implied in fact, relying on necessity and business efficacy; and the court further considered that the implied term was reasonable and equitable.[1004] Accordingly, only the seller's termination was valid, and they were entitled to the rest of the deposit.[1005]

Consequently, in the commercial context, where a duty of cooperation is at play, the courts have preferred the implication in fact route over other methods until the recent Court of Appeal's decision in *King Crude Carriers SA*.[1006] The buyers entered into a sale of three ships requiring them to pay a 10% deposit into an escrow account once the escrow account holder confirmed it was open and ready to receive funds, which was the condition precedent to the deposits being due. The sellers terminated the contracts and claimed the deposits as debt under the contracts. They argued that the buyers had failed to provide the required documentation under the contracts, which were necessary to open the account to the escrow account holder. In a unanimous decision, the Court of Appeal allowed the appeal, holding that the sellers could recover the deposits as debts. Indeed, the court looked at the 'presumed intention of the parties' which Popplewell LJ posits as the 'legal basis' of the rule in *Mackay* that a person should not be permitted to take advantage of their own wrong.[1007] The purpose of a deposit in commercial contracts is 'well known' and serves to provide security to the seller for the buyer's failure to

[1002] ibid.
[1003] [2019] EWHC 1927 (Comm), [2019] 2 CLC 231.
[1004] ibid [77].
[1005] ibid [97].
[1006] *King Crude Carriers SA* (n 995). Leave to appeal to the Supreme Court has been granted in October 2024, *Ridgebury November LLC v King Crude Carriers SA* (Permission to Appeal) [2024] 10 WLUK 676 (SC).
[1007] ibid [208] (Popplewell LJ).

complete the purchase. The default of the buyer, therefore, triggers the obligation for payment of the deposit, and the buyer cannot escape it by arguing that the condition precedent was not fulfilled, where the buyer itself was at fault for the non-fulfilment of the condition precedent.[1008] In essence, the court considered the role of the principle in *Mackay* to be to prevent the buyer from insisting on an understanding of the contract against the parties' presumed intentions.[1009] The court did not find any evidence that the parties had sought to alter the balance of risks whereby the buyer would be allowed to avoid its liability, and the seller would be restricted to a claim in damages.[1010] Essentially, the court's approach was to arrive at the duty of cooperation by way of interpretation of the contract and the parties' presumed intentions by taking into account how deposits are usually used in the commercial context, thereby adopting a contextual understanding of the deal.

It is unfortunate that the court in *King Crude Carriers SA* did not refer to good faith in its legal analysis.[1011] It is hereby suggested that good faith underlies the analysis of the court, as the reference to the 'presumed' intention of the parties incorporates a contextual understanding of the contracts, thereby adopting an objective analysis of such intention. Good faith works to control the exercise and possible breaches of positive obligations and rights in a contract.[1012] For example, the court in *Odyssey Aviation* could have arrived at the same result by interpreting the obligation of the buyer to obtain the documents to be exercised in good faith.[1013] As such, a timely request would have been interpreted to be part of the buyer's obligation, the breach of which would have entitled the seller to terminate the agreement and forfeit the deposit. This would have avoided reference to the implication of the terms methodology. Similarly, in *Equitable Life v Hyman*, the court could have arrived at the same result without referring to the implication method.[1014] Indeed, the reasoning applied to all 90,000 policy-holders, and not only to the particular relationship between Mr Hyman and Equitable Life. It is a case 'where construction of the contract as a whole is decisive.'[1015]

Instead of an implied term approach, which would also circumvent arguments that commercial contracts are not certain enough as a class of contracts, the use of interpretation by

[1008] ibid [213] (Nugee LJ).
[1009] ibid [214].
[1010] ibid [214] (Nugee LJ), '[…], [t]he parties had indeed intended that the buyer should pay the deposit.'
[1011] *King Crude Carriers SA* (n 995).
[1012] Peden, 'Incorporating Terms of Good Faith in Contract Law in Australia' (n 883) 232.
[1013] *Odyssey Aviation* (n 1003).
[1014] *Equitable Life* (n 836).
[1015] Furmston (n 735) 159.

the courts in settling commercial disputes would allow for a more direct approach to recognise good faith as the essence of all contracts and uphold the reasonable expectations of the parties.[1016] The courts' development of the literalist approach is clearly fuelled by a willingness to respect certainty in contracts, whereas the contextual approach would have gradually appeared to curb the harshness of the literalist one, which can be justified by an adherence to principles of justice or equity.[1017] All rules of construction can similarly be justified on the grounds upon which contract law is founded. A coherent approach to interpretation would be required in any case. Even where a 'default ethic' is recognised to underlie contracts, the adversarial understanding would have to be replaced by a cooperative default in all cases, 'not just exceptionally.'[1018] Therefore, a recognition of good faith as a rule of construction is more likely where it is also recognised as an overarching principle.[1019] Where literalist and contextual methods diverge, good faith could potentially unite them in their objective ascertainment of the contract's meaning and inform the way forward. However, given that the references to good faith in the case law are in regard to implication in fact rather than in construction, it is not possible to deduce that the courts are ready to adopt good faith as a new construction rule in commercial contract law any time soon.[1020]

4.4. Express Good Faith Clauses

Whilst the courts do recognise and seek to enforce express good faith clauses, the restrictive interpretation of such clauses has led to confining the duty to specific circumstances

[1016] Calnan (n 899) 7.18, argues that interpretation is a way for courts to bring into English law concepts of reasonableness and good faith in a covert manner, effectively operating to fetter freedom of contract.
[1017] For a discussion on certainty or predictability in construction of terms, see McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 57-58.
[1018] Brownsword, 'After Investors, Interpretation, Expectation and the Implicit Dimension of the 'New Contextualism'' (n 321) 135-136, argues that the default position for the basic ethic of contract law, furthered by contextual interpretation, if cooperative, should be grounded 'in some deeper theory of reasonable expectations (whether expressed in the form of general principle, particular standards, or contractual ethic.'
[1019] Peden, ''Implicit Good Faith' - or Do We Still Need an Implied Term of Good Faith?' (n 734) 5, argues that '[l]egal concepts that are applicable to all contracts are not achieved by implied terms, but rather through construction.' Schwartz, Scott, 'The Common Law of Contract and the Default Rule Project' (n 247) 1577-1587, where in the context of US law, the authors argue that the duty of good faith in commercial contexts is an interpretative rule, 'courts apply the duty by inferring the parties' contracting goals from the written terms, and then evaluate behaviour that the contract did not explicitly regulate in light of those goals.' As such, there is no independent duty of good faith which can be breached.
[1020] In *Globe Motors* (n 644) [68] (Beatson LJ), the court did not consider implication of a good faith duty as the case concerned the interpretation of the amendment clause of a car component purchase agreement contract. The court, in referring to *Carewatch* (n 3) insisted that good faith could only be implied where the language of the contract, viewed against its context, permits it. As such, 'it [good faith] is thus not a reflection of a special rule of interpretation for this category of contract.' Also see, McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 42.

envisaged by specific clauses in dispute.[1021] In *Berkeley Community Villages Ltd v Pullen*, the court upheld an express clause of 'utmost good faith.'[1022] It concerned a contract between a property developer and a landowner, who had agreed that the property developer would be entitled to a fee when the land was sold. The developer put in efforts to obtain the planning consent, which increased the value of the land. The landowner sought to sell the land before the consent had been granted, which would leave the developer with no entitlement to a fee. The developer argued that the landowner breached the agreement by contravening the duty to act in good faith. The court interpreted the clause and concluded that it imposed on the parties 'a contractual obligation to observe reasonable commercial standards of fair dealing (...) and also requiring faithfulness to the agreed common purpose and consistency with the justified expectations' of the developer.[1023] The reasonable expectation of the developer was that its efforts to promote the land would involve obtaining consent and enabling the sale on the open market of the property, entitling it to a contractual fee.[1024] In considering whether a term in fact should be implied to prevent the sale, the court stated that the express term of good faith was sufficient to prevent the sale in the circumstances. However, the court stated that if the express clause did not exist, it would have been necessary to give business efficacy to the contract to imply that the landowner should not sell the land.[1025]

A similar meaning was given to an express clause of good faith in *Health and Case Management Ltd v Physiotherapy Network Ltd*.[1026] The claimant provided services to insurance companies by managing referrals to physiotherapy clinics. The defendant had a nationwide network of clinics. The parties entered into a services agreement whereby the claimant referred patients to the defendant in return for fees. A clause of the agreement stated that the claimant should 'act in good faith' towards the defendant. The defendant decided to build its own network of clinics and used the information obtained under the contract with the claimant to further its own business. The defendant obtained the relevant information from the claimant by giving a false pretence, and would not have been provided by the claimant if the claimant had known of the defendant's real intent. In interpreting the good faith clause, the court stated that

[1021] See for instance, *Phones 4U Limited* (n 757) [653] where a general express good faith clause was held to be applicable only to obligations arising under particular clauses under the contract. Also, see David Pliener, Sri Carmichael, 'Are English Courts Still Hostile to a Doctrine of Good Faith?' (2017) 32(1) Butterworths Journal of International Banking and Financial Law 19, 20, who posit that the court's narrow approach to express good faith 'attaches to specific obligations and steers a way around conflicts with other express terms.'
[1022] [2007] EWHC 1330 (Ch).
[1023] ibid [97].
[1024] ibid [109].
[1025] ibid [134].
[1026] [2018] EWHC 869 (QB)

the defendant had breached its obligation by giving a dishonest reason for its request for data. The court stated that the defendant had 'failed 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 to act consistently with the justified expectations of the parties.'[1027] The court also indicated that, regardless of the dishonest request for data, the use of the data itself would have most likely been a breach of the good faith clause in itself.[1028] Moreover, the fact that the defendant had acted in an 'underhand and exploitative manner' by establishing itself as a competitor all the while continuing to benefit from the relationship with the claimant itself was a contravention to the good faith clause.[1029]

More recently, the Court of Appeal had the opportunity to delve into an extensive review of the meaning of an express clause of good faith in a shareholders' agreement in the context of an unfair prejudice petition in *Re Compound Photonics Group Ltd; Faulkner v Vollin Holdings Ltd*.[1030] In interpreting the clause, the court adopted a contextual methodology and stated that a duty of good faith was akin to a duty of honesty, and depending on the context, a duty not to engage in bad faith conduct. This did not bring much clarity to what is meant by good faith in express clauses, but the court's approach emphasised that the content of the duty will be context-dependent. As such, any further duties of good faith could only be derived as a matter of interpretation or implication from the other terms of the contract, taking into account the commercial context.[1031] The court was careful to distinguish the approach to the requirement to have regard to the interest of the other party as applied in commercial contracts. Indeed, in commercial contracts, such a requirement may be found where a business decision might adversely affect or deprive the other party of the commercial benefit expected to be enjoyed by the other party in their contract.[1032] Conversely, in the companies law context, the interests of the members are different to those of commercial parties, the longstanding rule being that the votes attached to shares are 'proprietary rights that the holder may exercise as they see fit in their own interests.'[1033] Such distinction in the rationale of interpretation of good faith clauses illustrates why categorising the types of contracts is important to encourage the recognition of good faith as a general principle and its concretisation in various categories.[1034]

[1027] ibid [128] (Nicklin J).
[1028] ibid [129] (Nicklin J).
[1029] ibid.
[1030] [2022] EWCA Civ 1371.
[1031] ibid [243], [275]-[276] (Snowden LJ, with whom Newey and Carr LJJ agreed).
[1032] ibid [197].
[1033] ibid [199].
[1034] See chp 1.3.2 for the discussion on the concretisation of principles into rules.

The individual instances of application and refinement of good faith duties would bolster a more coherent approach to the interpretation of contracts in general. However, the most recent decision of the Court of Appeal in *Aston Martin Mena Limited v Aston Martin Lagonda Limited* shows the reluctance to interpret express good faith as applying beyond the relevant contractual obligations, in the circumstances beyond termination obligations in the agency agreement.[1035] Moreover, the traditional tests for implication in fact would fail in the circumstances, and there was no discussion on the relationality of the contract, thereby negating the possibility of an implication in law to such contracts.[1036] The court, however, confirmed that the content of a good faith duty, had it been found to be implied, would not require a general requirement to have regard to the interests of the other party.[1037]

4.5. Contracting Out

We have already touched on good faith as a default standard above.[1038] The rationale of contracting out of legal standards is closely related to that of the law. Where the law takes on a role of regulation of the commercial behaviour of the parties or where it facilitates commerce by providing a framework and leaving the parties to fill in the content, the approach to contracting out will vary.[1039] Where good faith can be envisaged as a default, this necessarily entails that parties can contract out of it. Conversely, an implied term in law cannot be implied if inconsistent with an express term.[1040] As stated by Fraser J in *Bates*, 'if the express terms prevent the implication of a duty of good faith, then that will be the end of the matter.'[1041] Although this will be limited by public policy considerations.[1042]

In the context of good faith, a general contracting-out clause excluding its application is inherently inconsistent with good faith's purpose. First, the parties cannot contract out of

[1035] [2023] EWHC 3285 (Comm) [210], [212] (Moulder J), the express clause was found to be dealing with termination, therefore the court did not extend the good faith duties beyond termination obligations until the obligations under the distributorship agreement resumed after a transition period.
[1036] ibid [179].
[1037] ibid [220].
[1038] See chp 1.
[1039] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 472.
[1040] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 383.
[1041] *Bates* (n 48**)** [726].
[1042] For instance, in the context of employment contracts, see *Johnstone v Bloomsbury Area Health Authority* [1992] 2 QB 333, [1991] 2 All ER 293, [1991] 2 WLR 1362 (CA), where the court refused to uphold an express term of the contract requiring an employee to work for extended hours, deeming it to be contrary to public policy, and upholding the implied term in law that the employers had an implied duty to take reasonable steps to ensure the safety of their employees in the workplace.

general principles of contract law; they are not concretised rules which can be opted out of.[1043] Therefore, they would not be able to do so in the context of a general principle of good faith either.[1044] It is inconceivable to think that a court would be willing to enforce a contract where the parties have contracted out of the requirement for legal certainty and agreed that its terms need not be certain.[1045] In the context of contracting out of freedom of contract, there is a debate as to whether the decision in *Rock Advertising* was correct.[1046] The Supreme Court departed from the dominant common law approach and gave effect to a 'no oral modification clause.'[1047] The Supreme Court provided that for relief to be provided based on estoppel, '(i) there would have to be some words or conduct unequivocally representing that the variation was valid notwithstanding its informality; and (ii) something more would be required for this purpose than the informal promise itself.'[1048] However, if it had been openly recognised in English law, the Supreme Court potentially could have relied on a good faith principle to avoid the use of an estoppel doctrine. The second requirement set out by the Supreme Court, requiring 'something more', refers to the unconscionability of going back on a promise where the other party has relied on it. Again, a reference to a good faith principle would have avoided an unconscionability argument.

Secondly, good faith is intrinsically understood to be linked to the reasonable expectations of the parties. Therefore, where the parties agree to contract out of any of their expectations, this would either mean (i) they are setting out an express term (which itself would be interpreted in line with their reasonable expectations in regards to such a term), or (ii) they

[1043] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 56, in the context of interpreting contracts, the courts engage in a balancing exercise of various default principles. Although the role of public policy in the context of interpretation of contracts is limited, it tends to focus on 'whether and to what extent the courts should adopt a stricter reading of certain contracts or certain species of clause.'

[1044] Hogg (n 697) 1689 suspects that where good faith is seen as an underlying doctrine or a rule of law, 'the exclusion will be harder, if not impossible.' Further, this is in line with the view that where we can identify implied terms at law that are 'created or grounded on considerations of reasonableness, fairness and policy (…)' and which confer 'valuable rights upon a party (…)', the more resistant they become to exclusion, as they are viewed central to the contractual relationship, see Kwan Ho Lau, 'Terms Implied by Law: To Exclude or Not To Exclude?' (2026) 1 Journal of Business Law 18, 22.

[1045] For an opposite view, see Davies, 'Excluding Good Faith and Restricting Discretion' (n 585) 103, argues that parties should be able to contract out of good faith, even to contract out of honesty should be possible, because in any event this would not mean that the parties can commit fraud with impunity, rather that such fraud would not be a breach of contract. The innocent party would sue for deceit in tort and recover damages on the basis of a tortious measure, rather an expectation measure.

[1046] *Rock Advertising* (n 22). For criticism of the decision, see McMeel, 'Are There Any General Principles of Commercial Law?' (n 144) 192-193, who argues that the bar placed by the decision on the enforceability of 'no oral modification clauses' is too high as it relies on an argument based on estoppel.

[1047] ibid.

[1048] *Rock Advertising* (n 22) [16], citing *Actionstrength Ltd (t/a Vital Resources) v International Glass Engineering In Gl En SpA* [2003] UKHL 17, [2003] 2 AC 541 [9] (Lord Bingham), [51] (Lord Walker).

are agreeing to a practice or standard that is outside of what can be reasonably expected from the circumstances by the relevant community standards, for instance because they are expressly excluding the application of an industry custom, or because their agreed meaning of the term is different than to that used in the relevant business community. As with terms implied in law, where public policy considerations would make it illusory for the parties to contract out of them, good faith would similarly not be capable of being excluded from the fabric of the contract.[1049] Otherwise, this would amount to potentially giving legal force to contracts even when performed in bad faith or abusively.[1050] As explained above, it is argued that honesty is not a component of good faith, but even if it were, contracting out of honesty would not be possible, and would be void 'by analogy with the rule that a party cannot exclude liability for his own fraud.'[1051]

There may be an argument to say that where the parties contract with each other out of necessity but in a spirit of mistrust, the law should uphold their agreement because they are entering into the agreement knowing the risks.[1052] However, good faith as envisaged herein is linked to the reasonable expectations of the parties, gauged on an objective basis. [1053] Where objectively the parties' reasonable expectations are that they are accepting an objectively unreasonably dishonest agreement, contract law will have difficulty enforcing such expectations. Upholding an unreasonably dishonest view of the parties' conduct would mean that good faith is adopting not an objective but a subjective view of the parties' expectations. An objective approach to good faith would require that only the parties' reasonable expectations from an objective standpoint be given force. Let us imagine an unusual scenario. The parties contract that A will provide B with mechanical parts for B to manufacture a machine. They agree that they can lie to each other about the fitness for purpose of the part being provided and the machine being manufactured. Where A provides parts that are not fit for purpose and lies about their fitness, B will not have a contractual claim against A for having

[1049] Hooley (n 456) 81, 83 argues in the context of contractual discretions where a contract provides for 'absolute discretion' to the decision-maker, this will not mean that, due to reasons of public policy, that party should be able to contract out of honesty requirements, similar to the rule which provides that a party shall not be liable for his own fraud.

[1050] Whilst 'terms implied in law may be more difficult to exclude than those implied in fact (...), certain terms implied by statue are incapable of exclusion' such as Consumer Rights Act s 31(1).

[1051] See chp 1.3.3 '*Honesty*'. Peel, (n 672) 6-079; also see Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557) 314 (fn 56).

[1052] ibid 21.

[1053] Crabtree (n 828) 168, indeed, in the absence of express wording to the contrary, 'parties acting in good faith will presume that they should not intent to act dishonestly or negligently; likewise, they might well presume that the other should not seek to enforce or discharge their contractual rights and obligations in bad faith, where they lack a legitimate interest in doing so.'

agreed to be lied to about this topic. The reasonable expectation from the objective standpoint is that both parties have accepted the possibility that they will not be receiving parts or goods which were fit for purpose. As such, they cannot cry 'good faith'. Good faith's purpose is not to impose an outsider's view of what the expectation should have reasonably been, but to uphold what the parties have agreed to reasonably expect from the contract, even where such expectation goes against market norms. Therefore, it is not possible to contract out of the parties' reasonable expectations, as these constitute the essence of the contract. If the parties are engaging in dishonest conduct, the question then becomes whether the tort of deceit might have been committed, but where contract ends and tort begins is a debate in its own and beyond the scope of this thesis.[1054]

4.6. Change of Circumstances

4.6.1. The Doctrine of Frustration

Although frustration originated as an implied term explanation, it is no longer coherent to describe the doctrine in those terms. Modern case law treats frustration as a rule of law that operates independently of any reconstruction of party intention. The evolution of the doctrine of frustration is therefore a good example of how concepts can be explained through implied terms to then become independent doctrines. The doctrine operates as a rule, rather than a principle, as it is narrowly confined to exceptional circumstances which, when the legal threshold is met, operate independently of party intention and result in the discharge of the contract.[1055] Frustration, however, does not concern an incidental omission, but a fundamental disruption to the contractual basis itself, caused by an event that lies outside the ordinary scope of contractual planning. Gradually, the use of the implied terms explanation was dropped and the doctrine was applied independent of any reliance on intention, being instead justified by legal norms of fairness and justice. [1056]

To escape the application of the doctrine, the parties in commercial contracts may provide for the effect of unforeseen circumstances, such as in the form of *force majeure*.[1057] A *force majeure* clause will excuse one or more parties from performing their contractual

[1054] For instance, see Dennis Patterson, 'Good Faith in Tort and Contract Law: A Comment' (1994) 72 Texas Law Review 1291, who argues that good faith should be confined to contract law and not spill into tort law.
[1055] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 664.
[1056] ibid.
[1057] ibid 671.

obligations if they are prevented from doing so by unforeseen circumstances outside their control. The interpretation of the *force majeure* clause will determine the extent of the unforeseen circumstances covered by the contract, the conditions of application of the clause, and its effect on the performance of the parties' contractual obligations. Usually, the *force majeure* clauses will not be applicable in instances where the performance has become more expensive or less profitable.[1058]

Where no provision is made in the contract for change of circumstances, or where the relevant provisions are not triggered, the parties will be left with the doctrine of frustration. For this, further performance of the contract should have become impossible or radically different from those contemplated by the parties at the time of contracting. A restrictive approach is adopted towards the doctrine, as the effect of it is to set aside the contract.[1059] Therefore, ascertaining the expectations of the parties at the time of contracting will be important. In this assessment, determining the foreseeability of the event will be crucial. The less an event is foreseeable, the more likely it is to trigger the application of the doctrine. However, it does not mean that where an event was foreseeable, the application of the doctrine will not be possible. Where a foreseeable event renders the performance of the parties radically different from that which was planned, the doctrine of frustration may still be triggered. The question is therefore whether the supervening event has defeated the contractual expectations that formed the basis on which performance was undertaken, rather than whether it fell within the parties' subjective contemplation. In particular, where the contract has provided for the event, this will prevent the application of the doctrine unless the event is significantly more impactful than provided for in the contract.

In *Edwinton Commercial v Tsavliris Russ (Worldwide Salvage & Towage) Ltd (The Sea Angel)*, the Court of Appeal, holding that a 20-day time charter had not been frustrated by a delay of 108 days in redelivery of the vessel due to its detention by port authorities, stated that a 'multifactorial approach' should be followed.[1060] The approach articulated by Rix LJ confirms that frustration is concerned not with reconstructing intention, but with assessing whether the contractual allocation of risk, viewed objectively, can fairly be maintained in light of the supervening event. He clarified that

[1058] For instance, see *Thames Valley Power v Total Gas & Power* [2005] EWHC 2208 (Comm).
[1059] McKendrick, *Contract Law* (n 1) 292.
[1060] [2007] EWCA Civ 547, [2007] 1 CLC 876 [111] (Rix LJ, with whom Wall and Hooper LJJ agreed).

> [a]mong the factors which have to be considered are the terms of the contract itself, its matrix or context, the parties' knowledge, expectations, assumptions and contemplations, in particular as to risk, as at the time of contract, at any rate so far as these can be ascribed mutually and objectively, and then the nature of the supervening event, and the parties' reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances.[1061]

Application of the doctrine is confined to instances where the test of 'impossibility' or 'radically different' is satisfied. For this, the ascertainment of the parties' expectations at the time of contracting will be crucial. These expectations are not subjective beliefs held by the parties, but objective assumptions attributed to the by the law, informed by the contract, its context, and the nature of the risk that has materialised. As stressed by Rix LJ, understanding the contract's meaning will require a wholesome approach, where many factors are taken into account, not just the literal meaning of the words. Ultimately, this approach is in line with the contextual approach preferred by many judges, as seen above and seeks to promote a fairer outcome in the allocation of risk in contracts.

Rix LJ confirms that the doctrine of frustration itself is concerned with justice.[1062] Where the doctrine applies, this may result in a reversal of the contractual allocation of risk in favour of a just outcome. Judicial references to justice in frustration cases are not incidental. They reflect the fact that the doctrine operates as a legal control on contractual enforcement rather than as an exercise in interpretation or implication. Framing frustration in terms of expectation avoids the conceptual difficulty inherent in implied terms, while also explaining why foreseeability, risk allocation, and fairness occupy a central role in the doctrine. Similarly, the statements made by Sumner LJ in the Privy Council in *Hirji Mulji v Cheong Yue Steamship Co Ltd*, and Wright LJ in *Cricklewood Property and Investment Trust Ltd v Leighton's Investment Trust Ltd* clearly indicate that fairness is at the forefront of the logic of the doctrine.[1063] Indeed, Sumner LJ considers that '[i]t is really a device, by which the rules as to absolute contracts are reconciled with a special exception which justice demands,' and Wright LJ states that 'the doctrine of frustration is modern and flexible and is not subject to being

[1061] ibid.
[1062] ibid [112], stating that '[u]ltimately the application of the test cannot safely be performed without the consequences of the decision, one way or the other, being measured against the demands of justice.'
[1063] *The Sea Angel* (n 1059) [86] (Rix LJ citing respectively *Hirji Mulji v Cheong Yue Steamship Co Ltd* [1926] AC 497, and *Cricklewood Property and Investment Trust Ltd v Leighton's Investment Trust Ltd* [1945] AC 221).

constricted by an arbitrary formula.' Simon LJ statement in *National Carriers Ltd v Panalpina (Northern) Ltd* confirms that the doctrine is 'on the face of it apt to vindicate justice wherever, owing to relevant supervening circumstances, the enforcement of any contractual arrangement in its literal terms would produce injustice.'[1064]

The doctrine was initially developed based on an implied term.[1065] Implied term explanation rested on the assumption that, had the relevant supervening event been contemplated at the time of contracting, the parties would have agreed that the contract should come to an end. In examining the parties' intention at the time of contracting, if the contract could be interpreted to mean that the parties had intended for the continuation of the state of things, then the occurrence of an event to disrupt such state would mean that this would have to impliedly result in the discharge of the contract. Yet the doctrine of frustration applies precisely in circumstances where the supervening event neither provided for not truly contemplated by the parties at the time of contracting. The difficulty is therefore that the doctrine presupposes an implied agreement about an event whose defining feature is that it lay outside the parties' contemplation altogether. To treat such a disruption as resolvable through implied terms is to attribute to the parties a form of hypothetical agreement that goes beyond their bargain and instead reconstructs it after the fact.

The anchoring of the doctrine on a general principle of law has initially been problematic. The classical theory's approach to freedom of contract meant that the parties' agreement could not be restricted by a term which was not agreed at the outset. This internal tension was acknowledged by Radcliffe LJ in *Davis Contractors Ltd v Fareham UDC* where he observed that 'there is something of a logical difficulty in seeing how the parties could even impliedly have provided for something which, *ex hypothesi*, they neither expected nor foresaw (...).'[1066] Expanding the notion of contemplation does not resolve the difficulty. If the event was genuinely contemplated, frustration should not apply because the risk could and should have been allocated. If it was not contemplated, the implication of intention becomes fictitious.

Ultimately, the anchoring of frustration as an implied term had to find a better alternative.[1067] That alternative relied on fairness and was expressly referenced in various

[1064] [1981] AC 675 (HL) 701.
[1065] For an overview, see Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 424-427.
[1066] [1956] 2 All ER 145 (HL) 159.
[1067] Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 427 explain that implication is a two-stage test. First, the court should determine the reasonable expectations of the parties, taking into account the 'business

decisions.[1068] The implication of intention thus operates at a rhetorical level, preserving the appearance of consent, rather than at an analytical level capable of explaining the doctrine's operation. The implied term was ultimately a way in which to determine the expectations of the parties. Once this contradiction is exposed, the continued reliance on implied intention becomes unjustified, and the doctrine can only be coherently understood as operating independently of the parties' presumed will. Progressively, in practice it became akin to an implied term in law thereby resulting in a general doctrine of law applicable to all types of contracts.

This indicates that where a doctrine is adopted as generally applicable to all contracts, and where the relevant test for its applicability is being posed, the court must have first accepted that the doctrine was capable of application to all contracts. Whether the technique is through an alteration of the construction rules to accommodate the 'impossibility' or 'radically different' test in the assessment of the parties' reasonable expectations, or whether it is done through an implication in law, the ultimate goal of the doctrine is clear, and it is one of fairness. In distinguishing between the construction of the contract theory and the 'performance is radically different' or 'impossibility' test, Smith J in *Canary Wharf (BP4) T1 Ltd v European Medicines Agency*, was right to state that

> there is, in my judgment, a very material difference in how these two theories work in their application. Under the former, the true construction of the contract resolves all; the latter theory recognises the importance of the true construction of the contract, but also recognises that even construction has its limits when faced with extreme and unforeseeable supervening events.[1069]

Rather than operate as a rule of construction or a term implied in fact, to achieve its aim of 'just outcome,' frustration has been elevated to a 'rule of law.'[1070] Indeed, the direct references to fairness make the process of implication in law superfluous in the context of

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common sense' in a contextual approach, and secondly the court should proceed to apply the 'radically different' test to determine whether in light of the change of circumstances, the performance of those expectations would be caught by the test. The authors admit that the terminology for construction/implication as the basis of the doctrine is confusing, rather they should be viewed as 'techniques.' The aim should be to achieve a 'just solution' (fn 19).

[1068] *The Sea Angel* (n 1059), *Hirji Mulji* (n 1062), *Cricklewood Property* (n 1062), *National Carriers* (n 1063).

[1069] [2019] EWHC 335 (Ch) [26].

[1070] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 665, indicates that the debate on the judicial basis of frustration between one of construction/implication or one of 'rule of law' has been resolved in favour of the latter.

frustration. The historical movement away from implied terms towards frustration as an independent doctrine reflects the recognition that certain contractual failures cannot be addressed without abandoning implication altogether. Where the parties have not provided for a change of circumstances and where the 'impossibility' or 'radically different' test is satisfied, it is necessary to provide for an allocation of risk in all contracts where the interests of justice require it. The development of the doctrine of frustration illustrates how contract law, through incremental development, can transform a concept from an implied term into a legal rule.

4.6.2. Good Faith and the Doctrine of Frustration

The above analysis has similarities with the good faith debate. The modern doctrine of frustration performs a function that closely mirrors that attributed to good faith: it operates to prevent the enforcement of contractual obligations where doing so would defeat the reasonable expectations on which the contract was formed. The development of the doctrine of frustration can serve as a good example in regards to developing an overarching principle of good faith. However, there is a crucial difference from that of frustration. The courts have progressively refined the 'impossibility' or 'radically different' test in case law.[1071] Good faith has not benefited from the same judicial openness. However, other sources of law have made it clear that good faith is crucial to the essence of the doctrine of frustration. Indeed, during the COVID-19 pandemic, many contracts were affected by the change in trading circumstances, which might have affected the allocation of risk in the contracts. The European Law Institute published a document entitled *Principles for the COVID-19 Crisis*. The document was a guide and had no legal force on European States.[1072] However Principle 13.1 of the document is interesting in that it provides that the contractual allocation of the risk, in instances where the performance of a contract is temporarily or definitively prevented due to the pandemic, should be evaluated 'in the light of existing contracts, background legal regimes and the principle of good faith.'[1073] Similarly, the UK government also published guidance in May 2020.[1074] It was

[1071] For an overview, see Stone and Devenney, *The Modern Law of Contract* (2022) (n 1) 438-443.
[1072] European Law Institute, 'Principles for the COVID-19 Crisis' (*European Law Institute*, May 2020) <https://www.europeanlawinstitute.eu/fileadmin/user_upload/p_eli/Publications/ELI_Principles_for_the_COVID-19_Crisis.pdf> accessed 3 April 2025. The document indicates that '[t]hese [principles] are addressed to all European States (whether or not Member States of the EU), and are intended to guide European States, EU institutions and other bodies with the object of ensuring that everything that is done accords with the rule of law and democratic values.'
[1073] European Law Institute, 'Principles for the COVID-19 Crisis' (n 1087).
[1074] UK Government, 'Guidance on Responsible Contractual Behaviour in the Performance and Enforcement of Contracts Impacted by the COVID-19 Emergency' (*UK Government*, 7 May 2020) <https://www.gov.uk/government/publications/guidance-on-responsible-contractual-behaviour-in-the-

not a legally binding document, and simply encouraged contractual parties 'to act responsibly and fairly in the national interest in performing and enforcing their contract.'[1075] A later supplement published in June 2020 confirmed that the Guidance would remain in place indefinitely.[1076] The Guidance refers to fair and responsible contractual behaviour. Such behaviour goes beyond the scope of good faith and fair dealing identified by the courts. Indeed, the guide states that such behaviour includes

> being reasonable and proportionate in responding to performance issues and enforcing contracts (including dealing with any disputes), acting in a spirit of cooperation and aiming to achieve practical, just and equitable contractual outcomes having regard to the impact on the other party (or parties), the availability of financial resources, the protection of public health and the national interest.[1077]

Responsible and fair behaviour is said to be strongly encouraged, in particular for certain contractual obligations, and a specific reference is made to 'making, and responding to, force majeure, frustration (...) claims.'[1078] The Guidance is unlikely to have any effect on how the courts approach frustration. Indeed, the doctrine's underlying rationale is that of fairness, and the Guidance does not add any particular novelty to the interpretation of contracts where a contextual approach is preferred. It simply reaffirms the idea that a just outcome should be pursued in contractual disputes. For the doctrine of frustration, this has been clearly stated and affirmed in various case law.[1079] Outside of the context of change of circumstances, and in the context of the good faith debate, a strong judicial commitment to achieving fair outcomes has not been shown.

Regardless of its nonobligatory nature, the Guidance remains useful in reminding commercial law of its commitment to just outcomes in resolving contractual disputes where

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performance-and-enforcement-of-contracts-impacted-by-the-covid-19-emergency> accessed 3 April 2025 (*Guidance*).

[1075] ibid para 1.

[1076] UK Government, 'Update on Guidance on Responsible Contractual Behaviour in the Performance and Enforcement of Contracts Impacted by the COVID-19 Emergency' *(UK Government*, 30 June 2020) <https://assets.publishing.service.gov.uk/media/5f06ed4de90e0712cc90b706/__Update_-_Covid-19_and_Responsible_Contractual_Behaviour_-_30_June__final_for_web_.pdf> accessed 3 April 2025 (*Guidance Update*)

[1077] UK Government, *Guidance* (n 1073) para 14.

[1078] ibid, para 15(c).

[1079] *The Sea Angel* (n 1059), *Hirji Mulji* (n 1062), *Cricklewood Property* (n 1062), *National Carriers* (n 1063).

various interests should be taken into account before varying the contractual risk allocation.[1080] Moreover, it may prompt the judiciary to reconsider aspects of the scope of the doctrine of frustration as it is applied today and adopt a more flexible and welcoming approach to good faith as a general principle. Although frustration cases are not framed in terms of good faith, their emphasis on fairness, risk allocation and the defeat of contractual expectations is entirely consistent with a good faith analysis. In time, the development of the doctrine of frustration could also be tied into that of good faith, because good faith, as envisaged herein, is a unifying concept for all considerations of fairness in dispute resolution. Consequently, doctrines such as frustration would also come under the umbrella of an overarching concept of good faith and allow for the reasonable expectations of the parties to encompass such doctrines or duties. For example, where the circumstances change and make the performance of the parties' original obligations 'impossible' or 'radically different' from what they were originally envisaged, a duty to cooperate with one another might be developed to share the losses created by such change.[1081]

Such an approach would also alleviate the concerns of the critics of the doctrine of frustration. Indeed, the doctrine has been subject to extensive review and criticism, and has been left to face its fate with the increased and now extensive use of *force majeure* clauses or the like in commercial disputes.[1082] Where the risk of an unforeseeable event has not been allocated expressly in the contract, the approach of the doctrine of frustration has been to leave the loss lie where it falls, which raises doubts as to the doctrine's *raison d'être* in the first place. The development of the doctrine is hindered due to the narrow approach which has been adopted in its application. Uncertainty or efficiency-based approaches are not the cause of the hindrance, but its symptoms. The underlying cause is an anchoring issue. The explanation of the doctrine based on freedom of contract as an anchor poses an issue. Indeed, asking the parties to allocate a risk for an unforeseeable event would be a self-defeating argument. On an alternative view, where one considers all events to be foreseeable to some degree, then the silence of the parties amounts to a tacit acceptance that where no express allocation of risk has been provided, the loss will inevitably lie where it falls, regardless of whether this is what was agreed.

[1080] Leggatt, 'What is the Point of Commercial Law?' (n 236) reminds us that 'a further important function of commercial law is to provide fair and efficient means for resolving disputes about the meaning and effect of contractual documents.'
[1081] McKendrick, *Contract Law* (n 1**)** 293.
[1082] For an overview of the critics, see Morgan, *Great Debates in Contract Law* (n 212) 188-197.

Frustration demonstrates that English contract law already accepts that, in exceptional cases, justice requires judicial intervention that cannot be justified by implication or construction alone. Instead of a freedom of contract anchoring, where a good faith anchoring is preferred, the doctrine could further be developed and applied to cases, whether express clauses for allocation of risk have been provided or not. Indeed, the interpretation of such clauses would also benefit from an overarching good faith principle, as the narrow construction rules, such as the *contra proferentem*, may benefit from an overhaul under a more fair and consistent coverage of change of circumstance cases.[1083] The dichotomy which exists between preserving the doctrine of frustration, meanwhile developing the law solely based on *force majeure* or similar clauses would also disappear if the law on interrupted performance could be cohesively united under a general doctrine of good faith.[1084]

4.7. Conclusion

English law's preferred approach to good faith is to imply it in fact. It does not view it as a tool of interpretation, it does not imply it in law, and it restrains its application to the fettering of contractual discretions or an ill-defined category of relational contracts. When there is enough impetus to create a default rule to answer the reasonable expectations of honest people in a specific type of contract, good faith is also utilised to imply terms in law. The preference for implying good faith into contracts is not without criticism.[1085]

If good faith is to be recognised as an overarching principle, it can only be so based on an understanding that good faith permeates the essence of contracts. Consequently, contracts would have to be interpreted to give effect to that understanding. Using the implication method would then become unnecessary.[1086] Cases like *Socimer*, could then also be made subject to

[1083] McMeel, *McMeel on the Construction of Contracts, Interpretation, Implication and Rectification* (n 657) 316, indicates that 'the more contextual and common sense reading of commercial contracts has reduced the number of instances when the tie-breaking function of the maxim is required. Nevertheless, the courts continue to have recourse to *contra proferentem* reasoning both generally and on long-established authority in respect of exemption clauses, and in other cases where there is both ambiguity and good reason to prefer one party's interest to the other's.'

[1084] Morgan, *Great Debates in Contract Law* (n 212) 196, referring to McKendrick's argument that the law on change of circumstances should develop based on express clauses rather than a theoretical doctrine of frustration, which would point to an abolition of the doctrine of frustration all together.

[1085] See eg Peden, ''Implicit Good Faith' - or Do We Still Need an Implied Term of Good Faith?' (n 734) who suggests that good faith is implicit in the institution of contract law, making implication of good faith unnecessary. Instead, a good faith fettering on contractual discretions could be achieved through interpretation.

[1086] ibid 10, Peden argues that on such a view, implication would only be relevant where implying a higher standard of behaviour than required by the law, which would be possible but rare.

criticism for choosing the implication method. Where the court's insistence was on good faith and rationality as 'sufficient protection' against 'abuse caused by self-interest', it is regrettable that the court proceeded with implying good faith in fact, rather than using it as a construction tool to accept the fact that 'commercial contracts assume such good faith.'[1087] Consequently, the recourse to implied terms resembles too close an artificial reasoning to evade an express recognition of good faith as underlying contract law.

Where good faith is envisaged as enabling the upholding of the parties' as rational and honest parties, preventing them from evading contractual obligations, deviating from contractual objectives, exercising contractual discretions unreasonably, it hardly appears as a radical suggestion. Implied terms and interpretation of contracts already routinely provide solutions to such issues, but lack a cohesive basis for which good faith can serve as the ideal contractual standard.[1088] The progression of the doctrine of frustration is an example from which good faith can take inspiration. Indeed, the trajectory of frustration from implied term to rule of law provides a model for understanding how good faith currently confined to implication and specific contexts, might develop into a more general principle without undermining contractual certainty. Frustration this stand not only as a doctrine of change of circumstances, but as evidence that English contract law can accommodate fairness-based principles without abandoning its commitment to certainty. Just as the development of frustration clarifies the limits of contractual autonomy in exceptional cases, recognising good faith as an overarching principle requires addressing whether it can be displaced by agreement. Contracting out of good faith would be intrinsically incompatible with good faith's role in upholding the reasonable expectations of the parties.

We shall now turn to developing good faith in the specific category of franchising contracts, which will posit that the application of good faith as a principle, when reinforced by adequate legislative measures in a particular area, can pave the way forward for good faith in other categories too.

[1087] *Socimer* (n 156) [116]; Peden, ''Implicit Good Faith' - or Do We Still Need an Implied Term of Good Faith?' (n 734) 12.
[1088] Mitchell, 'Obligations in Commercial Contracts: A Matter of Law or Interpretation?' (n 7) 480 also argues that interpretation cannot be commercial contract law's primary task; rather commercial contract law is a 'repository of independent and substantive normative principles concerning the importance of making and performing agreements' and can develop 'standards according to which commercial contractors should conduct their dealings.'

CHAPTER 5: A PRAGMATIC APPROACH TO A CONCRETE DUTY OF GOOD FAITH: FRANCHISING

5.1. Introduction

Franchising is a contractual arrangement between two legally and financially independent parties where close and ongoing collaboration is required.[1089] Franchising is a particularly relevant category of contracts for analysing the concept of good faith.[1090] It is intended to be of long-term duration which provides good faith with an adequate testing ground for performance related disputes.[1091] Franchising contract is labelled as relational, due to involving more than an exchange but an ongoing effort to achieve the aims of the contract.[1092] Indeed, Leggatt J in *Yam Seng* expressly mentioned franchise contracts as being relational, however, he did not extend the categorisation to all franchise contracts.[1093] Franchising is also an industry which ranges across all sectors of the market.[1094] The explicit references to duties of good faith in the European Code of Ethics for Franchising, which has been adopted by the BFA, indicate the franchise industry's demands and should be taken into account in deciding the future direction of the law.[1095]

Australia offers a relevant comparison for the possible future evolution of English law in this area. A statutory duty of good faith was enacted for franchising contracts, together with a restriction on unconscionable conduct in contract performance.[1096] The relevance of this

[1089] BFA, 'The Code of Ethics for Franchising' (n 65), s 1.
[1090] Rozenn Perrigot, Andrew Terry, Cary Di Lerna, 'Good Faith in Franchising -The Perceptions of Franchisees, Franchisors and Their Lawyers in the French Context' (2019) 47(3) International Journal of Retail & Distribution Management 246, 246.
[1091] Benjamin Klein, The Economics of Franchise Contracts, (1995) 2 Journal of Corporate Finance 9, 36, considers that franchising serves as a 'good laboratory in which to study contractual arrangements more generally due to having an 'accessible source of standardized contract [that] vary across franchise systems and across areas within a franchise system and have evolved over time in response to changes in market conditions.' They further provide an insight into the 'economics of distribution and more generally, with insights into the nature of all vertical relationships.'
[1092] See for instance, Macneil, 'Contracts: Adjustment of Long-Term Economic Relations under Classical, Neoclassical and Relational Contract Law?' (n 81), Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557), Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (n 281).
[1093] *Yam Seng* (n 3).
[1094] Perrigot, Terry, Di Lerna, 'Good Faith in Franchising -The Perceptions of Franchisees, Franchisors and Their Lawyers in the French Context' (n 1089) 247. Gary J Castrogiovanni, James G Combs, Robert T Justis, 'Resource Scarcity and Agency Theory Predictions Concerning the Continued Use of Franchising in Multi-outlet Networks' (2006) 44(1) Journal of Small Business Management 27, 28, state that franchising as a model of business is rapidly expanding throughout the world.
[1095] BFA, 'The Code of Ethics for Franchising' (n 65). On the importance of soft law, see Elise Bant, Jeannie M Paterson, 'Statutory Interpretation and the Critical Role of Soft Law Guidelines in Developing a Coherent Law of Remedies in Australia' in R Levy and others (eds), *New Directions for Law in Australia: Essays in Contemporary Law Reform* (Australian National University Press 2017).
[1096] For details, see chp 5.4.

chapter is that where good faith can successfully be recognised in a specific category of commercial contracts, the fear of it creating uncertainty in the application of the law would dissipate in time. Moreover, the reference to relational contracts would not be required, and an extension of the duty into other categories of commercial contracts would be more likely. Indeed, the case law indicates that rather than having certain categories of contracts, such as franchise, distributorship, or joint ventures, classified as relational contracts, the courts do not always automatically attribute such relationality to all of these categories.[1097] Instead, they look at the individual characteristics of each contract, which inevitably provides an unreliable criterion for categorising contracts.[1098] The current state of affairs, therefore, requires such uncertainty to be remedied.

Chapter 5.2 will present the particularities of franchise contracts and its challenges in terms of opportunistic behaviour. Chapter 5.3 will focus on the difficulties of regulating opportunistic behaviour in English franchise contracts. Chapter 5.4 will reveal the statutory route to good faith taken in Australian franchise contracts. The juxtaposition with the Australian system will serve to set the scene for the final chapter, where statutory reform for English law will be proposed.

5.2. Franchising Contracts in General

5.2.1. Franchising Contracts in England and Wales

Franchising offers the franchisee and the franchisor an opportunity to engage in commercial activities on the basis of a prescribed business model.[1099] The British Franchising Association (BFA)'s Code of Ethics defines franchising as

> a system of marketing goods and/or services and/or technology, which is based upon a close and ongoing collaboration between legally and financially separate and independent undertakings, the [f]ranchisor and its individual [f]ranchisees, whereby the

[1097] For instance, in *Jani-King (GB) Ltd v Pula Enterprises Ltd* [2007] EWHC 2433 (QB), despite being a franchise contract, the court refused to classify it as a relational one in this case and refused to imply duties of good faith.
[1098] Soper (n 60) 56, for instance, *D&G Cars* (n 49) is a 'fairly standard service contract,' *Essex County Council* a waste management plant contract, and *Amey Birmingham Highways Ltd* (n 801) was a 'PFI contract intended to run for 25 years (...),' all of which were classified as relational.
[1099] Castrogiovanni, Combs, Justis (n 1093) 27-28, the franchisor 'sells the right to use its trade name, operating systems, and product specifications to another firm (...). The franchisee is then permitted to develop one or more retail outlets that offer the franchisor's product or service and bear the franchisor's name.'

> [f]ranchisor grants its individual [f]ranchisee the right, and imposes the obligation, to conduct a business in accordance with the [f]ranchisor's concept.[1100]

The franchisee has the benefit of tapping into the franchisor's business knowledge, resources, guidance and reputation.[1101] The franchisor has the benefit of expanding its market reach meanwhile retaining control over the management of its brand and the quality of the product or the service without risking significant capital investment.[1102] The franchisee pays a fee for the use of the franchisor's brand and necessary tools, which can be in the form of a one-off payment or a continuing one based on the agreement.[1103] Typically, a franchise fee and the royalty payments are the main monetary terms of a franchise agreement. The franchise fee would usually be a pre-determined one-time fixed fee, and the royalty a periodic fee which would usually be expressed as a percentage of the sales revenue generated by the franchisee.[1104] It is intended as a mutually beneficial business model which is characterised by an interdependent nature in terms of its execution.[1105] By its very nature, an asymmetry of power underpins the franchise relationship. Even though the balance of power is tilted in favour of the franchisor, it would be inaccurate to claim that only the franchisor is capable of abusing this power.[1106] In fact, the franchisee, by its very access to the network and systems of the franchisor, is also in a privileged position and can cause great harm to the franchisor's brand and finances. The franchise relationship is essentially one that is characterised by an imbalance of power, but the abusive behaviour can happen by either party.[1107]

[1100] BFA, 'The Code of Ethics for Franchising' (n 65); the definition adopted is the one which is provided at s 1 of the European Code of Ethics for Franchising.

[1101] SooCheong (Shawn) Jang, Kwangmin Park, 'A Sustainable Franchisor-Franchisee Relationship Model: Toward the Franchise Win-Win Theory' (2019) 76 International Journal of Hospitality Management 13,13, posit franchising as a 'growth strategy for franchisors' and a 'risk-alleviation strategy for franchisees.'

[1102] Castrogiovanni, Combs, Justis (n 1093), 28; there are two important theories that seek to explain the choice for the model; first is the resource scarcity theory which 'asserts that firms offer franchises in their early years because they lack the managerial expertise and capital needed to grow, and the agency theory, which explains that 'firms franchise when doing so minimizes agency costs via the best available alignment between outlet managers' incentives and firms' objectives.'

[1103] Frank G Mathewson and Ralph A Winter, 'The Economics of Franchise Contracts' 28(3) Journal of Law & Economics 503, 503.

[1104] Jungwon Yeo, 'The Factors of Revenue-Sharing Contracts in Franchising: Evidence from the Korean Franchise Industry' (2022) 36(1) International Economic Journal 77, 99.

[1105] Klein (n 1090) 11; What distinguishes franchising from other types of contracts, such as manufacturing and distributorship is the exclusivity between the franchisee and franchisor, where the focus of the franchisee's business is exclusively the product line or service of the franchisor and its brand.

[1106] See discussion further below, chp 5.2.2 'Opportunistic Conduct in Franchising.'

[1107] Terry and Di Lernia, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions?' (n 465) 548.

Franchising contracts are different from most commercial agreements because they need to reflect the interdependent, ongoing and lengthy nature of the franchise relationship.[1108] The parties' obligations are not one-off exchanges capable of discharging the entire contract. Rather, the obligations have a variable nature which must overcome hurdles or adapt to market developments with a flexible and cooperative approach.[1109] Contracts that do not reflect these qualities are likely to disappoint the parties and cause disagreements on their respective expectations. The franchisor's power lies in its ability to negotiate terms which retain its control of the use of its brand, through strict terms and conditions imposed on the franchisee. Usually, these will be presented as standard form contracts to the franchisees, in particular where the franchisor is already an established actor in the market.[1110] This is to ensure a uniform implementation of the business model across its network. The terms and conditions of the franchisor are unlikely to be open to negotiation, and once the franchise is underway, amendments to obligations may be unilaterally made by the franchisor. When the agreements concluded are those on the standard terms of the franchisor, the franchisee's rights and obligations might appear disproportionate to those of the franchisor, in particular where the franchisee is making a substantial capital investment up front. Such contracts leave the franchisees at the mercy of the franchisors.[1111] Where the parties meet each other's expectations, there is unlikely to be an issue. However, where a party seeks to maximise its return on the franchise relationship at the expense of the other in an abusive manner, the law must regulate such contracts in light of their interdependent and cooperative nature.

Not all franchising businesses are the same. There are indeed different ways in which a franchising business can organise itself. If both the franchisor and the franchisee are in the UK, then the business will usually be the standard one where the franchisor grants a franchise to the

[1108] David A Baucus, Melissa S Baucus, Sherrie E Human, 'Consensus in Franchise Organizations: A Cooperative Arrangement Among Entrepreneurs' (1996) 11 Journal of Business Venturing 359, 361; although the importance of the formal contract is recognised, the relationship's cooperative character is also important in advancing the common aims of the business as a whole.

[1109] Jang and Park (n 1100) 17-20, propose a 'win-win theory' of understanding franchise relations that make them sustainable, and identify the following criteria as the core components of such sustainability: (i) relational satisfaction (ii) trust between parties understood as honesty, acting ethical and efficacious (iii) long-term commitment to the relationship.

[1110] Klein (n 1090) 11; '[b]usiness format franchises' entail a higher degree of integration than 'product or tradename franchises' because they adopt a highly standardised exclusive retail arrangement.

[1111] Jang and Park (n 1100) 19 explain that a franchisee's perception of the fairness of the franchisor may contribute to the breakdown of the relationship. Fairness may relate to the procedural aspects of the exchange, such as the consistency of the procedures relating to franchisees, or the resource allocation process not being made subject to arbitrary decisions.

franchisee.[1112] Where the franchisor is based abroad, the franchisor may set up a joint venture together with a local company.[1113] This model may be disadvantageous to the franchisor as it tips the balance of bargaining power in favour of the franchisee; topics such as control of the joint venture or the distribution of the dividends are likely to be heavily negotiated. For this reason, the franchisor might require that the joint venture also enter into a master franchise agreement. In such a scenario, the franchisor runs the risk that if there is an issue with the master franchisee, the relationship with the independent sub-franchisees might also be affected.[1114] An alternative is for the franchisor to agree to an area development agreement (or also referred to as a multi-unit development agreement) with a developer who will have the right and obligation to open a certain number of locations, which it will own following a specified schedule, but without the right to sub-franchise to third-parties. While the majority of franchises in England and Wales operate on a direct grant model basis, there are also a small number of franchisors operating on alternative models.[1115]

In practice, franchise agreements in England and Wales are granted for five years, although a substantial majority is granted for ten years or longer.[1116] They provide for know-how to be licensed to the franchisee rather than transferred, as the rights to the know-how will have to revert to the franchisor at the end of the contract. Continuing fees to be paid by the franchisee to the franchisor are usually referred to as 'management service fees' rather than 'royalties' due to tax reasons, and most are calculated as a percentage of the franchisee's turnover.[1117] In addition, an advertising and promotion fee is also usually charged to the franchisee.[1118] Although the franchisor may opt to grant exclusive territory to the franchisee, this is not always the case. Further, it may be that the franchisor reserves its own right to trade within a sole territory.[1119]

The distinct nature of the franchising transaction has empowered its actors to define franchising as an industry. Although the industry of franchising can cover a wide range of goods and services, its essence is the standardisation of production, service delivery, and the

[1112] John Pratt and Hamilton Pratt, 'England and Wales' in D Campbell (ed), *International Franchising* (2nd edn, Juris Publishing 2022) 41.
[1113] ibid.
[1114] ibid.
[1115] ibid 4-5; the Trading Schemes Act 1996 and the market size of England and Wales may present an obstacle in area development agreements being widespread.
[1116] ibid 14.
[1117] ibid 15.
[1118] ibid, the average service management fee is usually between 8% and 9% of turnover, and the advertising and promotions fee is usually 2% of turnover.
[1119] ibid, it is estimated that around 70% of franchisors actually grant exclusive territories.

use of know-how.[1120] Such a unique feature makes franchising easy to export as a business model across borders. Even where exported, the basis of the operation ultimately is entrenched in a contractual document. Where franchising is seen as an industry, this allows considering its development within a wider scheme of governance, by identifying applicable trade norms, drafting self-imposed regulation, and further enquiring about whether legislation is needed to better serve its advancement. The franchising contract undoubtedly exists against the backdrop of its industrial organisation, which should factor into how the judiciary should view the legal characteristics of the individual franchise contract.

5.2.2. Opportunistic Conduct in Franchising

The inherent imbalance in the franchising relationship can put the franchisee at risk of the franchisor's opportunistic behaviour through exploitation of such imbalance.[1121] By the same token, the interdependent nature of the relationship also puts the franchisor at risk of opportunistic behaviour at the hands of a franchisee. The negative repercussions of opportunistic conduct in a single relationship can seep into the whole franchise network and the franchising industry as a whole.[1122] The imbalance itself is not a defect of the franchise relationships, which need to be corrected. Indeed, in the heart of the franchise relationship lies the conflicting interests of the franchisor to maintain quality control, and those of the franchisee to protect itself against the opportunism of the franchisor. The danger of abuse is inherent in the structure of franchising itself.[1123] Curbing opportunism can be done through various methods, ranging from a set of strict compulsory legislative rules of conduct to express clauses in individual contracts.[1124]

[1120] Veronica L Taylor, 'Contracts with the Lot: Franchises, Good Faith and Contract Regulation' (1997) 4 New Zealand Law Review 459, 465.

[1121] Alexander Rosado-Serrano, Justin Paul, 'A New Conceptual Model for International Franchising' (2018) 75 International Journal of Hospitality Management 179, 181, opportunism refers to 'actions taken by one contract partner to achieve their own goals which are apparently harmful to other contract partners.' In the context of franchisee opportunism, this may be, for example, by way of 'wilfully disregarding the franchisor's goals in pursuit of their own entrepreneurial interests,' or by engaging 'in criminal activities that can put in risk the franchisor; such as hacking POS systems to manipulate gift cards or other information.'

[1122] Jule B Gassenheimer, David B Baucus, Melissa S Baucus, 'Cooperative Arrangements among Entrepreneurs: An Analysis of Opportunism and Communication in Franchise Structures' (1996) 36 Journal of Business Research 67, 70, 76, opportunism 'impact[s] outcomes of cooperative arrangements, such as franchisee satisfaction and franchise system performance.'

[1123] Hadfield (n 63) 969.

[1124] Klein (n 1090) 17, recognises that the complexity of the franchise relationship cannot be perfectly regulated in a contract in a way to assure the parties' performance. Indeed, '[s]pecifications of or proxies for desired behavior are necessarily imperfect because desired behavior is extremely complex and difficult to measure, with contract specifications only incompletely covering all the many elements of performance and all the potential unforseen future contingencies.'

The franchisor will aim to establish and maintain the overall network of franchises to maximise returns through the licensing of its intellectual property and the collection of royalties across the franchise system. From the franchisor's perspective, the franchisor has ownership of the business model it has created. Yet, the individual franchise business will be an independent business existing separately from that of the franchisor.[1125] A potential problem is that of 'free-riding' by the franchisee, which equates to an underperformance on the part of the franchisee.[1126] Indeed, the franchisee will primarily be concerned with the level of profits generated by its individual business. The franchisee will have little interest in increasing the profits to benefit the franchisor, unless the franchisee receives a proportion of such benefits too. The franchisee will have no interest in undertaking any efforts or expenditures that will not be ultimately compensated.[1127] Conversely, where the franchisee decides to use the brand reputation of the franchise and offer substandard goods or services, any damages to the brand reputation would have to be shouldered not only by that specific franchisee, but by the entire network thereby potentially affecting the franchisor's future endeavours in selling more franchises and increasing its royalty revenues. Therefore, the franchisor would seek to curb such behaviour to achieve consistent delivery of goods and services to protect the brand reputation.[1128]

The franchisee's focus will be on its own unit franchise or franchises. It will be vulnerable to the franchisor's opportunistic behaviour in a way different to that of its potential opportunistic behaviour towards the franchisor.[1129] The interests between the parties may further diverge when those of the franchisor, as central management and the franchisee, as a unit, become irreconcilable. For instance, the franchisor may wish to saturate the market with as many franchisees as possible, whereas the franchisee would want to preserve its territorial claim in the market. Where the franchisor is seeking to impose a unified strategy which may

[1125] Baucus, Baucus, Human (n 1107) 362, the issues a franchisor may face are numerous, such as a franchisee 'ignoring franchisors' goals in pursuit of their own entrepreneurial interests, possibly misrepresenting costs and revenues, or by withholding royalties' or 'disagree[ing] about competitive methods, refus[ing] to participate in innovative marketing strategies, deviat[ing] from the franchisor's formula, resist[ing] changes needed to keep the system competitive, (...).'

[1126] Jeannie M Paterson, 'Good Faith in Commercial Contracts? A Franchising Case Study' (2001) 29 Australian Business Law Review 270, 281; Muris (n 109) 523; Hadfield (n 63) 949.

[1127] Klein (n 1090) 12.

[1128] ibid, 18-19, the author posits that the franchising contract which prescribes acceptable behaviour is only one of the ways in which the franchisor can use the threat of termination to incentivise the franchisee's performance. Another way for the contract is to operate as a 'self-enforcement mechanism' where the terms provide for 'sufficient rents or a future "premium stream" which, combined with the threat of termination, produce the incentive to perform.'

[1129] Baucus, Baucus, Human (n 1107) 362.

not be in favour of some of its franchisees, these franchisees may nevertheless agree to certain requests or changes to the contract by the franchisor under threat of termination by the franchisor and risk losing any upfront investment.[1130] Where the tools, skills, or any assets acquired given entering into the franchise agreement cannot be repurposed by the franchisee to recover the cost of investment in case of termination, the franchisee may be in a precarious position where it is forced to operate under the new terms imposed by the franchisor. This initial allocation of capital required of the franchisee is effectively sunk costs, which cannot be recovered if the franchisee were to cease trading.[1131] It is such costs that the franchisor has shifted onto the franchisee in exchange of risking the licensing of its brand.[1132] Indeed, sunk costs are crucial in gauging the opportunistic behaviour of the franchisor because the franchisee may have to continue operating despite not recovering its sunk costs, due to the franchisor's decisions which induce further losses short of pushing the franchisee out of business. The franchisor can do this in several ways, for instance (i) directly by raising the price of goods supplied to the franchisee, by increase rent or royalties, diverting advertising or training funds into self-benefiting purposes; or (ii) indirectly, by requesting that the franchisee makes excessive advertising investment, or participates in promotional programmes which are not cost-effective, or undertakes unnecessary renovations.[1133]

As a heavily reliant business on the know-how and the business competence of the franchisor, any poor management or negligence of the franchisor in addressing the business needs of its franchisees may jeopardise a franchisee's business. This may also be due to a conscious decision from the franchisor in helping out some franchisees and not others to fulfil an ulterior motive in self-interest. These types of behaviour are sometimes described as franchisees being 'held-up' by the franchisor.[1134] Holding-up behaviour may occur in various ways.[1135] For instance, the franchisor 'may increase the price of goods supplied to the franchisee or the rate of fees charged;' it may 'insist that the franchisee take excess stock held by the franchisor even though the franchisee will have difficulty selling the stock;' it may

[1130] Unilateral variation clauses in favour of franchisors including unilateral changes to operations manuals which bind the franchisees further compound the risk of opportunistic behaviour against franchisees, see Parliament of Australia, Opportunity Not Opportunism: Improving Conduct in Australian Franchising, 1 December 2008, <https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Completed_inquiries/2008-10/franchising/report/index> accessed 3 April 2025, 54.
[1131] Baucus, Baucus, Human (n 1107) 361; for instance, franchisees may have to purchase 'assets such as prepackaged business format, formal training, marketing strategy, operating procedures, and communications with their franchisor.
[1132] Hadfield (n 63) 986.
[1133] ibid 952.
[1134] ibid 282.
[1135] ibid 951.

'introduce new operating requirements which return less than proportionate benefits to individual outlets;' or 'introduce increasingly onerous changes to the system to drive the franchisee to terminate the franchise and to take over a profitable outlet for itself.'[1136]

Another way in which the franchisee may become disgruntled with the franchise is where the franchisor, having usually given itself a wide range of discretions under the contract, decides to make inappropriate use of them for originally unintended purposes. For instance, the franchisor may be seeking to replace the franchisor with a new one on better terms for itself, to overtake the franchisee's business for itself, or open new franchises in close proximity. The franchisee's expectations about renewal of the contract may also not be fulfilled as originally signalled by the franchisor. The franchisee may not be able to recoup its original investment, which could cause significant financial hardship to the franchisee where the contract is not renewed. Another potentially damaging behaviour is that of encroachment, where the franchisor authorises a new unit or operations within an existing unit within the franchisee's market area.[1137] The issue is further compounded by the internet, as the expansion of the franchisor's units can reach beyond territorial restrictions and tap into markets where there is direct competition with an already established franchisee. [1138] The phenomenon is more likely where the franchise network matures, and the franchisor has more financial resources to expand into new markets or seek to buy back its franchises to operate a company-owned unit rather than an independent franchise.[1139]

5.3. Challenges of Regulating Unfairness in the Performance of Franchise Contracts

[1136] Parliament of Australia, Opportunity Not Opportunism: Improving Conduct in Australian Franchising, 1 December 2008, <https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Completed_inquiries/2008-10/franchising/report/index> accessed 3 April 2025, 54.

[1137] Encroachment has been seen as an essential franchising issue in the US for many years, see RW Emerson, 'Franchise Encroachment' (2010) 47 American Business Law Journal 191, 193. However, in England and Wales, there are no statutory laws governing the issue of competing franchisees being granted territories in close proximity where one franchisee claims that its business is being affected due to such proximity. It may be that the non-derogation from grant principle can be applied where this issue arises where one franchisee is deprived from the enjoyment of the benefit conferred by the franchising contract.

[1138] Rozenn Perrigot, Guy Basset, Gerard Cliquet, 'E-commerce Opportunities and Challenges for Franchise Chains' in Hoy F, Perrigot R, Terry A (eds), *Handbook of Research on Franchising* (Edward Elgar Publishing 2017) ch 14.

[1139] Emerson, 'Franchise Encroachment' (n 1136) 202.

5.3.1. Categorisation of the Franchise Contract

A franchise contract is viewed as one which lies in the intermediate range between employment and independent contracting contracts.[1140] The franchisor's control of the trade mark and the know-how moves the scale towards an employment contract classification, whereas the franchisee's ownership of its own unit moves it towards the independent contractor model. Due to its unique nature, English courts have continuously struggled to determine the nature of the franchise relationship. In *Jani-King*, an argument that an obligation of trust and confidence should be implied into the contract failed.[1141] The court considered that (i) the term did not satisfy the test of necessity and that the contract could function perfectly without it; (ii) that where the contract was a complex commercial contract with negotiated terms, the court should be slow to imply terms in broad and imprecise language, and (iii) that commercial contracts are not employment contracts therefore do not justify such implication unless the franchise contract can be considered to be akin to an employment contract.[1142] The court found that the franchise contract was not to be considered akin to an employment contract because first, the agreement expressly stated the parties to be independent contractors, and second, that there are established authorities stating that the relationship is more akin to that between lessor and lessee rather than that of employer and employee.[1143] On the latter point, the court cited *Kall Kwik Printing (UK) Ltd v Rush,* in which the court had to consider the validity of a non-compete clause in a franchising agreement in light of the restraint of trade doctrine. In that context, the court stated that 'one way of perhaps looking at a franchise agreement is that this is a form of lease of goodwill for a term of years, with an obligation on the tenant, as it were, to retransfer the subject matter of the lease at the end of the lease in whatever state it is.[1144] The court highlighted the importance of identifying the nature of the relationship by situating it on a spectrum ranging between employer and employee relationships and vendor and purchaser ones, considering that franchise agreements are no longer viewed as akin to an employer and employee relationship.[1145]

In another case, which was cited in *Jani-King*, the court in *Dyno-Rod Plc v Reeve* had to decide on the breach of a restrictive covenant in a franchise agreement.[1146] Neuberger J said

[1140] Hadfield (n 63) 932.
[1141] *Jani-King* (n 1096).
[1142] ibid [48]-[50] (Peter Coulson QC J)
[1143] ibid [52].
[1144] [1996] FSR 114, 119 (Cooke J).
[1145] ibid 118.
[1146] [1999] FSR 148.

that a franchise agreement would come closer to qualifying as a vendor and purchaser agreement than one of employment.[1147] Consequently, the courts' attempts at assimilating franchising contracts to other categories of contracts must be viewed as unsatisfactory. The contortions in addressing whether a duty of trust and confidence could arise in a franchising contract show the reluctance of the courts in recognising that applications of legal rules by analogy can only take the law so far. Effectively, comparing franchising contracts to other types of contracts is problematic because it results in a conception of the commercial relationship that is defective and distorted. The franchise contract is essentially interdependent, and 'symbiotic' as recognised by Neuberger J himself in *Dyno-Rod v Reeve*.[1148]

From the perspective of the relational theorist, the franchising contract offers, no doubt, a fertile ground for exemplifying the relational framework.[1149] Whilst categorisation of contracts on the basis of being relational is problematic, an interpretation of contracts from a contextual point of view is crucial.[1150] Indeed, 'relation' can have various meanings; it can be the individual transactions which actually take place within the contractual framework, the respective strength of the parties in terms of their bargaining power, or it may also mean the position of the franchisee within the network and its relative importance to the franchisor.[1151] The point of departure to adjudicate commercial disputes is necessarily the contract however, an explicit recognition of good faith in contractual performance requires that the complexity of the contractual relationship be understood.

To avoid the limitations presented by the relation framework, a RGSC categorisation of franchising contracts would be most appropriate for implying duties of good faith.[1152] Indeed, franchising is a RGSC par excellence. The mutual efforts of the parties determine the success of the business and the respective rate of individual profits.[1153] Although English law

[1147] ibid 153 (Neuberger J).
[1148] ibid.
[1149] See for instance Macneil, 'Contracts: Adjustment of Long-Term Economic Relations under Classical, Neoclassical and Relational Contract Law? (n 81), Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (n 557), Viven-Wilksch, 'The Importance of Being Relational: Comparative Reflections on Relational Contracts in Australia and the United Kingdom' (n 281).
[1149] *Yam Seng* (n 3).
[1150] For issues raised by a relational categorisation, see discussion in chp 3.2.3.1.1 and 3.2.3.1.2.
[1151] Hadfield (n 63) 956.
[1152] A recent empirical study involving 300 restaurant franchise contracts in the South Korean franchise industry indeed confirmed the role of revenue-sharing as a tool to align the conflicting interests of the contracting parties and its use as a commitment device to a continued collaborative partnership between franchisors and franchisees due to the proportional link between royalty payments and the level of sales generated by the franchisee, see Yeo (n 1103) 100.
[1153] Chp 3.2.3.1.2.

does not recognise the concept of network contracts, it would be an unrealistic approach to ignore the nexus which qualifies franchising contracts.[1154] Whether the network is made up of a few franchisees or hundreds, the franchisor's focus would be expanding it, as it is an expansionist model by design. Therefore, the franchisor may find itself making decisions prioritising the interests of the whole network, and ultimately of itself, rather than the interests of the individual franchisor in a particular contract. This may lead to discriminatory conduct by the franchisor amongst its franchisees. For instance, the franchisor may choose to allow certain outlets to prosper and not others, either due to strategic business decisions on the future of the network or for no reasonable basis for such a decision. A breach of a good faith duty by the parties would entail the assessment of the reasonable expectations of the parties. The fact that the individual franchise is situated within a network serves only to inform the reasonable expectations of the parties within the individual contract. Therefore, the assessment of the conduct is made at the level of the individual franchisee contract, and not at the level of the franchising network as a whole. Undoubtedly, the objective assessment of the reasonable expectations will require a consideration of the context and the community standards which apply in the context of that particular franchise contract. Yet, a duty of loyalty would not be owed to the network but to the contracting party.[1155]

5.3.2. Curbing Opportunism in the Performance of Franchising Contracts

This definition puts a strong emphasis on franchising fundamentally being the licensing of the brand and a management consulting service, underlining the franchisor's obligations as being crucial to the exchange. Yet, the collaborative component of the exchange is also recognised, without which neither party could essentially profit from the whole enterprise. Despite the impression given by the definition as to the parties being on equal footing, a further reading of other sections of the Code is necessary to understand that this is not the case and that safeguards must exist against opportunism in the performance of the franchise contract. We now turn to such safeguards.

Unsurprisingly, the lack of a cohesive basis for addressing unfairness in contract performance discussed above is also clearly visible in the context of franchising contracts.[1156] In *Fleet Mobile Tyres Ltd v Stone*, the Court of Appeal applied the non-derogation from grant

[1154] See the discussion on networks in chp 3.2.3.1.1 above.
[1155] ibid.
[1156] See chp 2.

doctrine in favour of the franchisee.[1157] The franchise was a mobile tyre-fitting service. The franchisor also operated an online service for supplying and fitting various types of tyres under the 'eTyres' brand. The franchisor would essentially receive the order from the customer online and pass it on to its franchisees to execute. The franchisor terminated the agreement, alleging breach, following which the franchisee continued to trade in a way which would have contravened the restrictive covenants if valid. Although there was nothing in the contract preventing an online sale by the franchisor, the eTyres business was less profitable for the franchisee.[1158] The court considered that such an operation amounted to substantial impairment of the franchisee's rights under the agreement and amounted to a derogation from the grant of a franchise. The court's decision emanated from an interpretation of the contract with detailed provisions as to the rights of the parties. Relying on the decision in *Esso Petroleum Company Limited v Addison*, the court stated that the rights of the parties have to be understood 'by reference to the contract as a whole having due regard to its commercial context.'[1159] The interpretation of the contract did not allow for an understanding that the franchisor had 'an unfettered power' to exercise its contractual right to amend the contract but rather that the franchisor's right was subject to the limitation that in the absence of an express clause, the parties must be taken not to have intended 'to make significant derogations through the operation of a subsidiary clause from the primary benefits intended to be conferred under it.'[1160] In short, the franchisor's right was to be curtailed where the franchisee's contractual right to operate and promote the business under the brand name was substantially impeded. The 'substantial impediment' criterion was justified by the court 'because it cannot have been intended that the claimant was entitled to do anything so long as it fell short of a total impairment or extinguishment.'[1161] Arguably, the case could have been decided simply by way of interpreting the contract. The reference to the doctrine of non-derogation from grant seems to have facilitated the court's imposing of a qualifying criterion on the exercise of the rights of the franchisor. The issue is of course that the doctrine is usually used in the context of restrictive covenants in certain types of contracts, such as leases; however, it is accepted that other commercial contracts also can rely on the use of the doctrine, '[t]he principle may have evolved

[1157] [2006] EWCA Civ 1209. Keene LJ delivered the judgment, with whom Wall and Wilson LJJ agreed.
[1158] The franchisor's online business had a different brand name and the franchisor fixed the prices for that work, whereas the franchisee fixed the prices for the work with customers not originating from the online business of the franchisor. The franchisor effectively required the franchisee to promote the online business above the other business.
[1159] *Fleet Mobile Tyres* (n 1156) [54] (Keene LJ, citing Moore-Bick J *in Esso Petroleum Company Limited v Addison [2003] EWHC 1730 (Comm))*.
[1160] *Fleet Mobile Tyres* (n 1156), [54]-[55].
[1161] ibid [56].

principally in the field of real property but it is one of wider application.[1162] It is 'a principle which merely embodies in a legal maxim a rule of common honesty. It was imposed in the interest of fair dealing.'[1163]

As discussed in chapters 3 and 4, the courts restrain the application of a good faith duty to instances where an implication can be made into the contract by traditional methods, or where there is an express good faith term, that is interpreted and applied in a restrictive way. Typically, franchise contracts would be standard form documents drafted in favour of the franchisor, where the franchisor will reserve considerable discretion in performing its own obligations or amending the contract at its sole discretion.[1164] The franchisors may attempt to curb all scenarios of opportunism by resorting to extensive provisions detailing the obligations of the franchisees, and by providing for catch-all type standards (such as diligent performance, reasonableness, use of best efforts) to ensure the franchisee's adequate performance. There may even be an express clause of good faith inserted in favour of the franchisor or both the franchisor and the franchisee.[1165] Indeed, before *Yam Seng*, express good faith duties were required by the franchisee towards the franchisor; however, since *Yam Seng*, the franchisors have also self-imposed good faith duties to 'mitigate the risk of the court imposing wider and less certain implied obligations.'[1166] The franchisor's wish to keep a tight control over the entire system by providing itself with contractual rights, including extensive termination rights, to ensure uniformity in the network is understandable. However, fostering a relationship based on trust and honesty would also benefit the franchisor in the long run, therefore it would not be unusual to see contractual terms in favour of the franchisees where for instance the franchisor's termination rights are curtailed by precise qualifying scenarios or maximum levels which can only be altered by mutual agreement expressly agreed in the contract.[1167] In any event, any attempt to curb opportunism by express good faith clauses would be very restrictive, as the decisions in *Berkeley*, *Medirest* or more recently in *Aston Martin* have indicated.[1168]

[1162] ibid [53].
[1163] ibid, Keene LJ citing Nicholls LJ in *Johnston and Sons Ltd v Holland* [1988] 3 WLUK 22, where derogation from grant was applied in the context of a claim for interference with the use and enjoyment of leasehold property.
[1164] Terry and Di Lernia, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions?' (n 465) 563.
[1165] Pratt and Pratt (n 1111) eng/26.
[1166] John Pratt and James Barrett, 'Franchising in the United Kingdom' (2018) 38(1) Franchise Law Journal 1, 4.
[1167] Paterson, 'Good Faith in Commercial Contracts? A Franchising Case Study' (n 1125) 284.
[1168] *Berkeley* (n 1022), *Medirest* (n 97), *Aston Martin* (n 1035). *Mackie Motors (Brechin)* (n 49) [56-60] (Asplin LJ) is another recent case concerning a deal between a dealership, a manufacturer and the manufacturer's finance company. The claimant sought to argue that there was an implied umbrella 'relational' agreement with an implied term of good faith to allow for a longer notice period for termination. The court refused to imply an umbrella contract, and stated that even if such contract were to be found, a good faith duty could not be implied because it

Furthermore, *Yam Seng*'s qualification of franchising contracts as relational, which should have an implied duty of good faith, was not uniformly adopted in later decisions. Indeed, the usual constraints applied to good faith in commercial contracts continued to affect franchising contracts post-*Yam Seng*. In *Carewatch***,** where *Yam Seng* was tested in a franchise context, the court refused to find an implied duty of good faith or an implied positive obligation that a party to a contract should subordinate its own commercial interests to those of the other party.[1169] The application of *Yam Seng* in *Carewatch* was problematic due to mainly two reasons. First, the franchisees attempted to argue that a number of imprecise obligations should be implied into the contract, including alongside good faith, but the court refused on the basis that the terms were 'wide and imprecise' and unnecessary in a negotiated, detailed agreement.[1170] Second, the franchisees themselves were in breach of an express term of the agreement by running a competing business in parallel, and therefore, it would have been problematic to find that the franchisor was in breach of an implied duty of good faith where it could have terminated the contract for repudiatory breach.[1171] The decision was subject to criticism for failing to imply good faith as the franchise agreement in question 'was no more detailed than the great majority of the franchise agreements and contained no express terms which, in a franchising context, were unusual or could be construed as preventing an obligation of good faith arising.'[1172] The court's focus on the very detailed express terms should not have been interpreted as there being no 'clear lacuna,' as the same could be said for all franchise agreements.[1173]

In fettering contractual discretions in franchise contracts, the courts have been uncommitted to consistently adopting a good faith assessment too.[1174] Recently, in *Hunters Franchising Ltd*, the court restricted the assessment of the reasonableness of the decision based

would contravene to the express terms of the agreements in place between the claimant and the financing company.

[1169] *Carewatch* (n 3). In a more recent case, *Ellis & Ors v John Benson Ltd* [2025] EWHC 2096 (KB) [2025] 8 WLUK 84 [291] (Freedman J), the court recognised good faith duties in the context of franchising by way of an implied term in fact. The court did not accept that the relational features of franchising justify an automatic implication of good faith across all franchising agreements [292-300]. The case confirms that the courts remain more comfortable with implication in fact given that the law has not yet 'reached a stage where such an implied term as a matter of law can be implied into every franchise agreement' [297]. The subsequent costs' decision which also refused a permission to appeal the case by the franchisor also confirmed that the case turned on its facts, and was not intended to define the content or scope of good faith in franchising contracts generally, *Ellis & Ors v John Benson Ltd* [2025] EWHC 2257 (KB) [2025] 9 WLUK 9 [2025] Costs LR 1525 [23-25].

[1170] ibid [109], [119] (Henderson J).

[1171] ibid [125**]**.

[1172] Pratt and Pratt (n 1111) eng/28.

[1173] ibid.

[1174] *Hunters Franchising Ltd v Brybond Ltd* [2022] EWHC 3195 (Comm).

on the *Braganza* principle, where the discretion had to be exercised honestly, rationally and for the purpose for which it was conferred.[1175] Whilst the court was not required to consider whether a general duty of good faith exists, the court did consider the distinction between the *Braganza* principle and good faith.[1176] The court stated that a *Braganza* duty differs from a general implied duty of good faith and applies only where one party can exercise discretion on a matter that affects both parties with differing interests.[1177] However, the courts are usually more comfortable subjecting the use of contractual discretion to good faith than applying it to any other aspects of the franchising contract. Therefore, limitations set out in earlier case law, such as *Paragon Finance*, *Socimer* or *Esso Petroleum v Addison*, are more likely to be consistently applied in franchise contracts too.[1178]

Where the franchisors are 'denied the protection of broad powers of control over the operations of their franchise,' it is envisaged that they would 'be likely to substitute other methods of safeguarding their interests' such as charging increased fees, or compose onerous obligations of compliance and reporting, or 'not to invoke the franchise form at all.'[1179] The status quo favours the franchisor's position as it is the party with the stronger bargaining power, and therefore able to negotiate better terms for itself. The systemic nature of the imbalance in franchisor and franchisee contracts requires that the courts develop better tools for dealing with franchisor opportunism.[1180] The franchisee has limited options when the franchisor fails to act in a cooperative manner, without necessarily being in contradiction with the express terms of the agreement. A possible avenue for the franchisee would be to argue that the failure of the franchisor violates the reasonable expectations of the parties.[1181] A contextual reading of the contract can also potentially arrive at the same result by taking into account the upfront investment made by the franchisee, which would not have been made if it did not expect to

[1175] *Braganza* (n 583) [116] (Klein J). The case concerned a master regional development agreement in which Hunters exercised its right to withdraw the exclusivity granted to Brybond in its territory where Brybond failed to meet its development targets, which it had. Brybond was under an obligation to propose potential franchisees which, at Hunters' discretion, could be approved or disapproved. Brybond argued that Hunters breached the *Braganza* duty by disapproving potential franchisees. The court held that Hunters had clear policies in place which it applied consistently regarding the allocation of exclusive franchise territories, and that its decision was motivated by a commercial justification of reducing conflict between the franchisees and in pursuit of the common purpose of developing the Hunters brand in the given jurisdiction [126-127, 132].
[1176] *Hunters* (n 1173) [107] (Klein J), the defendant reframed its original complaint which had argued an implication on the basis of good faith for fettering contractual discretion, by replacing it with an argument on basis of a breach of a *Braganza* implied term.
[1177] ibid [109].
[1178] *Paragon Finance* (n 583), *Socimer* (n 156) or *Esso Petroleum* (n 1158).
[1179] Paterson, 'Good Faith in Commercial Contracts? A Franchising Case Study' (n 1125) 286.
[1180] Robert W Emerson, 'The Faithless Franchisor: Rethinking Good Faith in Franchising' (2021) 24 University of Pennsylvania Journal of Business Law 411, 430.
[1181] Chp 1.3.1.2.

recoup it by way of profits.[1182] The generation of profits is undoubtedly a joint effort in the context of franchising, and a good faith duty in the form of a duty to cooperate can inform the franchisee's reasonable expectations. However, the franchisee would be confronted with the hurdle of the traditional implication tests or the provisions of the agreement, which are usually extensively drafted and negate any possibility of there being a gap to fill.[1183] More expansively, instead of an implication, the conduct can be interpreted to be contrary to good faith due to a violation of the applicable business community standards.[1184] Essentially, these are the standards which determine whether the decision of the parties made business common sense in the context of their agreement. A good faith standard, which manifests through a reference to the reasonable expectations of the parties would not be an external standard but one based on the contract. This is because good faith is to be applied as an objective standard of conduct, and not a subjective one and with an understanding that the parties are to be deemed to be rational actors.[1185]

5.3.3. British Franchise Association's Code of Ethics for Franchising

As discussed above, franchise agreements are not subject to a general duty of good faith under the common law or any statutory provision. Curbing the opportunism of the parties in the context of a franchising contract will fall heavily onto the common law.[1186] For instance, the principle of 'non-derogation from grant' may be relevant where a party confers a benefit to the other and can be prevented from doing anything that substantially deprives that party of the enjoyment of that benefit.[1187] Where the contract contains an exemption clause to limit or exclude the liability of the franchisor to a franchisee, the UCTA 1977 may be triggered where the contract is concluded in a standard form contract.[1188] In such a case, the clause will have to be subject to a reasonableness test. The application of the UCTA 1977 is limited and cannot provide a solution for all unfairness issues in contractual performance.[1189]

[1182] Paterson, 'Good Faith in Commercial Contracts? A Franchising Case Study' (n 1125) 287.
[1183] As seen in *Carewatch* (n 3).
[1184] This would require a contextual approach as discussed in chp 4.2.
[1185] See discussion above in chp 4.2.
[1186] Pratt and Pratt (n 1111) eng/4. There are some statutes that are relevant for franchising but fall outside the scope of this research, such as the Trading Schemes Act 1996 or Competition Act 1998.
[1187] *Fleet Mobile Tyres* (n 1156).
[1188] Pratt and Barrett (n 1165) 17.
[1189] This will further be discussed in chp 6.4.2. Collins, 'Discretionary Powers in Contracts' (n 565) 236, 241 in examining the fettering of contractual discretions, also posits in regards to UCTA 1977 that despite the potential for abuse of discretionary power being relevant to the question of fairness or reasonableness of a contractual clause, 'the claim that it has in fact been abused by the power-holder is not determinative of the question whether the insertion of the power was unfair from the outset.' Rather, it is the good faith standard, subject to a test of

Given the inadequacy of the above controls on contract performance, the BFA has published a self-imposed code of ethics ('BFA Code') which must be adopted and respected by its members.[1190] Not all franchisors are members of the BFA as they would have to comply with its disciplinary, complaints, appeals, Advertising Standards Agency's Code of Advertising Practice, the BFA Code and certain reporting requirements. Although the BFA Code is voluntary, its content is insightful as it presumably indicates the most efficient rules which the industry has opted into rather than relying solely on the common law to avoid and resolve its potential disputes.[1191] The BFA Code is based upon the European Code of Ethics for franchising promulgated by the European Franchise Federation. The BFA has also published a guide to supplement the BFA Code titled 'Understanding the Code of Ethics.'[1192] The BFA Code applies only to BFA members, but in *Drivertime Recruitment Ltd re DST Ltd*, the court recognised the BFA Code's importance in assessing the behaviour of franchisors generally.[1193] Indeed, the court stated that the BFA Code's requirements 'indicate a standard of commercial morality which can usefully be applied in this unregulated industry.'[1194]

The BFA Code is useful in particular because the empirical research on the common types and frequency of contract clauses is limited.[1195] Nevertheless, a few simple generalisations can be drawn from the case law and the BFA Code. The franchise contract is expected to be long-term and a continuous one, where the parties each have their continuous obligations towards the other. The franchise contract is usually a standard form contract which will be drafted by the franchisor, without much possibility for the franchisee to negotiate any amendments. The duties are owed upwards by the franchisee; in comparison, those owed by the franchisor are limited. Rather than attempting to provide for all future eventualities, it restricts its bounds to delineating the framework underlying the commercial exchange by providing for the respective rights and obligations of the parties. The contract is focused on setting out the extensive obligations of the franchisee and the protections accorded to the franchisor in respect of its trademark and know-how. The franchising contract is, therefore,

irrationality, which asks whether the power was exercised capriciously or for an improper motive that helps with adjudicating unfairness in the use of contractual discretions.

[1190] BFA, 'The Code of Ethics for Franchising' (n 65).

[1191] For the discussion on efficiency of rules, see chp 1.2.1.

[1192] BFA, 'Understanding the Code of Ethics' (*BFA*, 2023) (published but not in the public domain).

[1193] [2004] EWHC 1637 (Ch), the case involved the winding up of a franchisor that was not a BFA member.

[1194] ibid [168].

[1195] For a list of empirical research in the US, see Hadfield (n 63) 939. These enumerate clauses on the franchisor's obligations on training, advertising, territorial scope of the franchise; the obligations of the franchisee, including to build or lease buildings, equipment or supplies, to maintain standards, to meet layout requirements, to pay royalties; the clauses on the trademark and licensing; and termination.

incomplete by its very nature because it is simply not possible for a contract designed to be long-term to accommodate all future scenarios.[1196]

The BFA provides for an informal conciliation, mediation and arbitration scheme for its members to resolve disputes.[1197] Conciliation is where the BFA acts as an intermediary between the parties to facilitate dialogue.[1198] If the parties cannot resolve their dispute, they can also try the mediation services of the BFA.[1199] If mediation fails, the parties can then seek to resolve their dispute through BFA arbitration or the courts. However, the BFA does not have any enforcement powers if the provisions of its code are breached. The most drastic action it can take is to terminate the membership of the member in question. There is a lack of transparency and data in terms of issues raised by franchisees within the BFA since it does not publish any statistics. Therefore, where the parties wish to formally resolve their dispute, they can either have recourse to arbitration or litigation.[1200] The lack of impetus for franchise regulation by successive UK governments is attributed to the rarity of complaints about franchising.[1201] More importantly, the lack of comprehensive and accurate information concerning all aspects of franchising nationally impedes shaping future policies on the topic. Although there may be reluctance on the part of franchisors to have a regulated industry, the industry's success depends on an accurate assessment of existing issues to further its development. However, the industry is growing fast, and an increase in court disputes regarding contractual performance is not difficult to envisage. Previous research has linked franchising to literature on small and medium-sized businesses, thereby acknowledging the inherent imbalance in the relationship between the franchisor and the franchisee.[1202] Where contractual opportunism becomes an increasing problem, the government may be obliged to consider

[1196] Hadfield (n 63) 947-948.
[1197] Pratt and Barrett (n 1165) 13.
[1198] BFA, 'BFA Dispute Resolution: Informal Conciliation Application' (BFA, 2024) <https://www.thebfa.org/wp-content/uploads/Informal-Conciliation-Application-Form-2023.pdf? accessed 3 April 2025.
[1199] BFA, 'BFA Dispute Resolution: Mediation Scheme Rules' (BFA, 2024) <https://www.thebfa.org/wp-content/uploads/Mediation-Rules-2023.pdf> accessed 3 April 2025.
[1200] For most breach of contract claims, parties usually prefer litigation to arbitration, see Lee Plave, 'Comparative Guides - Franchising' (Mondaq) <https://www.mondaq.com/Guides/Results/18/1223/all/UK-Franchising-Guide> accessed 3 April 2025, question 15.
[1201] Pratt and Barrett (n 1165) 2. Unfortunately, the Commercial Court does not break down the categories of claims by type, see Courts and Tribunals Judiciary, 'Business and Property Courts, The Commercial Court Report 2022-2023 (Including the Admiralty Court Report)' (n 183) 22.
[1202] See for instance, David Kirby, Anna Watson, 'Franchising as a Small Business Development Strategy: A Qualitative Study of Operational and ''Failed'' Franchisors in the UK' (1999) 6(4) Journal of Small Business and Enterprise Development 341; John Stanworth, Celia Stanworth, Anna Watson, David Purdy, Simon Healeas, 'Franchising as a Small Business Growth Strategy: A Resource-Based View of Organisational Development' (2004) 22(6) International Small Business Journal 539.

legislative intervention, in particular to protect the interests of the franchisees.[1203] We shall now turn to the Australian experience of a statutory good faith duty in franchising to envisage the future regulation of unfairness in the performance of franchising contracts in English law.

5.4. The Australian Experience of a Statutory Duty of Good Faith

Franchising in Australia has gained popularity since the 1960s with the introduction of fast food chains.[1204] The growth in the industry is attributed to the absence of 'intrusive regulatory controls at state and federal level, an increasingly affluent local population, and a willingness of the Australian people to accept new ideas and foreign investment.'[1205] Several issues were recurrent in the industry, such as 'insufficient disclosure by franchisors, pressure on franchisees to "sign-up," unconscionable conduct by franchisors, and a perception that franchising was generating a large number of disputes.'[1206] Although the number of litigated cases was few, they were important in 'crystallis[ing] conflicting views about how law and legal institutions should handle continuing relational contracts.'[1207] Indeed, the franchisors would insist on 'contract predictability and protection from overreaching claims for compensation by franchisees,' whereas the franchisees would require that the court takes a contextual view of the contract with 'trust, reliance and commercial morality' taken into account.[1208] Gradually, demand for greater industry regulation increased, which led to the formation of the Franchise Association of Australia (FAA) in 1981, which later became the Franchise Council of Australia (FCA), to represent the interests of both the franchisors and the franchisees.[1209] In 1998, the Franchising Code of Conduct (FCOC) was enacted into law through the Trade Practices Act 1974 (Cth).[1210] Although there were fears that extensive legal regulation would drive away franchisors, the franchising sector consistently continued to grow over the years in Australia.[1211] By enacting good faith into law, Australia joined in the

[1203] There may be various reasons why disgruntled franchisees chose not to litigate their disputes in public courts, whether due to reputational fears or the high costs involved, therefore the number of cases that reach the courts should not assume that disputes are not occurring in private forums, and the government should look at other factors for devising future policies on the topic in order to preempt future hindrances to the development of the sector, see Taylor (n 1119) 474.
[1204] Owen Wright, Andrew McAuley, 'Australian Franchising Research: Review, Synthesis and Future Research Directions' (2012) 20 Australasian Marketing Journal 158, 158.
[1205] ibid.
[1206] Taylor (n 1119) 471.
[1207] ibid 476.
[1208] ibid.
[1209] Wright, McAuley (n 1203). The demand for legislation may have been 'prompted by the publicised failure of a number of "home-grown" franchises during the 1980s,' see Taylor (n 1119) 471.
[1210] Wright, McAuley (n 1203) 159, for an historical overview of how the industry moved from an unregulated to a regulated one. Also see Taylor (n 1119) 471.
[1211] Wright, McAuley (n 1203) 159.

international trade that set standards for gauging contractual behaviour, rather than 'bright-line rules.'[1212] This section will first look at good faith generally in Australia (chapter 5.4.1), then explore good faith in franchising as a statutory norm (chapter 5.4.2) and finally explore the convergence of good faith and unconscionable conduct (chapter 5.4.3).

5.4.1. Good Faith in Australia

The development of the Australian concept of good faith can be traced back to the duty of cooperation.[1213] *Mackay* was later relied on by Australian cases to provide support for recognising a duty of cooperation within commercial contracts.[1214] In the context of a lease dispute, in *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pyt Ltd*, the court stated, in referring to *Mackay*, 'it is common ground that the contract imposed an implied obligation on each party to do all that was reasonably necessary to secure performance of the contract.'[1215] The court also stated that to imply such a duty where it was necessary to the performance of the contract by the parties, then the correct interpretation of the contract would depend on ascertaining the intention of the parties as manifested by the contract itself, rather than guided by a general rule of construction.[1216] The duty was said not to override express provisions of the contract, and was rather understood as a general rule of construction, to secure performance as far as reasonably necessary.[1217] The duty to cooperate in the performance of the contract has become well-established, being implied only where necessary to perform the contract as intended, and where not inconsistent with an express term.[1218] Later cases brought the two concepts together, where the duty to cooperate was understood to mean acting reasonably and in good faith.[1219] The Federal Court further emphasised that the duty to cooperate 'is not a mechanism for alleviating the consequences of hard, even harsh or unconscionable, contractual provision.'[1220] It is a duty which compels the parties to take a reasonable approach to contractual performance by taking into account the interests of the other party. The duty to cooperate was gradually overtaken by references to good faith, which came

[1212] Taylor (n 1119) 478.
[1213] Jessica Viven-Wilksch, 'Good Faith in Contracts: Australia at the Crossroads' (2019) 1 Journal of Commonwealth Law 273, 285-286<https://www.journalofcommonwealthlaw.org/article/10809-good-faith-in-contracts-australia-at-the-crossroads> accessed 3 April 2025.
[1214] *Mackay* (n 992).
[1215] (1979) 144 CLR 596 [607] (Mason J).
[1216] ibid [607]-[608].
[1217] *Servcorp WA Pty Ltd v Perron Investments Pty Ltd* [2016] WASCA 79 [81-83].
[1218] Peden, 'Incorporating Terms of Good Faith in Contract Law in Australia' (n 883) 222, 231; Viven-Wilksch, 'Good Faith in Contracts: Australia at the Crossroads' (n 1212**)** 279.
[1219] *Council of the City of Sydney v Goldspar Australia Pty Limited* [2006] FCA 472, [166].
[1220] ibid [162].

to increasingly occupy the spotlight. The New South Wales Court of Appeal decision in *Renard Constructions* is considered to be a landmark in that it recognised the possibility of implying good faith in the performance of Australian contracts.[1221]

In *Renard Constructions*, the New South Wales court held that in exercising a right under a contract, including a power to vary or terminate a construction contract, the principal must act reasonably. In doing so, the court effectively implied a duty to act in good faith, failing to decide whether it was implied in law or in fact. This was later followed in a series of decisions by New South Wales courts, some holding that such a duty could be implied by law into all types of commercial contracts. For instance, in *Alcatel Australia Limited v Scarcella & Ors*, a duty of good faith and reasonableness was implied into a lease contract in performing and exercising the rights in the contract. The implication was made as a matter of law. The court equated good faith to the cumulation of (i) an obligation on the parties to cooperate in achieving the contractual objects, (ii) compliance with honest standards of conduct, and (iii) compliance with standards of contract which are reasonable having regard to the interests of the parties.[1222] However, this approach does not necessarily reflect the one adopted in other Australian states. For instance, in Victoria, the Court of Appeal has rejected the proposition that there must be a good faith duty in all commercial contracts. In *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL* the court stated that where the application of a good faith duty would create uncertainty in commerce, then it should not be implied, in particular because good faith may be 'no more than a duty to act reasonable in performance and enforcement' which is a long-established duty.[1223] Other state courts also had trouble implying good faith into contracts, which contributed to the uncertain and tortured development of the doctrine of good faith in Australia.[1224] To date, it cannot be said with certainty that there is a general principle of good faith which operates in Australian contract law.[1225]

Nevertheless, a recent case has attempted to clarify the content of the duty. In *Virk Pty Ltd (in liq) v YUM! Restaurants Australia Pty Ltd*, the Federal Court simplified the formulation

[1221] *Renard Constructions* (n 133); Viven-Wilksch, 'Good Faith in Contracts: Australia at the Crossroads' (n 1212**)** 281.
[1222] (1998) 44 NSWLR 349, 367 (Sheller JA, with whom Powell and Beazley JJA agree). These notions are based on Mason, 'Contract, Good Faith and Equitable Standards in Fair Dealing' (n 3).
[1223] [2005] VSCA 228 (Warren CJ).
[1224] Tyrone M Carlin, 'The Rise (and Fall?) of Implied Duties of Good Faith in Contractual Performance in Australia' (2002) 25(1) University of New South Wales Law Journal 99, 122.
[1225] Terry and Lernia (n 465) 543, 547-548; Viven-Wilksch, 'Good Faith in Contracts: Australia at the Crossroads' (n 1212) 276, 299; Benjamin Djung, 'The Statutory Role of Good Faith in Franchising' (2017) 15(1) Canberra Law Review 1, 6.

of a duty of good faith in exercising a right or a power as being conduct which is 'capricious, dishonest, unconscionable, arbitrary or the product of a motive which was antithetical to the object of the contractual power.'[1226] Furthermore, the court held that reasonableness and good faith should not be viewed distinctly; rather, it should be expressed as one of good faith and reasonableness. Indeed, reasonableness is not to be held 'akin to a tortious duty to exercise due care and skill or to produce a reasonable outcome,' rather it should relate to the quality of the conduct as simplified above.[1227] The assessment of the conduct is objective and is 'adjudicated upon the evidence in a particular case and the context of the particular contract, having regard to acceptable norms of commercial conduct.'[1228] This reasoning has confirmed the earlier approach taken by the New South Wales Court of Appeal in *Burger King Corporation v Hungry Jack's Pty Limited*.[1229] The parties had entered into a franchising agreement, followed by subsequent agreements, including a Development Agreement in dispute. Under the latter, the franchisee had an unrestricted, non-exclusive right to develop restaurants throughout Australia. Following various disputes between the parties over the years, the franchisor terminated the agreement, alleging breach by the franchisee of the franchise agreement. The court held that the franchisor had breached an implied duty of good faith in exercising its right to terminate.[1230] The court considered that 'the franchisor was acting as part of a 'deliberate plan to prevent the [franchisee] expanding' to further expand in the market itself.[1231] The right to terminate could not be exercised 'for a purpose foreign to that for which it was granted, such as to thwart the respondent's right to develop and ultimately procure a situation where the Agreement could be terminated.'[1232] The implication was made in law, with an indication that obligations of good faith and reasonableness will be more readily implied in the case of standard form contracts, in particular where they provide for a general power of termination.[1233] The court also confirmed that there is no distinction of substance between the notion of reasonableness and good faith in Australian law.[1234] Moreover, the court rejected the argument that a duty of good faith should mean that a party must subjugate its interests to those of the other (referring to this as the 'fiduciary duty').[1235]

[1226] [2017] FCFCA 190 [164].
[1227] ibid.
[1228] ibid [183].
[1229] [2001] NSWCA 187.
[1230] ibid [186].
[1231] ibid [639].
[1232] ibid [187].
[1233] ibid [163], [165].
[1234] ibid [169].
[1235] ibid [187].

With franchising contracts, in general, the courts had a relatively clear approach. In *Far Horizons Pty Ltd v McDonalds Australia Ltd*, the Victorian Supreme Court stated that 'there is to be implied in a franchise agreement a term of good faith and fair dealing which obliges each party to exercise the powers conferred upon it by the agreement in good faith and reasonably, and not capriciously or for some extraneous purpose.'[1236] In a later case, in *AMC Commercial Cleaning (NSW) Pty Ltd v Coade*, the court found that a franchisor was bound by a duty of good faith, which was breached by serving a 'default notice' which was baseless, amongst other breaches. In other words, the franchisor had to act reasonably and honestly, and not act for an ulterior motive, which did not mean that it had to subjugate its interests to those of the franchisee.[1237] The court in *Meridian Retail Pty Ltd v Australian Unity Retail Network Pty Ltd* recognised that the debate of a duty of good faith in franchising contracts would revolve closely around the relational nature of the contract. Indeed, 'the implication of an obligation of good faith may be particularly appropriate in the context of a franchise relationship, doubtless because it frequently embodies a significant disparity of bargaining power.'[1238] However, this would entail that a duty of good faith would not be applicable where the franchisee is not vulnerable or has considerable bargaining power relative to the franchisor. The hesitation of the common law in implying duties of good faith into franchising contracts was later superseded by a statutory enactment in regards to small businesses, as explained in the next section below. While this was a big step forward in favour of good faith being normalised in commercial relationships, the common law remains responsible for regulating a relatively smaller number of franchise cases, which may involve disputes between parties on equal footing in terms of their bargaining power, and other types of commercial contracts.

5.4.2. Good Faith as a Statutory Norm

Franchising is a significant industry in Australia. It generates an approximate turnover of $201.2 billion in 2024-2025 and employs an estimated 549,000 people with a total of 1,234 businesses.[1239] The industry is diverse in its composition.[1240] Around 90% of the franchising

[1236] [2002] VSC 310 [120], the court did not find that McDonalds was in breach of such duty by not offering the claimant the license to operate a new restaurant in proximity to the claimant's restaurant, finding that McDonalds had legitimate business reasons for such a decision.
[1237] [2010] NSWSC 832.
[1238] [2006] VSC 223 [211], the court concluded in the case that there was no breach of a duty of good faith.
[1239] Claudia Burgio-Ficca, 'Franchising in Australia - Market Research Report (2015-2030)' (*IBISWorld*, January 2025) <https://www.ibisworld.com/au/industry/franchising/1902/> accessed 3 April 2025.
[1240] ibid.

systems are small businesses.[1241] Being a multicultural market, the consumer behaviour and franchisee composition is influenced by European, Asian, subcontinental and African migration in addition to influences by the US and the UK.[1242]

The FCOC is the main instrument to regulate the parties' conduct to a franchising agreement at the federal level.[1243] The latest version came into force on 1st of April 2025 and was promulgated under the Competition and Consumer Act 2010 (CCA 2010).[1244] The regular revisions to the FCOC are testament to the Australian Government's ability to implement new provisions more efficiently than other countries, such as the US.[1245] Despite its name, it is black letter law which is situated within the CCA 2010. The ACCC is responsible for enforcing the FCOC.[1246] The FCOC defines at its section 7 a franchising contract to be one where one party (the franchisor) grants the other (the franchisee) the right to carry on a business in Australia supplying or distributing goods or services under a system or marketing plan, where such business is substantially determined, controlled, or suggested by the franchisor; and where the operation of the business is substantially or materially associated with a particular trademark, marketing or commercial symbol owned, used, licensed, or specified by the franchisor; and where the franchisee must make, or agree to make, certain types of payments to the franchisor, before starting or continuing the business.[1247]

In an attempt to codify the common law principle of good faith, the FCOC provides at its s 18(1) that [1248]

[1241] Australian Department of the Treasury, 'Review of the Franchising Code of Conduct Consultation Paper' (August 2023) <https://treasury.gov.au/sites/default/files/2023-08/c2023-436091cp.pdf> accessed 3 April 2025, 7.

[1242] Franchise Council of Australia (2024) <https://franchise.org.au/> accessed 3 April 2025.

[1243] Relevant state laws relate to real estate and retail leasing, health and safety, and tax laws, whereas local laws deal mainly with real estate zoning and property rates and charges, Stephen Giles, Nigel Jones, 'Franchising Law and Practice in Australia' (2019) 38(4) Franchise Law Journal 583, 584.

[1244] Competition and Consumer (Industry Codes—Franchising) Regulation 2024 (Cth). The FCOC is due for statutory review before 1st of April 2030 to assess it impact and operation (FCOC, chp 1, pt 3, s 12).

[1245] Natalie Sears, 'Australia's Updated Franchise Code of Conduct: Does an Express Obligation of Good Faith Benefit the Franchisor and Franchisee' (2014) 20(1) Law and Business Review of the Americas 121, 122. The previous version of the FCOC, the Competition and Consumer (Industry Codes—Franchising) Regulation 2014 (Cth), was in force since 1 January 2015, which had itself replaced the Franchising Code of Conduct 1998.

[1246]Another key government body is the Australian Small Business and Family Enterprise Ombudsman ('ASBFEO') that supports small businesses, including franchising-based ones, to resolve disputes through mandatory dispute resolution frameworks, including the one provided for in FCOC. The Franchise Council of Australia, the equivalent of the British Franchise Association, is the industry body which has a role in safeguarding the reputation of franchising and educating the sector, and representing it before governments or regulators where needed. However, it is not legally responsible for supervising the enforcement of the FCOC.

[1247] A motor vehicle dealership agreement is also held to be a franchise agreement for the purposes of the FCOC, s 7(2)(c).

[1248] The FCOC obligation of good faith is intended to codify rather than substantially modify the common law obligation of good faith, see Michael Schaper, 'Independent Review of the Franchising Code of Conduct'

> [e]ach party to a franchise agreement must act towards another party with good faith, within the meaning of the unwritten law from time to time, in respect of any matter arising under or in relation to:
> (a) the agreement; and
> (b) this code.[1249]

It further indicates the factors which the court may have regard to in determining a breach of the obligation to act in good faith. For this, it provides at its s 18(3) that

> [w]ithout limiting the matters to which a court may have regard for the purpose of determining whether a party to a franchise agreement has contravened subsection
> (a) for all agreements - the court may have regard to:
> (i) whether the party acted honestly and not arbitrarily; and
> (ii) whether the party cooperated to achieve the purposes of the agreement;
> (…)

The ACCC further clarifies on its website that good faith, although not defined in the FCOC, must follow the definition of the common law, which currently means that 'the parties must exercise their powers reasonably and not arbitrarily or for some irrelevant purpose.'[1250] Dishonest conduct or failure to have regard to the legitimate interests of the other party is explicitly understood to be a breach of the good faith obligation.[1251] Examples can include a franchisor who fails to prevent online sales to customers within the exclusive territory of a

(Australian Department of the Treasury, December 2023) <https://treasury.gov.au/sites/default/files/2024-02/p2024-487230.pdf> accessed 3 April 2025, 61. This review was done in relation to the previous FCOC, however no changes were introduced in relation to good faith provisions under the new FCOC. The Government, in response to the review, stated that it will task the Australian Small Business and Family Enterprise Ombudsman with leading the development of best practice guidance, in consultation with the franchising sector and the ACCC and other relevant agencies to 'improve the comparability and publication of franchising data sets' in order to help provide further guidance on good faith requirements, see Australian Department of the Treasury, 'Government response to the Independent Review of the Franchising Code of Conduct' (May 2024) <https://treasury.gov.au/sites/default/files/2024-05/p2024-525558.pdf> accessed 3 April 2025, 4.

[1249] The good faith obligation is envisaged to apply to all aspects of the franchising relationship, including pre-contractual negotiations, performance of the contract, dispute resolution and the termination of the agreement (s 18(2) FCOC).

[1250] Australian Competition and Consumer Commission, 'Acting in Good Faith under the Franchising Code' (ACCC) <https://www.accc.gov.au/business/industry-codes/franchising-code-of-conduct/about-franchising/acting-in-good-faith-under-the-franchising-code> accessed 3 April 2025. Indeed, good faith is 'within the meaning of the unwritten law from time to time' (s 18(1) of the FCOC).

[1251] ACCC, 'Acting in Good Faith under the Franchising Code' (n 1249), to prevent potential breaches, the ACCC provides the following list of questions as a guideline for good faith conduct: 'Have you been honest with the other party? Have you considered the other party's interests? Have you made timely decisions? Have you consulted with the other party about issues or proposed changes? Do you have a contractual right to act in that way? Are you imposing any conditions on the other party? Are those conditions necessary to protect your interests? Where a dispute has arisen, have you attempted to resolve the dispute directly with the other party or through mediation? Are you acting for some ulterior purpose?'

franchisee; a franchisee who misleads customers that they are dealing with the franchisor where the franchisee used the franchisor's confidential client lists to 'take over' its clients; or a franchisor terminating the agreement for the franchisee' failure to comply with invoicing and reporting requirements where the franchisor failed itself to resolve invoicing and reporting issues raised earlier by the franchisee.[1252] Conversely, it is unlikely to be a breach of good faith duties where the franchisor opens a new unit itself and fails to give a franchisee the option to open it in its territory where there is no exclusivity and where the franchisee has previously failed to satisfy the franchisor's criteria to operate another unit.[1253] Moreover, it does not allow the franchisor to opt out of the above good faith obligation or to limit its scope.[1254] In section 18(4), it states that '[a] franchisor must not enter into a franchise agreement that includes a provision that limits or excludes, or purports to limit or exclude, the obligation to act in good faith.' It clarifies at its section 18(6) that 'the obligation to act in good faith does not prevent a party to a franchise agreement, or a person who proposes to become such a party, from acting in the party's, or the person's, legitimate commercial interests.' Indeed, a party is free to have regard for its own legitimate commercial interests. If the franchise agreement does not grant the franchisee the option to renew or extend the agreement, section 18(7) makes it clear that this alone does not mean the franchisor has breached the above obligation of good faith.[1255] All contraventions to good faith carry a civil penalty and can be levied by the ACCC.

The good faith obligation is supplemented by other sections which seek to curb any opportunistic behaviour. For instance, section 62 of the FCOC provides that the franchisor cannot unilaterally vary the agreement with retrospective effect unless the franchisee has given written consent to the variation. The extensive pre-contractual disclosure obligation imposed upon the franchisor also supplements the good faith obligation. For instance, in the case of unilateral variations, the franchisor must have expressly informed the franchisee of circumstances where the franchisor may unilaterally vary the agreement to be able to enforce such a right.[1256] Similarly, where the franchisor requests additional payments from the franchisee where the franchisor seeks to implement a change to the business, such as the

[1252] ibid.
[1253] ibid.
[1254] FCOC, s 18(4). Djung (n 1224) 15.
[1255] It was also recently confirmed by the Federal Court in *AHG WA (2015) Pty Ltd v Mercedes-Benz Australia/Pacific Pty Ltd* [2023] FCA 1022 exercising a power of non-renewal without cause does not contravene to the good faith obligation. Such an obligation does not expect the contract to continue indefinitely or prevent a party from acting in its own legitimate commercial interest. Even where a franchisee may be worse off due to a change to the contract by the franchisor, this does not necessarily constitute unconscionable conduct.
[1256] FCOC, s 20 and schedule 1 s 17.

adoption of innovative technology or a branding change related expenses, significant capital expenditure by the franchisee will be prohibited by the FCOC unless (i) the expenditure was disclosed to the franchisee in the disclosure document prior entry into the agreement or renewal of the agreement; or (ii) all franchisees are required to undertake the expenditure, then all or a majority of franchisees approve the expenditure, or (iii) the expenditure is necessary to comply with legislative obligations; or (iv) the expenditure is agreed by the franchisee.[1257]

The FCOC does not cover all franchising agreements.[1258] There are certain contracts which fall outside the scope of the FCOC. These serve to balance competing public policy interests, despite being mandatory in their application. Where public interest trumps the application of the FCOC, the FCOC is pushed aside. Otherwise, it is the main piece of applicable regulation to franchising contracts.[1259] The curtailing of public policy interests is done through competing pieces of legislation, which give way to more important pieces of regulation where needed. For instance, the FCOC does not apply to cooperatives, mutual entities, or contracts where other mandatory industry codes apply, such as the Oil Code of Conduct between wholesale suppliers and fuel resellers. Another exception which disapplies the FCOC is where the agreement is for goods and services that are substantially the same as those supplied by the franchisee for at least two years immediately before the contract date, and are likely to provide no more than 20% of the franchisee's gross turnover for goods or services in the first year of the franchise.[1260] Conversely, there are special provisions that apply to automotive franchise agreements. For such contracts, the FCOC requires the court to

[1257] FCOC, s 60 and schedule 1 s 14.

[1258] ACCC, 'Franchising Laws Including the Code' (*ACCC*, 2025) <https://www.accc.gov.au/business/industry-codes/franchising-code-of-conduct/about-franchising/franchising-laws-including-the-code> accessed 3 April 2025.

[1259] There exist other pieces of relevant legislation governing business relationships and fair trading which may be applicable such as competition and consumer laws however they remain outside the scope of this work. However, the recent rehaul on the 9th of November 2023 to unfair contract term provision (which include for instance the Australian Consumer Law 2010 (Cth) also have an effect on the regulation of franchising contracts, see ACCC, 'Unfair Contract Terms in Franchise Agreements' (ACCC, 15 December 2023) <https://www.accc.gov.au/system/files/unfair-contract-terms-franchise-agreements.pdf> accessed 3 April 2025. The new provisions prohibit standard form contracts with a small business or consumer containing unfair contract terms or to rely or purport to rely upon such terms, breach of which can impose significant financial penalties. Small business is defined as one employing fewer than 100 persons, or with an annual turnover of less than A$ 10 million. Typically, problematic terms include unilateral variation clauses to the price or other supply or acquisition of goods or services, automatic renewal clauses, especially with short notice, unilateral termination clauses or unjust fee clauses such as early termination penalties.

[1260] This is because it is recognised that the likelihood for opportunistic behaviour is significantly reduced because of the experience or sophistication of both parties, Australian Department of the Treasury, 'Review of the Franchising Code of Conduct Consultation Paper' (n 1240) 10.

consider whether the terms of a franchise agreement are fair and reasonable, which is in addition to the requirements provided under sections 18(1) and 18(3) discussed above.[1261]

In response to the consultation paper on the previous FCOC, industry-wide feedback was sought on its application and suitability for the purpose. [1262] The ACCC stated that the franchisors' alleged failure to act in good faith was consistently one of the top three issues raised by franchisees.[1263] The FCOC's permission to allow franchisors to prefer their own commercial interest instead of the franchisees was a problematic point for franchisees, stating that franchising, under the current code, was effectively 'a license to exploit.'[1264] The recommendation by the franchisees was to clarify and strengthen the provisions in the FCOC by providing examples or by requesting that the franchisors be required to consider and justify the impact of the commercial decision on franchisees before acting in their own commercial interests.[1265] Conversely, the franchisors submitted that the good faith obligation restricted their opportunities to decisively act in the case of a poor-performing franchisee causing significant damage to the overall system.[1266] Moreover, some stakeholders considered that no changes are required and the FCOC as it stands is clear, in particular in light of the recent case law such as the *AHG WA (2015) Pty Ltd v Mercedes-Benz Australia/Pacific Pty Ltd* case decision which further clarified the good faith principle in regards to motor vehicle agreements.[1267] In essence, good faith is fulfilled when the party exercising a power under a contract acts reasonably.[1268] Essentially, the uncertainty in the application of a good faith obligation is recognised, but it is accepted as being 'a feature of flexible principle-based laws.'[1269] Therefore, no recommendation was made to further exemplify specific actions of bad faith or clarify 'legitimate commercial interest' in FCOC, as this would inevitably undermine the clear and developing jurisprudence and limit the purposefully flexible nature of the obligation.[1270] The provision on good faith in the FCOC is deemed to be fit for a franchising contract, where, in

[1261] FCOC, s 18(3)(b).
[1262] Schaper (n 1247).
[1263] ibid 60.
[1264] ibid, referring to the Submission on behalf of the Australian Association of Franchisees.
[1265] ibid, referring to ASBFEO's Franchising Code Review Submission.
[1266] ibid 61, referring to The Australian Automotive Aftermarket Association Response to the Franchising Code of Conduct Consultation Paper.
[1267] ibid, referring to the Federal Chamber of Automotive Industries Submission to the Review of the Franchising Code of Conduct Consultation Paper. For case reference, see n 1254 above. Another recent case clarifying the duty of good faith is *Virk Pty Ltd (in liq) v YUM! Restaurants Australia Pty Ltd* (n 1225).
[1268] Giles and Jones (n 1242) 589.
[1269] Schaper (n 1247) 61.
[1270] ibid 61-62.

particular, other norms continue to operate in parallel to further curb opportunistic behaviour in such contracts.[1271] Now we shall look at one of these norms.

5.4.3. Convergence of Good Faith and Unconscionable Conduct

One of the norms curbing opportunistic behaviour is the CCA 2010 Sch 2, which encompasses Australian consumer law, and prohibits unconscionable conduct between businesses.[1272] Usually, opportunistic behaviour in franchising contracts is presented as a breach of the FCOC's disclosure or good faith obligations or as unconscionable conduct under the CCA 2010.[1273] The latter was considered as an alternative to the obligation of good faith in the drafting of FCOC, but it was 'deemed to require too onerous a standard of proof for the purposes of franchising.'[1274] The prohibition of unconscionable behaviour in the CCA 2010 is usually referred to as statutory unconscionability, as opposed to equitable unconscionability, which is provided for under s 20 of the CCA 2010.[1275] Unconscionability is defined as conduct which goes 'against good conscience as judged against the norms of society.'[1276] To help the courts in their determination of unconscionable conduct, the CCA 2010 provides for a non-exhaustive list of factors to consider on a case-by-case basis, including the relative strengths of the bargaining positions, whether the stronger party has imposed conditions that aren't reasonably necessary to protect their legitimate interests, and the extent to which the parties acted in good faith.[1277]

Recently, the Commonwealth Federal Court in *Australian Competition and Consumer Commission v Quantum Housing Group Pty Ltd* held that while exploitation of some

[1271] ibid 62.
[1272] CCA 2010, s 21. Another norm curbing opportunistic behaviour between businesses in Australia is contained in ss 23 and 24 of the CCA 2010. These prohibit unfair contract terms contained in standard form contracts between small businesses, breach of which can lead to financial penalties by the ACCC. According to ACCC, a significant proportion of franchisees are likely to be protected under these provisions, see ACCC, 'Unfair Contract Terms in Franchise Agreements' (n 1258).
[1273] For statistical information, see Commonwealth Department of Jobs and Small Business, 'Parliamentary Joint Committee on Corporations and Financial Services, Inquiry into the Operation and Effectiveness of the Franchising Code of Conduct' (4 May 2018) <https://www.aph.gov.au/DocumentStore.ashx?id=d2597a27-4fb5-4ceb-98a8-6f6efb6d6c73&subId=565813> accessed 3 April 2025. The report states that in 2018, breaches of the obligation to act in good faith constituted 18% of all mediation requests under the FCOC, which was the second most disputed issue after the breach of the franchise agreement. Moreover, in 71% of disputes, the franchisees were the ones to start the mediation process.
[1274] Schaper (n 1247) 61.
[1275] CCA 2010 Sch 2, s 20 provides for prohibition of unconscionable conduct within the meaning of the unwritten law, i.e. under the doctrine of unconscionability in equity.
[1276] Australian Department of the Treasury, 'Unfair Trading Practices - Consultation Regulation Impact Statement' (August 2023) <https://treasury.gov.au/sites/default/files/2023-08/c2023-430458-cris1.pdf> accessed 3 April 2025, 13.
[1277] CCA 2010, s 22.

vulnerability or disadvantage will be a feature of unconscionable conduct, such conduct is not a prerequisite to establishing statutory unconscionability.[1278] The defendant company arranged investments in properties that qualified for the affordable housing scheme run by the government, which made available incentives to those who built or offered affordable rental accommodation. The defendant would receive the incentives and pass them on to its investors. This meant that the defendant was in a superior bargaining position as the investors were reliant on the defendant for the incentives. The defendant pressured the investors, with whom it had separate agreements, to obtain property management services from property managers that were chosen by the defendant. The proceedings were brought by the ACCC alleging that such conduct was unconscionable under the CCA 2010. The Federal Court clarified that even though the investors were sophisticated commercial parties who were not subject to a special vulnerability or disadvantage, the defendant's conduct could still amount to unconscionable behaviour under the CCA 2010.[1279] In its decision, the court took into account, among other factors, the 'dishonest lack of good faith' which was exhibited by the defendant's unjustified and unnecessary requirement to switch property managers for the defendant to extract financial benefits which were undisclosed to the investors.[1280]

Despite a statutory provision providing for unconscionability, which seeks to have a wider scope than that of equitable unconscionability, it is considered that statutory unconscionability is limited in its ability to curb unfair practices because it is not equivalent to unfair conduct and requires a high threshold of misconduct to be met.[1281] Therefore, there is a gap in the law which does not catch unfair conduct which falls short of the threshold for unconscionability; however the concern currently seems to be limited to consumer cases.[1282] In response to this gap, a review of the current regulation on unfair trade practices is being undertaken.[1283] The consultation sought a response in regards to four options. First option proposed no change, acknowledging that the limitations of the current system whereby unfair trading practices are not covered by existing regulations would continue, with consumers and

[1278] [2021] FCAFC 40; whereas such conduct would be required to establish an equitable unconscionability, [2].
[1279] ibid [4].
[1280] ibid.
[1281] Australian Department of the Treasury, 'Unfair Trading Practices - Consultation Regulation Impact Statement' (n 1275) 14.
[1282] ibid, equitable unconscionability's scope is narrower than statutory unconscionability. Equitable unconscionability 'prohibits a business from taking advantage of a consumer's special disadvantage. A special disadvantage may be age, sickness, illiteracy, lack of education, a language barrier, or some other factor or combination of factors, which seriously affects a person's ability to make a judgment as to their own best interests.'
[1283] ibid.

small businesses bearing financial and non-financial costs of such practices, with no effective options for redress.[1284] The second option proposed to broaden the scope of statutory unconscionable conduct by imposing on courts an obligation to assess unfair conduct as a factor in determining whether conduct is unconscionable. This option acknowledged that a new body of judicial precedent would need time to develop, meanwhile leaving businesses exposed to such trading practices, and acknowledges transition costs on businesses and regulatory bodies.[1285] The third option proposed to create a new general prohibition across all sectors on unfair trading practices that carry civil penalties for breach. This could be achieved either by adopting a flexible and principles-based norm of conduct, or by providing for an explicit definition of what constitutes an unfair practice.[1286] The ultimate goal would be that the norm be adept at adapting to technological and commercial change. This approach, as with the previous option, recognised the compliance costs on businesses and enforcement costs on regulators, the time needed to develop judicial precedent, and the uncertainty that this may create for parties in the interim.[1287] The fourth option proposed a combination of the third option with an added list of specific prohibited practices, which was revealed to be to most popular option amongst the stakeholders.[1288] Despite being mainly focused on consumer protection and small businesses, the supplemental consultation on the design of proposed general and specific prohibitions indicates that a staged approach is envisaged, initially applying a general prohibition of unfair trading practices in B2C contracts, then gradually to all B2B dealings, thereby allowing the case law to develop and provide better commercial certainty in the operation of the prohibition.[1288] Whilst the concerns for the previous option remain valid for this one, it would align Australia with other international jurisdictions and better protect the market players against opportunistic behaviour where currently applicable protections fail. Despite the envisaged reform, a criticism may be made as to the failure of the courts in recent case law to seize the opportunity to expand the scope of statutory unconscionability beyond an equitable one.[1289] In the face of new forms of misconduct that do

[1284] ibid 22.
[1285] ibid 24.
[1286] ibid 25.
[1287] ibid 26.
[1288] Australian Department of the Treasury, 'Unfair Trading Practices Consultation on the Design of Proposed General and Specific Prohibitions' (November 2024) <https://treasury.gov.au/sites/default/files/2024-11/c2024-602157-cp.pdf> accessed 3 April 2025, 3, 25. Once the consultation process has concluded, the Treasury will publish a Decision Regulation Impact Statement outlining the evidence gathered and the preferred policy approach.
[1289] Jeannie M Paterson, Elise Bant, Nicholas Felstead, Eugene Twomey, 'Beyond the Unwritten Law: The Limits of Statutory Unconscionable Conduct' (2023) 17(1) Journal of Equity 1, 4.

not amount to overt advantage taking, more subtle forms of misuse of influence will be better served by a flexible approach to statutory unconscionability.[1290] Indeed, if the courts do not adopt a progressive approach to the statutory prohibition, it may be 'time to recognise its limits and adopt a differently expressed safety net standard.'[1291]

5.5. Conclusion

The examination of franchising contracts and the role of good faith in contractual performance reveals a complex interplay between legal obligations and ethical considerations. As the industry continues to grow and face challenges, the promotion of transparency, accountability, and ethical conduct remains paramount for fostering trust and sustainability in franchising relationships and the industry as a whole. The reference to good faith in BFA's voluntary code of conduct signifies a commitment to ethical standards that can influence the future direction of franchise law. However, the absence of a general principle of good faith in common law, or the lack of legislation on the matter poses significant hurdles to developing the concept beyond its current conception. Indeed, franchise contracts do not have any special treatment from the courts other than occasionally being referred to as relational contracts, which may attract good faith duties by such classification. However, relational classification of contracts is problematic, instead, a RGSC one would be better suited if good faith duties were to be implied by law into franchise contracts. Regardless, the courts continue to resort to restrictive alternative doctrines such as that of 'non-derogation from grant', which cannot effectively curb various types of future opportunistic behaviour.

Franchising does not present a greater challenge than any other commercial contract in terms of the extent of legal solutions that may be devised for the contractual problems it may raise. Therefore, franchising does not provide for new legal responses to address unfairness in the performance of English franchising contracts. Rather, it represents an opportunity for reshaping contract law in light of the imports of modern contract theory, which focuses on the underlying cooperative nature of franchising, and more generally of all commercial contracts. Although the Australian example is imperfect, its enactment of the good faith standard into law for franchising is commendable. Although uncertainty is inherent to the concept, and the Australian legislator has declined to define it, it has liberated the judiciary from the debate on whether good faith should be implied into franchise contracts and on the judicial basis of its

[1290] ibid 25.
[1291] ibid 4, 30, such as one based on the idea of 'unfair trading.'

application. The flexibility of good faith in providing a balance to the performance of the contractual duties in franchising in Australia is tempered by regulatory (through ACCC guidance) and judicial work (through case law) to provide the certainty required by dispute adjudication. The lack of transparency and data in regards to disputes in the industry in England and Wales is a major impediment to identifying the extent of legislative intervention which may be required to address existing opportunistic conduct. Like Australia, England and Wales would benefit from carefully crafted legislative responses of good faith, in supplement to, and not as a substitute for, a comprehensive regulatory scheme.[1292] We shall now discuss the importance of legislative reform for good faith beyond franchising contracts.

[1292] Andrew Terry, Cary Di Lernia, Rozenn Perrigot, 'The Obligation of Good Faith and its Role in Franchise Regulation' in Hoy F, Perrigot R, Terry A (eds), *Handbook of Research on Franchising* (Edward Elgar Publishing 2017) 186.

CHAPTER 6: LEGAL REFORM OR SELF-REGULATION?

6.1. Introduction

The examination of the case law in commercial contracts has shown that the recognition of good faith as an overarching principle is dependent on the stance of the individual judges. If a judge in favour of deriving duties from a good faith principle in contracts, is presented with the opportunity to decide on the matter, they may do so in a landmark decision. However, this is highly unlikely to be in the form of an implication in law or a recognition of good faith as an interpretative principle of commercial contracts. Rather, the incremental nature of the system does not favour big leaps of faith, although, as seen with *Yam Seng*, it can produce case law that challenges the status quo.[1293] Regulating commercial actors' conduct can be done in various ways. [1294] A party may be influenced by more than the existence of the laws to refrain from opportunistic behaviour, such as deference to custom, or a self-preserving aim to protect its reputation. As such, the importance of social norms cannot be discounted in the decision-making process of commercial actors.[1295] However, the courts are not equipped, tasked or should be providing regulatory direction to policies that would fall within the Parliament's purview. The questions of *whose*, *how* and *to what extent* opportunistic behaviour should be curbed are ultimately a policy question which has only partially been dealt with by the Parliament.[1296] However, as evident by the examination of franchising contracts above, the Parliament has not always opted to legislate on all commercial contracts where there is an inherent imbalance of information or power in the relationship. This points to a 'co-regulation' framework for the regulation of commercial transactions, where the State sets out public policy limits but otherwise leaves the contracting parties to self-regulate within those limits.[1297] The issue with this view is that the framework of public policy has not been drawn particularly well in the context of commercial contracts, where parties who are systematically vulnerable to stronger parties' opportunistic behaviour, such as small businesses or franchisees, are left to fend for themselves within the limits of the available mechanisms.[1298]

[1293] *Yam Seng* (n 3).
[1294] Collins, *Regulating Contracts* (1999) (n 111) 7.
[1295] ibid.
[1296] Such as in the context of consumer or insurance laws where there is a stark inherent imbalance in the relationship.
[1297] Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 103.
[1298] Such as by arguing implied terms of good faith in fact, or by arguing unconscionability.

A statute providing for good faith in contractual performance would provide a cohesive protection against all opportunistic behaviour, regardless of the type of contract. The protection against certain types of unfair terms in business contracts (in UCTA 1977) or against anti-competitive behaviour that adversely impacts the market in which the parties operate through competition laws already evidences the need to protect commercial actors against certain types of behaviour. Further evidence is found in industry initiatives that seek to implement such protection by adopting a good faith standard as a way of maintaining flexibility for future opportunistic behaviour in contract performance. A statutory standard of good faith in commercial contracts would also allow the courts to solely focus on developing the doctrine, knowing that they did not overstep their lawmaking powers, which could potentially subject them to legitimacy criticisms.[1299]

This chapter begins by highlighting the importance of the lessons which can be drawn from the Australian statutory duty of good faith experience (chapter 6.2). Then industry and governmental initiatives in the UK context will be addressed to evidence the increase in importance of good faith duties in the market (chapter 6.3). The last section will emphasise the necessity of legislative reform to give good faith a statutory foothold by focusing on the limitations of UCTA 1977 and the new DMCCA 2024 (chapter 6.4).

6.2. Significance of the Australian Approach

The franchisors and the franchisees may not place the same demands on the law's treatment of franchising contracts. Where the interests of a franchisor may focus on protection from excessive claims for compensation by the franchisees, the franchisees' interest is better served by a contextual understanding of the contractual relationship, where the contract's remit is disputed further into the contractual relationship.[1300] As seen with the example of the Australian regulation of good faith in franchising, the streamlining of the obligation has come with the enactment of the obligation into law through a specific industry code. Although this thesis is not concerned with the regulation of franchising as a whole, but only with the obligation of good faith in that context, the juxtaposition of the Australian example with the English one raises interesting questions for the future direction of franchising regulations in

[1299] Alysia Blackham, 'Legitimacy and Empirical Evidence in the UK Courts' (2016) 25(3) Griffith Law Review 414, 414, posits that '[i]nstitutional legitimacy of legal institutions is fundamental for an effective and functioning legal system and for securing compliance with judicial decisions. Legitimacy is fundamental for ensuring the sustainability and stability of legal systems in a modern democracy.'
[1300] Taylor (n 1119) 476.

the UK. The direction taken by Australia in franchising is clear: more emphasis on educating the stakeholders or prospective stakeholders, gathering feedback and information from the users of the regulations to review them periodically to gauge their appropriateness, and improving on fair and effective alternative dispute resolution mechanisms to minimise disputes and reduce costs to parties. Overall, this approach is geared to help the sustainable development of the industry as a whole by precisely catering to its needs. Franchising being an industry encompassing a variety of business sectors, the drafting of the good faith provisions in the FCOC is purposefully kept succinct, and sets a minimal framework for dealing with the parties.

An important point to note on the statutory implementation of FCOC is the reduced opportunity for the courts to further develop good faith obligations in the context of franchising.[1301] Under the FCOC, the parties have several dispute resolution alternatives such as conciliation, multiple party mediation or conciliation, or arbitration, instead of or before taking legal action through the state courts. Mediation, if engaged by a party, is mandatory and has been successful in resolving disputes in 80% of cases.[1302] The dispute resolution process is indeed mandated by the FCOC.[1303] The process is handled mainly by the parties themselves, the ACCC only becoming involved in individual or small business disputes if it raises wider issues of public interest.[1304] Therefore, franchising disputes are likely to be resolved before they reach any state courts.[1305]

Where an industry-specific code is enacted, and a regulator is designated for its enforcement, the regulation of such industry is more likely to be in line with commercial expectations of the market players, as their feedback is actively sought out and implemented in future changes of the law. Industry codes, by nature, are limited to their relevant industry. In the case of franchising, the code is naturally limited to regulating businesses operating within a franchise system. Therefore, any application of a good faith duty emanating from an industry code would be limited to that specific industry. All contracts operating outside the industry

[1301] Sears (n 1244) 130, at the time when FCOC 2014 was in force, she had argued that the lack of a clear definition of good faith in the FCOC would ultimately lead to more litigation and thereby allow the doctrine to develop further.
[1302] Giles and Jones (n 1242) 599.
[1303] ACCC, 'Resolving Franchising Disputes' (ACCC) <https://www.accc.gov.au/business/industry-codes/franchising-code-of-conduct/when-things-go-wrong-with-a-franchise/resolving-franchising-disputes> accessed 3 April 2025.
[1304] Australian Department of the Treasury, 'Review of the Franchising Code of Conduct Consultation Paper' (n 1240) 26.
[1305] Giles and Jones (n 1242**)** 584, provide that arbitration is rarely used in the context of franchising in Australia due to the low incidence of disputes, the success of the FCOC mediation process and the rarity of punitive damages in case law.

would need to fall back on the common law or other relevant legislation to curb any opportunism. However, where there is no statutory good faith applicable in all business contexts, the case law has to shoulder the load in developing its application. Where the body of law develops further, there can be more support for the obligation to be enacted into legislation, as the application of a statutory good faith can draw on developing case law.[1306]

Indeed, the introduction of good faith into FCOC was not straightforward at its inception. Initially, the government refused the introduction of the duty suggesting that the common law doctrine was still evolving and therefore a statutory duty would create uncertainty.[1307] This was in response to a parliamentary committee recommending the introduction of an express duty of good faith as an overarching standard of conduct.[1308] The view of the committee was that

> the concept of good faith has not only received strong judicial support, but now has reached the point in Australia where its nature and scope is being defined with an increasing degree of precision. Consequently, there is a ready body of law on which a statutory duty of good faith could quite readily and usefully draw upon in seeking to promote ethical business conduct.[1309]

Despite the initial reluctance, in 2010, a clause was inserted into FCOC that '[n]othing in this code limits any obligation imposed by the common law, applicable in a State or Territory, on

[1306]Australian Senate Standing Committee on Economics, 'The Need, Scope and Content of a Definition of Unconscionable Conduct for the Purposes of Part IVA of the Trade Practices Act 1974,' (3 December 2008) <https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Completed_inquiries/2008-10/tpa_unconscionable_08/report/index> accessed 3 April 2025, ch 5, para 5.43, the Australian Parliamentary Committee held a similar view when it was questioning whether good faith could be defined and enacted into a statute in the context of reviewing amendments to the Trade Practices Act 1974.

[1307] Commonwealth Government Response to the Report of the Parliamentary Joint Committee on Corporations and Financial Services Opportunity Not Opportunism: Improving Conduct in Australian Franchising (2009) (Department of Innovation, Industry, Science and Research, 5 November 2009) < https://treasury.gov.au/publication/government-response-to-the-report-of-the-parliamentary-joint-committee-on-corporations-and-financial-services-opportunity-not-opportunism-improving-conduct-in-australian-franchising> accessed 3 April 2025, 13-14.

[1308] Parliamentary Joint Committee on Corporations and Financial Services, 'Opportunity Not Opportunism: Improving Conduct in Australian Franchising' (1 December 2008) <https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Completed_inquiries/2008-10/franchising/report/index> accessed 3 April 2025, recommendation 8.60.

[1309] ibid, para 8.27, citing the recommendations of Associate Professor Frank Zumbo.

the parties to a franchise agreement to act in good faith.'[1310] A subsequent review of the FCOC in 2013 led to the insertion of the express obligation of good faith.[1311]

Whilst enacting the obligation of good faith expressly, the legislator did not provide a definition. The same was true for defining the term 'unconscionable conduct.'[1312] Indeed, it was argued that 'any attempt to define the concept, even through examples, will lead to loss of flexibility in interpretation and loss of guidance on the norm provided by the legal precedent.'[1313] The Franchise Council of Australia also opposed a statutory definition of 'unconscionable conduct' and its examples, claiming that the FCOC, together with the existing provisions of the Trade Practices Act 1974, disallowing conduct that is 'in all the circumstances, unconscionable' at its section 51AC for businesses was a sufficient legal framework.[1314] CCA 2010 subsequently replaced the said section of the Trade Practices Act 1974 within the CCA 2010; however kept the original provision as a general norm with the list of factors to determine whether the conduct is in fact unconscionable.[1315] It is held by the courts to mean conduct 'that is not in good conscience by reference to the norms of society, irreconcilable with what is right and reasonable, and conduct that is commercially reprehensible in all the circumstances.'[1316] Ultimately, the assessment of whether conduct is unconscionable is decided on a case-by-case basis in light of the circumstances of each case, with the guidance provided in s 22 of CCA 2010. In sum, the Australian legislative process was initially, then partially, characterised by the same reluctance affecting the opponents of good faith, who view it as a threat to the certainty of the law. However, the fear that good faith would wreak havoc in contract law did not materialise due to the careful parliamentary consultations involving various stakeholders, which served as the basis of the legislation, and which continues to be the subject of regular review.

[1310] Trade Practices (Industry Codes—Franchising) Regulations 1998 (Cth) s 23A.
[1311] Alan Wein, 'Review of the Franchising Code of Conduct' (*Treasury*, 30 April 2013) <https://treasury.gov.au/sites/default/files/2019-03/ReviewoftheFranchisingCodeofConduct.pdf> accessed 3 April 2025, 63.
[1312] Australian Senate Standing Committee on Economics (n 1305), Ch 5 para 5.17-5.18 (fn 14), the Committee did not recommend introducing a definition into Part IVA of the Trade Practices Act 1974 (Cth) and it disapproved of replacing the word 'unconscionable' with 'unfair' arguing that this would lower the threshold for triggering the application of the duty under the Act and would require enacting wider legislation 'supporting national general prohibition on unfair conduct.' The ultimate concern was that this would create transactional and judicial uncertainty.
[1313] ibid, chp 4, para 4.11, this reasoning was put forward by the Law Council of Australia.
[1314] ibid, chp 4, para 4.18.
[1315] ibid, chp 5, para 5.55.
[1316] Giles and Jones (n 1242) 588.

6.3. Tackling the Statutory Good Faith Gap in English Commercial Contracts

Besides the protections accorded to consumers in English law, recent initiatives have allowed for the establishment of minimum levels of commercial good faith in the commercial context. Despite their restrictive scope of application, such initiatives hint at a need for wider-scale regulation for commercial contracts. The franchising context examined above was a prime example of voluntary regulation (in the English context), which could easily be turned into a mandatory code with the right amount of governmental and industry initiatives (as in the Australian context). The initiatives examined below do not fundamentally disrupt the law of contract as it is currently laid out, but raise the question as to whether a wider protection needs to be accorded to businesses of all sizes applicable beyond fragmented and industry-specific contexts.

6.3.1. Industry Codes

The common law's failure to clearly enunciate a good faith duty in contract performance means that parties must think of other ways around the problem. The emergence of good faith in certain industry codes is a clear indication of the need for market players to factor such a duty into the contract. For instance, on 31 January 2024, the Intellectual Property Office published a voluntary code of conduct setting standards of good practice about music streaming.[1317] It was signed by several trade associations, membership organisations and collecting societies, and is currently going through an implementation period, and it will undergo a formal review to evaluate the code's impact.[1318] It aims to increase transparency and cooperation within the context of licensing of intellectual property rights and, most importantly, the processing and reporting of usage data and associated revenues and royalties. As it is a voluntary code, it expressly indicates that a failure to abide by its provisions shall not constitute a breach of any other legislation or any relevant contracts.[1319] It further provides that '[a]ll parties commit to acting reasonably, proportionately and in good faith regarding the principles articulated in this [c]ode, taking into account what is reasonably practicable, commercial and proportionate in the relevant circumstances.'[1320] Regrettably, the code does not provide for effective dispute resolution or grant enforcement or complaint handling powers

[1317] Intellectual Property Office, 'UK Voluntary Code of Good Practice on Transparency in Music Streaming' (*UK Government*, 31 January 2024) <https://www.gov.uk/guidance/uk-voluntary-code-of-good-practice-on-transparency-in-music-streaming#implementation-period> accessed 3 April 2025, 31.
[1318] ibid.
[1319] ibid.
[1320] ibid.

to any particular bodies. In the event of a breach, the disgruntled party is to contact the breaching party 'to discuss their concerns and seek to resolve the matter without further escalation.' If there is no resolution, the case can be escalated to the relevant trade body which may resolve the matter.[1321]

Another example of a code of conduct is the Groceries Supply Code of Practice ('GSCP') which was published on 4 August 2009 following a market investigation by the Competition and Markets Authority (then the Competition Commission).[1322] Despite its name, it is in fact a compulsory piece of legislation which applies to the relevant retailers in their dealings with their suppliers. The aim was to curb supply chain practices adopted by retailers that transferred excessive risks and unexpected costs to their grocery suppliers, thereby avoiding adverse effects on competition and customers.[1323] It was created to ensure that the UK's largest groceries retailers, with an annual turnover of more than £1 billion, treat their direct suppliers lawfully and fairly, regardless of whether the latter are based inside or outside the UK.[1324] In 2013, the Groceries Code Adjudicator ('GCA') was established to overview compliance with the GSCP.[1325] It can investigate suspected breaches of the GSCP and bindingly arbitrate disputes between the parties.[1326] It also has the authority to impose financial penalties up to a maximum of 1% of a retailer's annual UK turnover.[1327] Moreover, each retailer is required to appoint a Code Compliance Officer independent from its buying team to act as a point of contact for suppliers in regards to enquiries concerning the GSCP.[1328] In section 2, the GSCP provides for a principle of fair dealing, which is understood as

[1321] ibid.
[1322] Department of Business and Trade and Department for Business, Energy, and Industrial Strategy, 'Guidance Groceries Supply Code of Practice' (*UK Government*, 4 August 2009) <https://www.gov.uk/government/publications/groceries-supply-code-of-practice/groceries-supply-code-of-practice> accessed 3 April 2025.
[1323] Competition and Markets Authority, 'GSCOP Explanatory Note' (*CMA*, 4 August 2009) <https://www.gov.uk/government/publications/groceries-supply-chain-practices-market-investigation-order> accessed 3 April 2025, 1.
[1324] GCA, 'Code Confident Pack' (*GCA*, February 2025) < https://www.gov.uk/government/publications/code-confident-pack> accessed 3 April 2025, 3.
[1325] ibid.
[1326] Groceries Code Adjudicator Act 2013, s 2. To date, only two investigations were carried out: (i) Groceries Code Adjudicator, 'GCA Investigation into Tesco plc' (*GCA*, 26 January 2016) <https://www.gov.uk/government/publications/gca-investigation-into-tesco-plc> accessed 3 April 2025, (ii) 'GCA Investigation Report into Co-operative Group Limited' (*GCA*, 25 March 2019) <https://www.gov.uk/government/publications/gca-investigation-report-into-co-operative-group-limited> accessed 3 April 2025.
[1327] Groceries Code Adjudicator Act 2013, s 6. This can only be challenged through High Court proceedings or a judicial review process under s 9(3) of the Groceries Code Adjudicator Act 2013.
[1328] GCA, 'Code Confident Pack' (n 1323) 9.

> requiring the [r]etailer to conduct its trading relationships with [s]uppliers in good faith, without distinction between formal or informal arrangements, without duress and in recognition of the [s]uppliers' need for certainty as regards the risks and costs of trading, particularly in relation to production, delivery and payment issues.[1329]

The GSCP does not cover issues relevant to pricing, food safety and labelling, and focuses on the expressly listed practices therein, such as prompt payment, not varying supply agreements without notice, paying compensation for forecasting errors or not charging for shrinkage or wastage.[1330] The GCA can, from time to time, publish clarification case studies to inform the market participants on types of conduct which would be considered to be a breach of the GSCO.[1331] In a 2015 GCA annual survey, direct suppliers have responded that delay in payments, variation of supply agreements and terms of supply, obligation to contribute to marketing costs, and no compensation for forecasting errors were voted as amongst the top issues with retailers operating under the GSCP.[1332] Explicit feedback was sought in later annual surveys on the good faith and fair conduct of the retailers. In 2020, although there were variations depending on the specific retailer, the direct suppliers' responses ranged between 44% (Iceland) and 80% (Aldi), with the majority considering that trading relationships with retailers were conducted in good faith.[1333] In the 2022 survey, failure to act in good faith and without duress was included in the list of issues experienced by the direct suppliers.[1334] The responses showed these came third amongst all issues experienced, constituting 9% of the total.[1335] However, 18% of issues were marked as uncertain, therefore potentially relevant for the good faith category. Moreover, some of the other issues could also be categorised into

[1329] Department of Business and Trade, Department for Business, Energy, and Industrial Strategy, 'Guidance Groceries Supply Code of Practice' (n 1321).
[1330] GCA, 'Code Confident Pack' (n 1323) 5.
[1331] GCA, 'Guidance Code Provisions and Related GCA Action' (*GCA*, 24 June 2020) <https://www.gov.uk/government/publications/code-provisions-and-related-gca-action/code-provisions-and-related-gca-action#paragraph-3---variation-of-supply-agreements> accessed 3 April 2025.
[1332] YouGov, 'GCA Annual Survey Results' (*YouGov*, 2015) <https://assets.publishing.service.gov.uk/media/5a8003e2e5274a2e87db7576/2015_Conference_-_YouGov_slides.pdf> accessed 3 April 2025, 18.
[1333] YouGov, 'GCA Annual Survey' (*YouGov*, 2020) <https://assets.publishing.service.gov.uk/media/5ed8fc6486650c76a4ca43f9/GCA_YouGov_2020_Presentation.pdf> accessed 3 April 2025, 19.
[1334] 'GCA Annual Survey' (*YouGov*, 2022) <https://assets.publishing.service.gov.uk/media/62a1a8ede90e0703a2fed814/GCA_annual_survey_results_2022_for_publication.pdf> accessed 3 April 2025, 3.
[1335] The percentage remained the same in 2023, see 'GCA Annual Survey 2023' (*YouGov*, 2023) <https://assets.publishing.service.gov.uk/media/648aad7cb32b9e000ca967a8/GCA_annual_survey_results_2023.pdf> accessed 3 April 2025, 3. It went down to 8% in 2024, see GCA, 'GCA Annual Survey 2024' (*YouGov*, 2024) accessed 3 April 2025, 3.

failure to observe good faith, such as delay in payments, or not applying due care when ordering promotions, or payment as a condition of being a supplier.[1336] Similarly, most of the issues phrased in the supplier language indicate that breaches of the good faith duty might be equally relevant for cases where the retailer refuses to consider a cost price increase, or the supplier incurs significant costs because of inaccurate forecasting by retailers.[1337]

Although the polls hint at a general sense about the direct suppliers' experience with the retailers being in good faith, the overlap of different issues in the results, and the potential failure of direct suppliers in identifying good faith breaches likely distort the general picture of good faith dealings in this particular industry. The increase in the number of suppliers receiving training on the GSCP and their reporting of alleged breaches by the retailers to the GCA over the past decade most likely had an impact on curbing the opportunistic behaviour of the retailers. The positive impact of the GSCP and the GCA on improving retailer behaviour and addressing the imbalance of power, thereby making the grocery market fairer to operate in, was reported in the statutory review of the GCA.[1338] Similarly, the retailers accepted the positive impact as it 'levelled the playing field' across retailers.[1339] Indeed, the direct suppliers who had experienced an issue have decreased from 79% in 2014 to 36% in 2023, and to 33% in 2024.[1340] GCA's work as an independent regulator also contributed to holding retailers to account, in particular for SME businesses.[1341] The retailers' view was that the oversight of the retailers themselves and the sanctions the GCA can issue lead to more consistent behaviours.[1342] In fact, they considered that the 'GCA's regulatory approach had helped them embed a strong culture of collaboration between them and their suppliers.'[1343] The low number of arbitrations may be taken as an indication of the effectiveness of the GCA in resolving disputes before they are brought to formal arbitration.[1344] Consequently, a clear point emerges from the industry

[1336] ibid.
[1337] ibid 4. Both categories stand at 16% and 18% respectively in 2024, see GCA, 'GCA Annual Survey 2024' (n 1334) 4.
[1338] Department for Business and Trade, 'Statutory Review of the Groceries Code Adjudicator: 2019-2022' (*UK Government*, July 2023) <https://assets.publishing.service.gov.uk/media/64b69f6571749c001389edc5/statutory-review-of-the-groceries-code-adjudicator-2019-2022.pdf> accessed 3 April 2025, para 29.
[1339] ibid, para 31.
[1340] YouGov, 'GCA Annual Survey 2023' (n 1350) 3, YouGov, 'GCA Annual Survey 2024' (n 1334) 3.
[1341] Department for Business and Trade, 'Statutory Review of the Groceries Code Adjudicator: 2019-2022' (n 1353), para 24.
[1342] ibid, para 26.
[1343] Department for Business, Energy and Industrial Strategy, 'Statutory Review of the Groceries Code Adjudicator: 2016-2019' (UK Government, July 2020) <https://assets.publishing.service.gov.uk/media/5f0f1aa13a6f40037ed484db/gca-report.pdf> accessed 3 April 2025, para 38.
[1344] Department for Business and Trade, 'Statutory Review of the Groceries Code Adjudicator: 2019-2022' (n 1353), paras 18, 50.

feedback on the application of the GSCP and the GCA's role, which is that curbing opportunistic behaviour is in the interest of all parties and has overall positive consequences for the market.

Another important point is that all parties considered it was necessary to have a regulatory body to enforce the GSCP without which they believed the retailers would swiftly return to their previous poor behaviour towards suppliers.[1345] This shows that in an industry where inequality of bargaining is rife, there is a need for regulatory intervention to prevent and sanction the opportunistic behaviour. Some of the feedback from the market participants also highlighted the need for the remit of the GCA to be extended or another regulator to be introduced to cover business-to-business trading relationships of retailers with lower turnover.[1346] However, the Government's response was that extending the remit was not necessary, rather targeted measures to address sector-specific issues were more appropriate.[1347] Therefore, it did not merge the GCA with the Competition and Markets Authority, 'in recognition of the importance of the Adjudicator in ensuring fairness in the UK food supply chain.'[1348]

The analysis of the GSCP reveals important lessons for parties affected by the shortcomings of the GCA. In sum, smaller retailers or the parties affected by topics not covered by the GSCP's scope continue to remain unprotected.[1349] Moreover, the GSCP does not regulate the business between different suppliers, but only the deals between the retailers and the suppliers, and within that context, it is only limited to regulating the conduct of the retailers rather than the suppliers. Therefore, any misbehaviour by the supplier against the retailer will not trigger the enforcement powers of the GCA.

[1345] ibid, paras 65-66.
[1346] Department for Business and Trade, 'Statutory Review of the Groceries Code Adjudicator: 2016-2019' (n 1358**)** paras 58-59.
[1347] ibid, para 80, for example by dealing with supply chain problems through the enactment of the Agriculture Act 2020.
[1348] Department for Business and Trade, 'Statutory Review of the Groceries Code Adjudicator 2019-2022' (n 1353) 3.
[1349] Also, in 2023, 17% of direct suppliers did not understand GCA's role, and 15% did not understand it well, which indicates that there is room for improvement in the application of the GSCP and GCA's regulatory duties, see YouGov, 'GCA Annual Survey 2023' (n 1350) 2. There is slow progress in this area as the most recent poll indicates that the numbers are down to 16% and 13% respectively, see YouGov, 'GCA Annual Survey 2024' (n 1334) 2.

6.3.2. Standard Form Contracts

Over the years, the construction industry has had to take the matter into its hands. In the most commonly used forms of standard form, contracts require that parties act in a spirit of mutual trust and cooperation. The most popular types of standard form construction contracts used in the industry are the Joint Contracts Tribunal ('JCT') contracts, New Engineering Contract ('NEC') contracts or Royal Institute of British Architects ('RIBA') building contracts.[1350] For example, clause 10.1 in NEC3 (now clause 10.2 in NEC4) form of contract requires that the parties act in a 'spirit of mutual trust and co-operation'. The NEC form was created by the Institution of Civil Engineers as an alternative to the traditional form of contracting which focuses only on the legal rights and obligations, and instead to encourage good project management.[1351] In essence, the ideology of the NEC form is to 'promote collaboration.'[1352] The 'mutual trust and co-operation' entails more than only honest and reasonable conduct, but a positive obligation to carry the contract out collaboratively.[1353]

In *Costain Ltd v Tarmac Holdings Ltd*, the court had to decide whether the defendants were in breach of the obligation of mutual trust and co-operation under clause 10.1 of NEC3 by failing to sufficiently communicate with the claimant about the interpretation of the dispute resolution procedures in the contract.[1354] The court accepted that such an obligation goes beyond a negative obligation and extends to a positive obligation to correct a false assumption, but failed to approve a further extension.[1355] As such, the court's approach is considered to be a hardening against good faith, which prefers a restrictive self-interested understanding of construction contracts rather than a flexible and collaborative one.[1356] More recently, in *Van Oord v Dragados*, the court stated that the aforementioned clause 'reflects and reinforces the general principle of good faith in contract.'[1357] Importantly, it aligns with the proposition of

[1350] RIBA, 'RIBA Construction Contracts and Law Report 2022' (*RIBA*, 2022) <https://riba-prd-assets.azureedge.net/-/media/Files/Contracts/RIBA-Construction-Contracts-and-Law-Report-2022.pdf?rev=131db86dc10b4ceca07551c939ac6d0f&hash=3E58876E8418A4B0FFC620CF2DD8961A> accessed 3 April 2025, 17.
[1351] Lukas Lee, *International Construction Contract Law* (2nd edn, John Wiley & Sons Incorporated 2018) 581.
[1352] ibid 586.
[1353] Humphrey Lloyd, 'Some Thoughts on NEC3', (NEC Contract, January 2009) <https://www.neccontract.com/getmedia/1dea6551-0589-4574-b5f3-500c1a1d34e4/NEC-news-lloyd-special-web-version-2.pdf> accessed 3 April 2025, 4.
[1354] [2017] EWHC 319 (TCC).
[1355] ibid [124].
[1356] David S Christie, ''Splendid, But What Does It Actually Mean?': Good Faith and Relational Contracts in the UK Construction Industry' (2019) 1 Journal of Commonwealth Law 403 <https://www.journalofcommonwealthlaw.org/article/10813-splendid-but-what-does-it-actually-mean-good-faith-and-relational-contracts-in-the-uk-construction-industry> accessed 3 April 2025, 485.
[1357] [2021] CSIH 50, 2021 SLT 1317, [1320].

English law, whether as an implied term or as a rule of contractual interpretation, that a party cannot gain an advantage from its own breach. Although it is a Scottish court decision and the court has not discussed the content of the obligation in detail, it may have the effect of influencing the recognition of a duty of good faith in construction contracts in English courts.[1358]

Similarly, at its schedule 8, the JCT 2016 form provided for an optional clause for 'collaborative working,' where the parties will 'work with each other and with other project team members in a co-operative and collaborative manner, in good faith and a spirit of trust and respect.'[1359] However, the newer JCT 2024 edition promoted the obligation to collaborate in good faith to a core mandatory provision.[1360] Evidently, the growing trend in construction contracts is to 'move away from formal legal 'black letter' contracts to contracts fulfilling a different role which includes seeing contract as a management tool and a stimulus for collaboration.'[1361] Although it was not expressly mentioned, good faith underpinned the recommendations made by the Latham Report.[1362] Indeed, a cultural shift towards collaborative work was needed to leave behind the adversarial understanding of the relationships. Although the Latham Report influenced legislation, it did not lead to a good faith standard for contractual performance in construction contracts.[1363] Despite embracing a fast-track form of dispute resolution, the culture remains very much anchored in disputes.[1364] The popular standard form contracts in reality align with the recommendations of the Latham Report. However, there is a lack of a general duty of good faith operating within the construction industry. Therefore, when unforeseeable events, such as Covid-19, happen and have a negative impact on the economy,

[1358] Christie, Saintier, Viven-Wilksch, 'Industry-Led Standards, Relational Contracts and Good Faith: Are the UK and Australia Setting the Pace in (Construction) Contract Law?' (n 786**)** 291 (fn 14).
[1359] Joint Contracts Tribunal, 'JCT Contracts Complete 2016 Edition' (JCT, 2016) https://www.jctltd.co.uk/category/jct-contracts-complete-2016-edition accessed 3 April 2025. A newer version of these forms has come out in 2024, Joint Contracts Tribunal, 'Design and Build Contract (DB 2024)' (JCT, 2024) <https://www.jctltd.co.uk/product/design-and-build-contract-2024> accessed 3 April 2025.
[1360] Article 3, JCT 2024.
[1361] Jim Mason, 'Contracting in Good Faith – Giving the Parties What They Want' (2007) 23(6) Construction Law Journal 436, 437.
[1362] Michael Latham, 'Constructing the Team: Joint Review of Procurement and Contractual Arrangements in the United Kingdom Construction Industry' (July 1994) <https://constructingexcellence.org.uk/wp-content/uploads/2014/10/Constructing-the-team-The-Latham-Report.pdf> accessed 3 April 2025. The report was commissioned by the UK Government to investigate the way forward in addressing the systemic problems affecting the UK construction industry, such as an adversarial culture leading to frequent disputes, outdated contractual practices or low efficiency and productivity.
[1363] Housing Grants, Construction and Regeneration Act 1996 notably implemented the report's recommendations, including fair payment practices and the statutory right to adjudication. Also see, Mason (n 1360) 443.
[1364] Shona Frame, 'A Catalyst for Change? International Bar Association' (*IBA*, September 2020) <https://www.ibanet.org/article/f731fbd8-8529-4a6d-92a4-fa1803be52dd> accessed 3 April 2025.

it is not surprising to see Government publications on responsible contractual behaviour in the performance and enforcement of contracts.[1365] With an expressly recognised good faith duty in the newer JCT 2024 form, the importance of collaborative working in the industry has now been expressly recognised. The appearance of new trends such as alliancing, which is based on collaborative models based on good faith, features in the new NEC4 contracts. Although this type of contracting is likely to require 'significant investments in effort and funds to operate smoothly,' and 'the apportionment of risk and profit sharing means that the parties' interests are aligned through different processes (...).'[1366] Similarly, Project 13, an industry-led initiative for alternatives to traditional contracting models, is another indication that the industry is seeking new ways of transacting beyond the traditional contractual paradigm of party-centric models.[1367] Indeed, it is a new business model based on an enterprise to 'boost certainty and productivity in delivery, improve whole life outcomes in operation and support a more sustainable, innovative, highly skilled industry.'[1368] In sum, the restrictive interpretation of good faith currently embraced by the English courts in construction contracts runs against such developing trends and hinders the centring of the collaborative framework for understanding construction contracts.[1369] However, this is a developing area of law and the new good faith obligation expressly recognised in the JCT 2024 form is likely to be increasingly relied on by the parties in dispute and allow the courts to expand its scope of application.[1370]

6.3.3. Governmental Initiatives

Under the Enterprise Act 2016, the office of the Small Business Commissioner (SBC) was set up by the government. It aims to 'empower small businesses to resolve payment

[1365] See for instance, UK Government 'Guidance' (n 1073); Construction Leadership Council, 'COVID-19 Contractual Best Practice Guidance' Construction Leadership Council' (*CLC*, 7 May 2020) <https://www.constructionleadershipcouncil.co.uk/wp-content/uploads/2020/06/Construction-Leadership-Council-Covid-19-Contractual-Best-Practice-Guidance-7-May-2020.pdf> accessed 3 April 2025, which encourages collaborative approach towards successful project delivery; Scottish Government, 'Coronavirus (COVID-19): Impact on Construction Contracts: CPN 1/2020 Scottish Procurement and Property Directorate' (Scottish Government, 9 April 2020) <www.gov.scot/publications/coronavirus-covid-19-impact-on-construction-contracts-cpn-1-2020> accessed 3 April 2025, which suggests honest, open and constructive engagement, and recommends that the situation is not used as an opportunity for one party to gain from the loss of another party.

[1366] Christie, ''Splendid, But What Does It Actually Mean?': Good Faith and Relational Contracts in the UK Construction Industry' (n 1355) 412.

[1367] Project 13, 'Welcome to the Project 13 Network' <https://www.project13.info/> accessed 3 April 2025.

[1368] ibid.

[1369] Christie, ''Splendid, But What Does It Actually Mean?': Good Faith and Relational Contracts in the UK Construction' (n 1355) 442.

[1370] Shy Jackson, 'JCT 2024 Contracts – Good Faith in Practice' (BCLP Insights, 14 January 2025), <https://www.bclplaw.com/en-US/events-insights-news/jct-2024-contracts-good-faith-in-practice.html#:~:text=Article%203%20requires%20the%20parties,behaviour%20which%20is%20not%20collaborative.> accessed 3 April 2025.

disputes with larger businesses and avoid future issues by encouraging a culture change in payment practices and how businesses deal with each other.'[1371] Indeed, small businesses account for two-thirds of the UK's private sector employment and more than half of business turnover, and £23.4 billion worth of late invoices were owed in 2021.[1372] To tackle the negative impact on small businesses of such practice, the SBC introduced the Prompt Payment Code ('PPC') in 2021, which obliges signatory companies to pay small businesses within 30 days.[1373] Where the signatory businesses do not comply with the PPC, the SBC can strike it off for poor practice and publicise it on its website. However, the SBC does not have any enforcement powers in regards to the PPC, nor does the remit of its work extend beyond small businesses. Therefore, a consultation is underway regarding the strengthening of the SBC's ability to provide small businesses with mechanisms for redress in respect of late payments.[1374] The consultation specifically requests information on whether (i) the SBC should have any enforcement powers in regards to non-compliance with its information requests, (ii) its powers should extend to complaints between small businesses, (iii) sanctions should be imposed in certain circumstances, (iv) SBC should have the power to carry out reviews on relevant legislation, policies and practices on small businesses and extend to issues beyond payment matters.[1375]

The statutory review of the SBC was conducted in 2023, and the outcome was published in March 2024.[1376] The feedback from the small businesses indicates that they are largely unaware of the existence of the SBC or its particular role.[1377] Almost half of the feedback indicates that the SBC has had limited or no impact in general on business relationships,

[1371] Department for Business, Energy & Industrial Strategy, 'Small Business Commissioner Framework Document' (*UK Government*, December 2018) <https://assets.publishing.service.gov.uk/media/5c1927e2ed915d0c6bd78ff4/sbc-framework-document.pdf> accessed 3 April 2025.
[1372] Department for Business, Energy & Industrial Strategy, Small Business Commissioner, Kwasi Kwarteng, Paul Scully, 'Press Release: Government Tackles Late Payments to Small Firms to Protect Jobs' (*UK Government*, 19 January 2021) <https://www.gov.uk/government/news/government-tackles-late-payments-to-small-firms-to-protect-jobs> accessed 3 April 2025.
[1373] ibid.
[1374] Department for Business, Energy & Industrial Strategy and Department for Business, Energy & Industrial Strategy, 'Increasing the Scope and Powers of the Small Business Commissioner' (*UK Government*, 24 December 2020) <https://assets.publishing.service.gov.uk/media/5f74a4fe8fa8f518898b46cc/consultation-increasing-scope-of-small-business-commissioner.pdf> accessed 3 April 2025. The outcome of the consultation has not yet been published.
[1375] ibid 9.
[1376] Department for Business & Trade, 'Statutory Review of the Small Business Commissioner Response to Views and Evidence', (*UK Government*, 8 March 2024) <https://www.gov.uk/government/publications/publication-of-the-prompt-payment-and-cash-flow-review/statutory-review-of-the-small-business-commissioner-response-to-views-and-evidence> accessed 3 April 2025. In total, there were 99 responses, most responding on behalf of small businesses, and some responding for large businesses.
[1377] ibid, question 1.

possibly due to the lack of awareness of the SBC or limited powers available to the SBC.[1378] In particular, most responses considered SBC's complaint scheme or its investigations following a complaint by a small business to be ineffective.[1379] Importantly, several responses highlighted the need to improve the policy landscape by making it clearer and needing a clear and joined-up statutory framework for payment times backed up with fines.[1380] Clearly, the expansion of the SBC's powers of investigation and increasing awareness and clarity of its role are required for better tackling the late payment issues faced by small businesses.[1381] The SBC's own view is that it is limited in its powers to resolve complaints effectively, and is reluctant to publicise non-compliant businesses for fear of losing constructive working relationships.[1382] Where small firms had signed up to contracts with suppliers which might have had unfavourable payment terms for them, the SBC lacks the power to resolve such situations.[1383] The future steps in remedying the issues raised by the statutory review necessitate changes through primary legislation, which the Government intends to introduce at a later date.[1384] Based on the feedback, the Government's view is that currently there is no need to introduce punitive powers, given the businesses' concern for maintaining relationships with the large businesses they supply. However the public consultation which is currently underway clearly understands the link between efficiency and enforcement powers, and even references relevant comparatives such as the GCA or the Financial Services Ombudsman in the UK and the Australian Small Business and Family Enterprise Ombudsman in Australia, all of which have enforcement powers far beyond those of the SBC.[1385] The protection of small businesses using the SBC route is currently restricted by the Government's decisions implementing the feedback from the industry, and only if it chooses to do so.

6.4. Statutory Reform

6.4.1. Why is Statutory Reform Necessary?

Attempts at ensuring good faith in performance of contracts in English law discussed above demonstrate a fragmentary approach. An organising principle of good faith could no

[1378] ibid, questions 4 and 6.
[1379] ibid, question 8.
[1380] ibid, question 9.
[1381] ibid, question 11.
[1382] ibid, Views of the Small Business Commissioner Team.
[1383] ibid.
[1384] ibid, Summary of Findings. This also includes changing the name of the SBC to remove any confusion as to the remit of its powers.
[1385] Department for Business, Energy & Industrial Strategy and Department for Business, Energy & Industrial Strategy, 'Increasing the Scope and Powers of the Small Business Commissioner' (n 1373) 11-13.

doubt serve to bridge the gap between the cracks. Any future proposals for reforming contract law without mention of good faith would be incomplete.[1386] As demonstrated by a review of important case law on good faith herein, English courts do not recognise an overarching principle of good faith in contract performance, nor do they interpret contracts with an understanding that good faith is of the essence of the contract.[1387] The courts' reluctance in defining good faith in contracts may be attributed to the enormity of the task, which the parliament can better equip itself to undertake.[1388] It may also be due to judges not being elected officials, thereby not being 'best placed to implement broad ideas that could have such substantial effect on the common law.'[1389] As correctly observed by McKendrick,

> judges (...) are generally much too concerned with the resolution of individual cases to be concerned with the formulation of new general principles. And, once a legal system concludes, for one reason or another, that there is no general principle or doctrine of good faith, it is not easy for it then to change course and recognise the existence of such a general principle.

A legislation of general application expressly recognising good faith in contracts would certainly not be a gradual implementation cherished by the case law tradition of the courts however it may be what is necessary to provide certainty and predictability in resolving future contract performance disputes.[1390] Indeed,

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[1386] Legislation is a type of regulation, which is understood as 'any system of rules intended to govern the behaviour of its subjects,' see Collins, *Regulating Contracts* (1999) (n 111) 7. For the relationship between law and regulation, see Brownsword, 'Regulating Transactions: Good Faith and Fair Dealing' (n 50) 91.

[1387] Capper (n 559) 504 also recognised in the context of merging the doctrines of unconscionability and undue influence into one doctrine, or in adopting an overarching doctrine of unconscionability in terms of procedural unfairness, that 'the nature of the overhaul needed to accomplish this judicially would probably require an extremely fortuitous concurrence of cases and judges. Legislation might therefore be a quicker and more satisfactory way of proceeding.'

[1388] Janet O'Sullivan, *O'Sullivan and Hilliard's The Law of Contract* (10th edn, Oxford University Press 2022) 195 in the context of implying good faith into relational contracts, argues that 'such a major, transformative development to commercial transactions might have been better left to Parliament, with the implications considered by the Law Commission.' For an opposite view, see Chen-Wishart and Dixon, 'Good Faith in English Contract Law: A Humble '3 by 4' Approach' (n 205) 190 who argue that 'details of contract law will not command the same priority on Parliamentary time as, say, terrorism, Brexit, or fiscal policy' and favour an incremental development of the law by the courts.

[1389] Davies, *JC Smith's the Law of Contract* (n 56) 299.

[1390] Collins, *Regulating Contracts* (1999) (n 111) 110, 113, argues that unless there are public policy considerations requiring the imposition of standards of good faith in commercial contracts, that such a standard should not be imposed on unwilling parties. This is because he sees the role of the State to be a facilitatory of the range of options available to contractors. Contrary to his view, it is argued that legislation for commercial parties should not be dismissed hastily because, enacting legislation is a matter of policy, involving cost considerations, which can only be fully appreciated after a proper parliamentary consultation is put into place.

> statutes, when they are first introduced, inevitably create a degree of uncertainty, particularly where they contain discretionary rules, but that uncertainty can be reduced by the courts over time as they interpret the statute and provide guidelines for its interpretation. Just as the courts develop principles in the development of the common law, so can they develop principles to guide parties as to how a discretion is likely to be exercised in the context of the interpretation of a statute.[1391]

The introduction of voluntary codes of conduct, the use of various standard form contracts or the creation of governmental offices such as that of Small Business Commissioner are steps in the right direction, however, they offer a fragmented picture of dissonant responses to contractual performance. A bottom-up approach to regulatory gap-filling provides an opportunity for developing an understanding and interpretation of good faith in contracts. Therefore, any avoidance of courts to address and recognise an explicit good faith duty will come under pressure as such initiatives are increasingly adopted.[1392] The adoption of voluntary and mandatory codes of conduct in the UK is commendable, as it paves the way for other industries and creates certainty within their sphere of application.[1393] Although the initial implementation stage may generate costs and uncertainties in the short term, the benefits could certainly lead to less litigation in courts and more effective and collaborative dispute resolution mechanisms that preserve business deals and relationships rather than antagonise the parties and destroy their relationship.[1394]

Despite dealing with long-term contracts that require collaboration of the parties, particular industry codes cannot be expected to regulate all aspects of business life. For instance, the BFA's Franchise Code of Ethical Conduct in the UK aims to regulate the conduct of parties to franchising contracts, or the GSCP seeks to curb anti-competitive practices of grocery chains, which ultimately have detrimental effects on consumers. The success of a code ultimately depends on whether (i) it is 'the only authoritative statement of law' on the topic and (i) its approach is balanced enough between catering to specific needs, all the while being

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[1391] McKendrick, 'Doctrine and Discretion in the Law of Contract Revisited' (n 238) 4.

[1392] Muris (n 109) 524 argues that 'threat of opportunism increases transaction costs because potential opportunists and victims expend resources perpetrating and protecting against opportunism.' Therefore, the law should seek to eliminate or reduce these expenditures to free up the resources for productive use, the challenge being to 'help reduce these costs without imposing still higher costs in the process.'

[1393] See chps 5.3.3 and 6.3.1.

[1394] Schaper (n 1247) 92-93, indeed the review of the Australian Franchising Code of Conduct indicates that effective dispute resolution 'allows parties to work constructively to resolve their differences quickly and at minimal cost, allowing the relationship to recover.' Some respondents, including the Law Council, suggested that arbitration in the context of franchising should be compulsory, in order to 'encourage recalcitrant franchisors to engage more constructively at mediation or conciliation.'

general enough to be long-lasting.[1395] Where the voluntary code has not been enacted into law, it already fails the first criterion of success. Moreover, bypassing parliamentary processes raises legitimacy issues, as it limits public scrutiny and concentrates regulatory power in the hands of the few industry players whose vested interests make self-regulation problematic.[1396] In particular where there is an innate imbalance of information and bargaining power in a relationship, such as that of a franchise, where a large proportion of the parties are made up of small businesses, the need to protect against opportunism of the stronger party will be higher.[1397]

The need for flexibility in the face of ever-changing technology and market demands points to a need for a framework for contractual performance which is not fixed in a rule but rather is flexible and expressed in a standard. This need is also closely related to the gradual 'shrinking canvas' upon which the traditional common law rules of contract have operated.[1398] Indeed, although the role of commercial courts in adjudicating disputes continues to remain important, it has been challenged by an increase in private ordering of contracts through specialist tribunals dealing with specific areas of law, such as competition, employment, property, and the use of alternative dispute resolution mechanisms such as arbitration.[1399] Private ordering is defined as 'a process of rule-making and enforcement not derived directly from state authority to create law, nor dependent on the state's monopoly on the use of force.'[1400] The parties also may resort to alternative contractual rules, opting out of the defaults provided by the common law and, wherever possible, the legislation, by incorporating provisions, for instance, generally adopted in their specific industry.[1401] Moreover, regulatory bodies also provide dispute resolution services, which, if resolved, remove the need for court litigation.[1402]

The attempts of the judiciary to pigeonhole good faith as a rule result in uncertain applications of the concept to certain categories of contracts. To the contrary, good faith, as argued herein, is envisaged as a standard of general application to all types of contracts. The emphasis on good faith in various industries clearly indicates that the law and the practice are

[1395] Viven-Wilksch, 'Good Faith in Contracts: Australia at the Crossroads' (n 1212) 307.
[1396] ibid 308.
[1397] As will be discussed in chp 6.4.3, the legislative regime to protect small businesses against unfair conduct has not yet materialised.
[1398] Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 87.
[1399] ibid.
[1400] ibid 91.
[1401] Such as the ones discussed in the context of the construction industry in chp 6.3.2.
[1402] An example is the GCA discussed in chp 6.3.1.

not on the same page.[1403] At present, good faith derived duties are restricted to certain types of contracts or parties. Protecting one type of contract or party leaves the other party vulnerable to opportunistic behaviour as isolated market actors. This is further evidenced by the restrictive judicial treatment of express good faith clauses.[1404] However, the recognition of the crucial role of private ordering requires that it is recognised as a valid, and perhaps superior, 'method for structuring economic exchange, with contract law as a last resort gap filler, or at best a limited corrective to any failure in private ordering.'[1405] This is further supported by the fact that the courts are reluctant to intervene in the operation of freely concluded contracts between business parties, even when the contract was concluded on a standard form. In particular, where the contractual terms have adopted the standard industry ones, such reluctance of the courts to intervene may raise potential issues.[1406] First, the industry terms are likely to reflect the norms of its 'dominant members rather than a fair compromise between all the participants in the collective.'[1407] Second, any mandated dispute resolution mechanism by the industry or regulatory norm-making body may be formally or informally ousting the jurisdiction of the courts, making it unlikely for most users of the private norms to pursue legal action in public courts.[1408] Third, influential norm-making bodies may be influencing lawmakers to avoid any legislative measures restricting the applicability of their norms.[1409] In light of these factors, it may be that the courts' deference to private ordering is influenced not by a fervent dedication to protecting the freedom of contract, but by 'exogenous factors such as the desire to be seen as a receptive and friendly legal home for the operation of a market.'[1410]

Given the above analysis, the enactment of good faith into law as a standard of contractual performance is necessary. This would also alleviate the courts' burden caused by their norm-making capacity, and would restrict their role to a more comfortable one of

[1403] Other industry codes of conduct also refer to good faith as a standard of conduct, which shows that good faith reaches beyond individual business contracts, but is envisaged as the default framework within which parties in business dealings should operate; see eg Financial Conduct Authority, 'FCA Handbook' <https://www.handbook.fca.org.uk/handbook/PRIN/2A/?view=chapter> accessed 3 April 2025, which provides that '[a]cting in good faith is a *standard* of conduct characterised by honesty, fair and open dealing and acting consistently with the reasonable expectations of retail customers' [Prin 2A.2.2, emphasis added].
[1404] See chp 4.4.
[1405] Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 89, for example, common law rules on unfair terms in contracts have been ousted in favour of the rules applicable by the Financial Conduct Authority or the CMA, for contracts within their remit. Also see Avery W Katz, 'Taking Private Ordering Seriously' (1996) 144 University of Pennsylvania Law Review 1745, 1747.
[1406] Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 93.
[1407] ibid.
[1408] ibid.
[1409] ibid.
[1410] ibid 94.

interpretation and application of the law to specific instances of contractual breach. Opting out should not be possible for the reasons discussed in chapter 4.5, as an optional nature would weaken and hamper reform and contractual practice. Ultimately, the contract remains the most critical piece of document which regulates contractual behaviour; however, an uneven approach to good faith implication of duties or interpretation of contracts, at times literal and other times contextual, is precisely the uncertainty in law which the courts are essentially trying to avoid. The responsibility of developing a consistent understanding of good faith across different industries would still fall upon the courts. Repeating the same concept of good faith in various pieces of legislation would be costly and inefficient, and increase the risk of inconsistencies in interpretation.[1411] Reducing the regulatory load on business actors by unifying the fragmented responses to fairness is also necessary due to the difference in rationale behind regulation and law.[1412] Indeed, regulation is concerned with the collective protection of contractual rights and obligations, whereas the law is concerned with individual protection.[1413] In other words, the affected party must seek redress by individual action through the courts, whereas a regulatory body can effect change market-wide, influencing the rights of action of its members. The common law's increasing surrender of its role as 'regulator of contractual activity' in favour of a limited one of 'enforcer of commercial contracts' is problematic.[1414] This criticism is particularly relevant regarding contracts which do not fall within the scope of any regulation or legislation, such as commercial contracts negotiated between businesses falling within the scope of this research. A general principle of good faith would provide a safety net for many such contracts in curbing opportunistic conduct in contractual performance. The flexibility in commercial law required to adjust the misalignment between commercial practice and commercial law would also avoid the requirement for achieving individual policy objectives for different types of commercial contracts, for instance, depending on the bargaining power of the parties. Instead, 'commercial justice' would be achieved by requiring

[1411] Moreover, due to the intersection of the laws applied by the regulators and the courts, there may be inconsistencies in their application, Mitchell, *Vanishing Contract Law – Common Law in the Age of Contracts* (n 76) 101.

[1412] ibid 206, 208, the author posits that the common law rules 'have become marginal to all but a minor subset of transactions' involving discrete contracts. The major issue with the common law's clinging to ideas of freedom of contract by avoiding recognition of societal effects of major change in contract practice, is that it has condemned itself to becoming obsolete, and cannot contribute 'to the important task of controlling the abuse and exploitation of contract norms (...).'

[1413] ibid 101.

[1414] ibid 113 156, moreover, private dispute adjudication, whether mandated by a regulator body or not, does not help create publicly available rules which can serve in future applications of the case, and it is not guided by the 'basic tenet of justice to treat like cases alike,' thereby posing an 'existential threat to legal development, particularly in the common law.'

all commercial contracts to be subjected to the same criterion for flexibility set by the parties' reasonable commercial expectations.[1415]

6.4.2. UCTA 1977

Unreasonable Clauses in B2B Contracts

The regulation of unfairness in contract terms is relevant for curbing opportunistic behaviour in contractual performance.[1416] UCTA 1977 has expanded the regulation of unfairness beyond the common law rules.[1417] Under UCTA 1977, the parties are no longer able to limit or exclude liability for breach of contract, subject to its provisions. As such, UCTA 1977 has ensured a uniform application of such practice in the context of B2B contracts where the parties are dealing based on either one's standard terms. The initial fears that the criteria of 'reasonableness' may cause uncertainty in the application of the law were not realised.[1418] It is a commercial reality that in B2B contracts, even though standard forms might be used, some will be negotiated beforehand depending on the bargaining power of the parties in question. In *Commercial Management (Investments) Ltd v Mitchell Design and Construct Limited and another*, the High Court decided that the exclusion of liability clause in the contract in question was subject to UCTA 1977 despite being a negotiated standard form contract.[1419]

Exclusion clauses will include those that exclude liability for negligence, for misrepresentation, for breach of contract or a substantially different performance of the contract. Such clauses will be subject to a reasonableness requirement under section 11 of UCTA 1977. The term shall have been fair and reasonable, having regard to circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made. A list of factors is listed in schedule 2 of the Act for the court to

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[1415] Puig (n 12) 330, the author frames the need for flexibility in commercial law to achieve commercial justice as being subject to policy considerations. However, this thesis argues that good faith, as a fundamental principle of commercial law, should not be excluded on policy grounds, as doing so would undermine the very flexibility required by commercial practice and run counter to the demands of commercial justice.

[1416] See chps 2.2 and 2.4 on discussion between procedural and substantive unfairness.

[1417] Indeed, prior to UCTA 1977, where an ambiguous clause in a commercial contract was in issue, *contra proferentem* would have required that the clause be interpreted against the party seeking to benefit from it. McKendrick, 'Doctrine and Discretion in the Law of Contract Revisited' (n 238) 15, considers that the *contra proferentem* rule has become irrelevant in the commercial context in particular where the parties have roughly equal bargaining power.

[1418] McKendrick, 'Doctrine and Discretion in the Law of Contract Revisited' (n 238) 11-13, McKendrick considers that despite the fact that 'the balancing exercise can be a difficult one and, while one can occasionally find cases where the balance appears to have been struck by different courts in different places, overall the Act can be said to have achieved its task of regulating the use (and abuse) of exclusion and limitation clauses without impairing unduly the ability of contracting parties of roughly equal bargaining power to allocate the risk of loss flowing from a breach of contract.'

[1419] [2016] EWHC 76 (TCC), [2016] 1 WLUK 306.

consider whether it would be fair and reasonable to incorporate such an exclusion clause into the contract based on the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties to the contract at the time the contract was made. For instance, the Court should consider, if relevant, the respective bargaining positions of the parties; whether the customer received an inducement to agree to the term; whether the customer knew or ought reasonably to have known of the existence and the extent of the term, whether compliance with any condition linked to the operation of the exclusion clause would be practicable at the time of the contract; and whether the goods were manufactured, processed or adapted to the special order of the customer. It is immaterial whether the breach was inadvertent or intentional, or whether liability for it arises directly or vicariously.[1420] Although exclusion clauses for death and personal injury will not be valid, the parties can contract to exclude liability for negligence for loss or damage, subject to the requirement of reasonableness.[1421] There are further considerations to be taken into account at section 13(1), where UCTA 1977 provides for a variety of exclusion or restriction clauses that cannot be made subject to restrictive or onerous conditions.[1422] UCTA 1977's aim to ensure fairness in B2B contracts concluded on standard terms is commendable. However, it remains a topical solution in regards to limitation and exclusion of liability clauses in very specific instances and does not tackle issues related to the performance of the contract.

Law Commissions on UCTA 1977

The submissions made in regards to the reform of the UCTA 1977 in 2015 indicate that efforts to adopt and define good faith in contracts were quickly stopped in their tracks. Indeed, the Law Commissions considered that 'it was neither necessary nor desirable to include an explicit reference to good faith.'[1423] Despite acknowledging that 'everything required by good faith should also be required by this [fair and reasonable] test.'[1424] The reason was essentially that good faith was a foreign concept to English law and was likely to create confusion and mislead the parties. Indeed, UCTA 1977's scope was never expanded further beyond those dealing as businesses on either party's standard terms.[1425] Indeed, the Law Commissions

[1420] UCTA 1977, s 1(4).
[1421] UCTA 1977, s 2.
[1422] UCTA 1977, s 13(1)(a).
[1423] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts* (Law Com No 292, Scottish Law Com No 199, 2005) ('*Unfair Terms in Contracts Report'*) para 3.86.
[1424] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, Scottish Law DP No 119, 2002) ('*Unfair Terms in Contracts Consultation'*) para 4.89.
[1425] However, ss 2(2), 6(3) and 7(3) do apply the reasonableness requirement to exemption clauses in contracts where the contract is not a standard form.

considered that in the context of deals on non-standard terms, the business concerned would have been given the opportunity to negotiate the term, or at least be aware of it and consider the possible consequences of entering into the contract on that basis.[1426] The scope of UCTA 1977's application was not restricted to small businesses; rather, the size of the business was deemed to be a relevant factor in applying the reasonableness test.[1427] Additionally, the scope of UCTA 1977 only covers exclusion and limitation of liability clauses, therefore, other unfair terms are outside its remit, even though it provides the possibility to challenge a term allowing a party to render a contractual performance substantially different from that which was reasonably expected.[1428] The Commissions considered that subjecting a larger business' contract terms to review would create uncertainty.[1429] Therefore, their recommendation was restricted to expanding the protection only for small businesses.[1430]

Despite initially being willing to afford the protection afforded to consumers to all business contracts, the feedback on the Consultation Paper evidenced 'resistance to interference with contracts between businesses in general but widespread support for greater protection for small businesses.'[1431] This was because small businesses are usually subject to many of the disadvantages which apply to consumers.[1432] Indeed, they enter into contracts with larger businesses that have excessively disproportionate bargaining power.[1433] In doing so, a substantial proportion does not seek legal advice.[1434] The number of affected businesses was not insignificant. In 2001, 69% of all UK enterprises had no employees, 20% had between one and four employees, and 5% had between five and nine employees.[1435] More recent statistics show a more significant number of small businesses. In 2024, 95% of all businesses were micro

[1426] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Consultation* (n 1423) para 5.43.
[1427] ibid, para 5.40.
[1428] UCTA 1977, s 3(2)(b)(i).
[1429] Most opponents of a fairness control over all business contracts were the legal professionals, their only argument being the element of uncertainty which would be injected into the legal system, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 4.10.
[1430] ibid, paras 2.24, 5.27-5.30, the protection envisaged went beyond exclusion and liability clauses, and encompassed all of the 'non-core' standard terms.
[1431] ibid, paras 1.12, 5.1.
[1432] ibid, para 4.17.
[1433] ibid, para 5.11.
[1434] In 2022, 9% of small business without employees sought advice on legal issues, Department for Business and Trade, 'Longitudinal Small Business Survey: Business With No Employees, UK 2022', August 2023, <https://assets.publishing.service.gov.uk/media/64e631c0db1c07000d22b34f/LSBS_2022_non_employers.pdf> accessed 3 April 2025, 24; in the same year, only 12% of small businesses with employees sought advice on legal issues, Department for Business and Trade, 'Longitudinal Small Business Survey: SME Employers – UK, 2022', August 2023, <https://assets.publishing.service.gov.uk/media/64e88c0d691aa3000da56df2/LSBS_2022_SME_Employers.pdf> accessed 3 April 2025, 37.
[1435]Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 5.14.

businesses with nine or fewer employees, and 4% were small businesses with ten to 49 employees.[1436] Micro and small businesses combined constituted 35% of total business turnover in the UK (20% and 15% respectively).[1437] The Commissions' recommendation was a separate regime for micro businesses protecting against unfair terms in standard form contracts, excluding review of any of their individually negotiated terms.[1438] Although the Commissions defined small business as employing nine or fewer employees, these essentially constitute micro-businesses.[1439] The reason why the criteria for defining small businesses based on the number of employees and not on turnover was that the regime of proposed micro businesses was 'aiming to protect the least sophisticated businesses, which are so small that they are unlikely to have expertise in contracting or the resources to seek legal advice.'[1440] The same protection was not to be extended to small businesses employing 10 to 49 employees because they were not deemed to require the same level of protection as micro businesses. The recommendation also excluded those companies 'associated with' larger businesses, such as where they belong to the same group of companies. For instance, a small franchise would most likely not have qualified for the small business regime even where it would employ nine or fewer employees.[1441] A 'transaction value limit' was also proposed, for contracts exceeding £500,000 to be excluded from the small business regime.[1442] The reason for this threshold was indicated as twofold. First, it sought to exclude finance businesses that deal with very high value transactions but happen to have very few employees, and second, most small businesses would depend on a few commercial relationships therefore the average annual turnover of a small business was held as the determining factor, albeit admitting that the Commissions relied on a limited research on this sum.[1443] The uncertainty involved in determining the transaction

[1436] Parliament in Georgina Hutton, 'Research Briefing: Business Statistics' (UK Parliament, House of Commons, 11 November 2024) <https://researchbriefings.files.parliament.uk/documents/SN06152/SN06152.pdf> accessed 3 April 2025, 12.
[1437] ibid. Medium-size businesses of 50 to 249 employees constituted 18% of total business turnover, and large businesses with 250 employees or more accounted for 48% of total business turnover.
[1438] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 5.12.
[1439] See the terminology used by the Parliament in Hutton, (n 1435) 12. The number of employees was to be determined based on the average daily number of employees over the course of the preceding twelve months, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 5.40.
[1440] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 5.35. Also, turnover as a criterion for protection was rejected for three reasons, first the sophistication of business and its turnover is not always directly correlated, second, it is easier to determine the number of employees than turnover when entering into a transaction with a business, third, handing over turnover information to other businesses could jeopardise the competitiveness of small business as this information was deemed to be market-sensitive [paras 5.36-5.38].
[1441] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 2.37. k
[1442] ibid, para 2.40.
[1443] ibid, para 5.57.

value was also highlighted in the report.[1444] Contracts which were exempt under the UCTA 1977 would also be exempt for small business contracts.[1445] In any event, individually negotiated contracts would also be excluded from review.

A Statutory Good Faith Clause

If a statutory clause regulating unfairness in contractual performance were to be enacted in UCTA 1977, the issue would only partly be solved due to the instrument's limited scope of application. Where its scope is extended to cover all types of business contracts, exemptions may be created for certain industries or types of contracts that are already regulated under other specific legislation. This would prevent doubling up on similar provisions and avoid confusion in the application of the rules. The limitation of UCTA 1977 in making space for a new statutory good faith clause is essentially problematic. UCTA 1977 specifically deals with unfair terms that limit liability or impose onerous obligations in contracts, particularly protecting parties in weaker bargaining positions. Therefore, its main focus is on balancing the bargaining power in contract terms rather than regulating the conduct of parties during contractual performance. However, a statutory good faith clause as envisaged herein aims to provide protection against opportunistic behaviour regardless of the bargaining power of the parties, the type of commercial contract or the type of contractual clause therein. If its aim were to be revised, then its scope of application could be extended to cover the good faith standard in contractual performance.

As the Australian example has shown us in the context of franchising, the applicable statutory provision of the general duty of good faith would best be served by a standard rather than a rule with a detailed definition.[1446] This is because 'the only solution to devising regulation that has the potential to conform to its policy objectives must be one that employs standards that permit the adjudicator to consider all the circumstances of the impugned transaction.'[1447] A potential provision in the UCTA 1977 can read as follows:

[1444] ibid, para 5.62.

[1445] ibid, para 5.2. These contracts were insurance contracts, contracts for the creation, transfer or termination of an interest in land or in intellectual property, contracts for formation or dissolution of a company, or the creation or transfer of securities, and in some cases contracts of marine salvage and towage, charterparty contracts of ships or hovercrafts, and contracts for the carriage of goods by ship or hovercraft, [para 4.81]. Moreover, financial services contracts were also exempt from the proposed small businesses regime due to already being a regulated area [para 5.65].

[1446] Also see discussion on good faith being an open norm and the distinction between rule and principle at chp 1.3.2.

[1447] Collins, *Regulating Contracts* (2002) (n 344) 267.

i. A party shall act in good faith in the exercise of its rights and in the performance of its obligations arising within [or in connection with] a contract. For the purposes of this section, the party alleging breach need not show vulnerability or any disadvantage relative to the other side.

ii. A party is presumed to act in good faith unless it has failed to exercise the diligence required by the circumstances. For the purposes of this section, the court must have regard to all circumstances that were reasonably foreseeable at the time of the alleged breach. In assessing the conduct of the breaching party, the court may have regard, without limitation, to

    a) whether the party has acted honestly,
    b) whether the party has acted arbitrarily,
    c) whether the party has cooperated to achieve the purposes of the agreement.

iii. The application or the effect of this section shall not be limited by the parties' agreement.

The brackets in section (i) refer to two issues which fall outside the scope of this work but would require further drafting depending on the outcome of such research. The first issue is whether the good faith duties extend to the pre-contractual phase and conduct during dispute resolution. The second is the extent to which third-party rights are affected if they rely on the agreement.

Further, the second sentence of section (i) is to clarify that for good faith duties to operate, the parties need not be dependent on each other in any way, and that even sophisticated commercial parties can claim breach of good faith against another sophisticated commercial party. This helps avoid inequality of bargaining arguments and distinguishes the duty from other common law breaches, such as negligent misstatement, where a duty of loyalty must be owed, or equitable doctrines such as unconscionability, where the vulnerability or disadvantage of the innocent party serves as a deciding factor.

As to section (ii), a presumption of good faith would reflect the general understanding advocated herein that good faith is of the essence of the contract, and any allegation of breach must be proved. A party against whom a breach of good faith duty is alleged has the benefit of a legal presumption that it has acted in good faith. However, the presumption is rebuttable and can be rebutted by the other side when the other side proves that the breaching party has not

exercised the diligence required by the circumstances. The presence of a legal presumption is necessary because the court would not be able to assess the prima facie good faith of the parties, and any breach of the essence of the contract must be proved by the party alleging breach, as with any other breach of contractual performance. However, the creation of a presumption is not entirely in line with the requirement under UCTA 1977 that the burden of showing that a term is reasonable is on the party claiming that the term satisfies the requirement of reasonableness. The party claiming the term is enforceable must show that it is a reasonable term. Therefore, the innocent party need not prove breach of any type, the onus is on the other party to prove not the lack of breach, but the lack of unfairness in respect of the relevant term.[1448] The difference in approach for the onus of proof between the reasonableness of terms and the good faith performance can be justified by reference to the nature of these clauses.[1449] The former deals with the validity of the term in the context of standard form contracts, whereas good faith duties deal with the performance of all types of business contracts, whether negotiated or not.

Section (ii) also refers to the concept of diligence. The diligence required by the circumstances is broader than taking reasonable care or exercising reasonable skill in the context of negligent breach as defined in s1(1) of UCTA 1977. Contractual liability is triggered not because of a breach of a duty of care understood in the tortious sense, but because of the violation of a statutory duty of good faith, which does not distinguish between the bargaining power of the parties. As the assessment of the breach must be objective, the assessment of the circumstances is also on an objective basis, which can be further supported by a contextual interpretation of the contract.[1450] The timing of the assessment must be the time of contracting.[1451] Moreover, no mention is made of reasonableness because it would not be possible to perform in good faith without the behaviour being reasonable.[1452] Reasonableness is also implicit in the reference made to arbitrariness in (ii)(b), for a party cannot act reasonably

[1448] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 4.73.
[1449] The Law Commissions also had proposed to put the burden of proof on the small businesses, unlike in the consumer regime, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) paras 5.31, 5.85.
[1450] ibid, para 3.96, the Law Commissions also had proposed that the assessment of whether a term is fair and reasonable should be determined by reference to 'all circumstances existing when the contract was made.' The enacted law later included reference to 'circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made' (s 11(1) UCTA 1977).
[1451] Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 3.96; this was also how the UCTA 1977 times the assessment of the fairness and reasonableness criteria.
[1452] The Law Commissions also considered there is very little difference between fairness and reasonableness tests in discussing the reform of UCTA 1977, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 3.85.

and arbitrarily at the same time. The parties should be understood as rational people.[1453] Also, there is no mention of a duty to have regard to the interests of the other party or not to have to subordinate one's interests to those of the other party. As indicated in (ii)(c), the loyalty is to be had to the bargain, in which both rational parties understand that each party is to contribute to the deal but is also entitled to take its agreed share of profits. The framing of parties as rational actors also reflects the need for each party to have regard to the interests of the other party, without having to submit one's interest to the other party's.

The list of factors which the court may take into account is non-exhaustive and remains general guidance. A schedule may be useful, similar to that adopted by the UCTA 1977 at its schedule 2 to provide guidelines for assessing diligent behaviour. However, such lists are by nature never complete and carry the risk that the parties may seek to evade the application of the provision by showing that their behaviour fits within one of the examples provided, despite being dishonest or arbitrary conduct.[1454] Therefore, the guidelines drafted as a standard, such as in the above proposed formulation, rather than a specific application of it, should be preferred.[1455]

Section (iii) indicates that the parties cannot contract out of the duty of good faith, and any express duty of good faith in a contract shall be drafted accordingly. The parties can, for instance, indicate their own definitions of good faith or scenarios where good faith shall be breached, but if such scenarios are too restrictive, they may be declared inapplicable under this section. Also, this section prevents the application of express good faith clauses to only some parts of the contract and not others. As such, performance of all contractual obligations is made subject to good faith.

The statutory good faith envisaged herein does not create an independent statutory cause of action, instead, such a claim would operate as a breach of contract.[1456] Moreover, it

[1453] See discussion above in chp 4.2 on rational choice theory.
[1454] Similar concerns were raised previously in regards to the reform of the UCTA 1977, where it was noted by the Law Commissions that examples in legislation may quickly become out of date or turn out to be incorrect or create loopholes to the detriment of the consumer. Instead, the Law Commissions considered that it would be more appropriate to provide the examples in the Explanatory Notes to accompany the draft bill, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) paras 2.53, 3.104, 3.119.
[1455] Elise Bant, Jeannie M Paterson, 'Statutory Interpretation and the Critical Role of Soft Law Guidelines in Developing a Coherent Law of Remedies in Australia' (n 1094) 307, argues that soft law, such as practice notes, can also play a significant role in providing guidance to market players by 'encapsulat[ing] key legal principles in a straightforward and accessible format and then illustrat[ing] their operation by reference to a series of simple but realistic examples.'
[1456] Indeed, this would be akin to an implication in law of good faith duties, although the need for the court to fulfill the necessity criteria required for implying terms in law for specific types of contracts would be dispensed with due to the existence of this statutory provision.

can be used as an interpretative tool (requiring all contractual interpretations to be compatible with good faith), to create new causes of action (such as pre-contractual duties) and it may also serve as a legal basis for anchoring, developing or expanding existing doctrines (such as a duty to cooperate in the context of specific types of contracts). Where a breach of the duty of good faith occurs, this would entitle the innocent party to damages as with any other breach of contract, expectation damages being the relevant measure of damages.[1457] This is not to discard an independent cause of action for good faith in the future, although this would necessitate research both into the role of good faith in the pre-contractual phase and the termination of contracts.[1458] The extent of damages should not be limited to pecuniary loss but also encompass non-pecuniary loss, as also recognised in the new Digital Markets, Competition and Consumers Act 2024 ('DMCCA').[1459] Moreover, the parties remain free to draft liquidated damages clauses into their contracts, thereby limiting the amount recoverable through court action, meanwhile continuing to be subject to the rules on restriction of penalty clauses. Equitable remedies, such as specific performance, are also available, ensuring that the expectations of the parties are fulfilled where compensation by monetary damages is not adequate. Civil penalties may potentially be imposed by the court however they would be more suitable within the context of specific industries or codes of conduct which are then enacted into law to deter breaches of good faith where there is a recognised imbalance of power between the parties, such as in franchising, or in the context of small businesses.

Clearly, the disorganised state of the legislation which affects most B2B contracts favours a call for harmonising and unifying the applicable legislation to business contracts. For instance, the Sale of Goods Act 1979 defines good faith as an act done honestly, whether negligent or not.[1460] However, other legislation relating to the sale of goods or services does

[1457] This would correspond to the 'relentless woodpecker' version of good faith as named by Wishart-Chen and Dixon, 'Good Faith in English Contract Law A Humble '3 by 4' Approach' (n 205) 200, see text to n 424 above. Although the authors advocate for a 'measured tortoise' version of good faith as discussed at text to n 428 above, their rejection of the 'relentless woodpecker' version is unsatisfactorily justified by English's law preference for a rule-based, incremental legal reasoning (202, 210-211). However, they admit that the difference between both versions if a 'matter of degree,' and that 'they may overlap, insofar as incrementalism may facilitate the evolution of new obligations.' (204). For an opposite view, see Davies, 'Excluding Good Faith and Restricting Discretion' (n 585) 104, who argues that even if good faith were to be implied in law (which he opposes), good faith should be viewed not as a term of the contract for which the innocent party can claim breach, rather it should be envisaged as a principle which would prevent a party from enforcing a contract or allow for rescission, as in the case of unconscionability.

[1458] This would correspond to the 'charging bull' version of good faith which is advised against by Chen-Wishart and Dixon, 'Good Faith in English Contract Law A Humble '3 by 4' Approach' (n 205) 198, see n 424 above.

[1459] DMCCA 2024, s 233 for consumers.

[1460] Sale of Goods Act 1979, s 1(3).

not mention good faith.[1461] Not only is good faith restricted to the confines of the Sale of Goods Act 1979, but a particular set of facts can trigger the application of other relevant legislation too. The overlapping scopes of application and the multiplicity of the legislation concerning business transactions are no doubt burdensome, in particular to small businesses. Harmonising legislation regarding business transactions would also appease the concerns of the legislator who would not want, in the first instance, to impose such good faith duties to all contracts beyond those between businesses, similar to a general principle of contract law which is recognised explicitly in a code of obligations in a civil law jurisdiction.[1462] A more substantial rehaul would involve consolidated piece(s) of legislation where competition, consumer and business contracts are grouped into a cohesive framework. Indeed, the Australian example is commendable and reflects an understanding of separate market actors and market rules, which ultimately must co-exist and function together.[1463] Any discord in the functioning of competition rules would negatively affect the functioning of consumer interests, and a malfunction in the application of the business contracts would also directly or indirectly impact consumer interests. Similarly, the non-protection of consumer interests would also have an adverse impact on business interests.

Consequently, the proposed provision seeks to balance clarity with flexibility, thereby allowing the courts to adapt the standard of good faith to the requirements of diverse commercial contexts.[1464] This removes ambiguity about whether and when good faith applies, offering businesses and courts a clear legal framework. Whilst the term 'good faith' is broad and undefined, it is capable of practical application by the courts, who can adopt a contextual understanding of the contract and uphold the parties' presumed intention, where their actual intention is ambiguous. Commercial parties can draft contracts with a clearer understanding of the baseline expectation of the law for contracting parties. Further, by indicating that the courts consider 'reasonably foreseeable circumstances,' the provision clarifies the requirement for a contextual understanding of commercial contracts. Moreover, section (ii) provides a helpful

[1461] Such as the Sale and Supply of Goods Act 1994, Supply of Goods and Services Act 1982, Supply of Goods (Implied Terms) Act 1973.
[1462] Such as s 242 of the German Civil Code, s 1104 of the French Civil Code, ss 2 and 3 of the Swiss Civil Code.
[1463] See discussion in chp 5.4.
[1464] Puig (n 12) 333, the author posits that in order for judicial activity to facilitate commerce and meet the reasonable expectations of the parties, a commercial approach, namely one which seeks to understand the context of the deal rather than only the literal deal, must be adopted by the courts to avoid misalignment between commercial law and commercial practice. This necessitates a flexible application of flexible legal doctrine to commercial practice (330). Speculative concerns for uncertainty arguments can be avoided by anchoring commercial law to the concept of reasonable expectations of the parties (331).

non-exhaustive guideline for judicial interpretation. The abstract nature of the drafting is necessary to ensure that the standard can evolve with case law and reflect the commercial practices over time. This is crucial in addressing the challenges posed by contracting in new contexts, such as digital contracts, where the development of common law can be slow.[1465] It is also necessary to account for various characteristics of a commercial contract, such as the equality of the bargaining power or the absence thereof. Although there may appear to be a stronger argument to recognise good faith to protect vulnerable parties in systemically power-imbalanced contracts or industries, the argument is just as strong in the context of sophisticated commercial parties negotiating at arm's length. This is because good faith, as posited herein, is inherently connected to the reasonable expectations of the parties and where the contract is ambiguous, such expectations are presumed based on an objectively defined reasonable person's viewpoint adopting a contextual understanding of the parties' deal.

Moreover, the proposal aims to consolidate the common law's fragmented approach to unfair behaviour into a unified statutory standard. Whilst some references to good faith exist as explored in this thesis above, they fall short of embodying the full potential of the concept and fail to recognise the reality of commercial contexts in determining the parties' intentions as presumed rational actors. By giving the good faith standard a legislative foothold, it provides a clear baseline for commercial actors and reduces reliance on existing piecemeal and uncertain common law developments. Further, a statutory standard minimises the risk of diverging judicial interpretations, particularly in areas where the common law has been hesitant to impose a duty of good faith, for instance in determining whether such duties exist in fettering contractual discretions. Another important function of this proposal is that, unlike the existing common law, which has often developed to react to specific disputes, it proactively encourages commercial parties to act in good faith, fostering trust and cooperation in business dealings from the outset and for the duration of the contract. This proposal ultimately fills an important gap in the common law by explicitly addressing opportunistic behaviour and ensuring that good faith operates as a principle in its own right rather than an incidental one or an afterthought once a dispute arises.

As with any new statutory provision, there may be an initial period during which its application raises questions of uncertainty. However, such risk is mitigated by the drafting of

[1465] See for instance, Farshad Ghodoosi, 'Contracting in the Age of Smart Contracts' (2021) 96 Washington Law Review 51, who posits the challenges of analysing smart contracts from a traditional contract law lens and proposes a reliance-based framework to resolve associated disputes.

the proposed provision itself. For instance, it provides for a presumption of good faith, creating a default position against which all contractual conduct will be assessed. The requirement for diligence and the guideline referring to honesty, arbitrariness and cooperation offer concrete benchmarks for courts and commercial actors to follow. Also, the courts are required to consider all reasonably foreseeable circumstances, which provides for an objective assessment, discarding, or limiting overly subjective interpretations. In addition, by specifying that the standard applies regardless of the parties' agreement, the proposal avoids the potential for contractual clauses to undermine its effectiveness. Overall, any risk of uncertainty in the short term is outweighed by the long-term benefits of establishing good faith as an overarching principle in contractual performance. Refinement of the concept and its application will come in time as the courts and the parties rely on it in settling disputes.

6.4.3. Regulatory Oversight and the Digital Markets, Competition and Consumers Act 2024

Regulatory Rule Making

The regulatory approach to tackling risks and problems is multifaceted. Baldwin and Black adopt an analysis by contrasting risk-based and problem-centred regulatory techniques. A risk may be 'adverse events that may occur in the future' whereas problems are 'things that have happened or are happening or may happen and which require attention.'[1466] Rather than distinguishing between these two concepts, a three-step identification and prioritisation process is applied to both: (i) first, theoretical or ideological perspectives, (ii) second, operational constraints, and (iii) third, political, communicative or reputational factors are identified.[1467] Risk-based regulation is how the UK government has approached regulation-making, by focusing on the most serious risks that stand in the way of achieving its objectives. [1468] The most important aspect of this approach is understanding how risks are 'constructed, packaged and identified', for which the authors propose the three-step process above.[1469]

A statutory approach to good faith, rather than an industry or contract-type based one, would allow for various relevant regulators to adopt a tailor-made approach to meeting their respective objectives. Adopting a single standard in the performance of commercial contracts

[1466] Robert Baldwin and Julia Black, 'Driving Priorities in Risk-based Regulation: What's the Problem?' (2016) 43(4) Journal of Law and Society 565, 566-567.
[1467] ibid 566.
[1468] ibid 565.
[1469] ibid 569-570.

would not mean that all regulatory agencies would approach good faith duties in a uniform manner. Indeed, depending on the various choices made by the specific regulator, where the three-step method is applied, a differentiated roadmap may be adopted for each regulator to achieve its legal mandate. For instance, the GCA may not approach good faith duties imposed within the context of supply chain practices of retailers and grocery suppliers in the same way as the SBC seeks to tackle late payment issues faced by small businesses.[1470] The identification of the risks or problems in a given industry, where a regulator exists or is to be established, can serve as the 'building blocks of regulation' within that particular industry.[1471] Therefore, identifying the risk and consequences of opportunistic conduct which can negatively affect commercial parties in that particular industry, and therefore the industry as a whole, and devising regulations accordingly is crucial. If the regulators can

> focus on communicating the rationales for their identification, selection, and prioritization of risks to external communities, facing head-on the public scrutiny that transparency brings, and being open about the complex balancing of risks, resources and reputations that risk-based regulation involves,[1472]

they can avoid 'myopia or system-blindness' which can result in 'feedback loops' that 'reinforce the currently dominant frame and stand in the way of the adjustments that are needed to make that framework relevant to a shifting world.'[1473]

Rule-making is context-dependent; however, a standardised approach can be adopted by focusing first on the design of the regulatory system, second, the significance of the market context, third, the circumstances in which interpretive communities can be built, and fourth, the relevance of the regulatory system's own evolution.[1474] The design of the regulator system is important as it determines what type of rules will be adopted. For instance, a regulator may be inclined to adopt strict, detailed rules or vague rules which do not attract legal consequences. Thus, the regulator will determine what uses of rules are deemed 'appropriate and acceptable.'[1475] For instance, different consequences for the violation of good faith duties may

[1470] ibid 586-588. Indeed, such differences are attributed to various factors, such as the regulatory objective of the respective regulator, the extent of the information gathered in order to assess the risk, the strategies developed by the respective regulator in order to tackle the risk, or the existence or absence of any enforcement action to comply with the legislative framework.
[1471] ibid 593.
[1472] ibid 595.
[1473] ibid 594.
[1474] Black (n 394) 247.
[1475] ibid 248.

be provided by the regulator's rules in industries where there is a systemic imbalance of power, and different ones for those where such imbalance is minimal. Second, the market context closely relates to the interpretation of the rules; therefore, the aim of the rule. This is because the rule maker will seek to optimise how the rule can achieve its purpose, for instance by providing for a multiplicity of rule types to avoid the issue of under- or over-inclusiveness of the rules.[1476] Therefore, a regulator in an industry where there is a systemic power imbalance between market players can provide for both specific ways of conduct in particular instances where the weaker market players may be at risk of harm, and for guidelines for desired conduct by the stronger parties in other instances where such risk of harm towards weaker players would not exist. Third, the development of interpretative communities can have a significant impact on the use of the rule. To minimise the risk that users of the rule would seek to exploit loopholes in the rule, the rule maker can seek to ensure that the interpretation of the rule is as uniform as possible, for instance by limiting the discretion provided under the rule, or providing a particular criterion for interpretation.[1477] Therefore, institutional practices can be strengthened through training or education whereby institutional players such as the 'rule makers, regulatees, enforcers, adjudicators' all share the same interpretative approach to the rule.[1478] There may be tension between judicial interpretation and the regulatory one in that the courts may impose 'an interpretation or allow an interpretive strategy that the regulator or regulated (at least in the absence of professional legal advice) would not share.'[1479] This may be overcome, for instance, by

> [c]onfer[ring] power on the regulator to formulate rules which had evidential status and which thus served as guides for the interpretation of vaguer legislative provisions, instructing the court, in effect, as to their interpretation.[1480]

The legislator may also 'close off' the possibility for the courts to interpret regulatory rules by providing that the breaches of these regulatory rules are not subject to private enforcement by individuals in courts, but only through regulatory disciplinary action.[1481] Such strategies can affect the effectiveness of interpretive communities and tackle issues of creative

[1476] ibid 7-8, indeed, as rules are generalisations, the process of rule-making requires that the rule maker focuses on the 'causally relevant' aspects of particular instances which can optimally achieve the aim of such rule. Such selection amongst various instances can result in some instances not being caught by the rule (under-inclusiveness) or other instances being unnecessarily caught by the rule (over-inclusiveness).
[1477] ibid 30.
[1478] ibid 31-32.
[1479] ibid 33.
[1480] ibid.
[1481] ibid 34.

compliance.[1482] Importantly, interpretive communities do not develop naturally, without active planning. Ultimately, the 'aim in developing interpretive communities is to develop mutuality of interpretation amongst all those involved in the regulatory process: rule maker, enforcer, regulated.'[1483] Finally, the regulatory system's own evolution can also affect the use of its rules, where if the system is in its infancy, the rules may not be effectively used, whereas the more developed it is, the more efficient the rules will be.[1484]

This theory of regulatory rule-making suggests that if applied in the context of good faith, and where a statutory good faith clause is enacted as suggested herein, then the responsibility for developing and applying such a clause would not solely rest on the courts. Indeed, promoting a contextual understanding of commercial contracts and adopting a collaborative rather than adversarial view of contracting can be more effectively achieved where the interpretive community adopts such a common view. A statutory provision enables the rule-making on a regulatory level to begin, and protects against opportunistic behaviour in the performance of commercial contracts at the outset. Where a regulator is present or is set up and new rule-making is in process, the regulator can rely on such a statutory clause to design and implement its rules. Where no regulation is currently necessary, or where a regulator does not yet exist, the statutory provision provides an anchor for courts in settling disputes where contractual performance fails to meet the reasonably expected good faith standard in the context.

Consequently, such a statutory provision of expansive application cannot be understood or applied in a vacuum; performance of commercial contracts requires a dynamic and context-sensitive approach that acknowledges the interplay between legal principles, regulatory objectives, and market realities. By relying on a statutory standard of good faith, regulators can craft industry-specific frameworks that balance flexibility with legal certainty, ensuring that commercial practices evolve in line with broader economic and ethical considerations. This ensures that the expectations of fairness, honesty, and reasonableness in commercial dealings

[1482] ibid 35.
[1483] ibid 35-36. The author notes that such self-regulation allows flexibility and facilitates the use of vague, purposive rules and avoids issues raised by legalism or literalism. Consequently, the rule maker can be confident that its interpretation will be adopted by other members of the interpretive community. To avoid any issues relating to the accountability of regulators if the monopoly is given solely to the rule maker, the author proposes that other members of the interpretive community become involved in the formation of the rules or that a particular judicial interpretive approach is adopted by giving precedence to the regulator's interpretation of its rules, 'striking it down only if it was not within the range of interpretations that could be reasonably expected of the rule' (37).
[1484] ibid 249.

are not only aspirational but also enforceable, thereby fostering a culture of compliance and cooperation, reducing adversarial disputes and enhancing business relationships.

The Digital Markets, Competition and Consumers Act 2024

There is a clear link between the existence of a robust regulatory institution and the effectiveness of the regulations within its remit. For instance, the GCA is responsible for overseeing the application of the GSCP in the UK, the ACCC is responsible for the application of the FCOC in Australia.[1485] Even the voluntary codes have recognised that institutional oversight is needed. Indeed, the BFA oversees the application of the BFA Code, or the Intellectual Property Office oversees the UK Voluntary Code of Good Practice on Transparency in Music Streaming.[1486] Similarly, in Australia, the ACCC is responsible for overseeing the voluntary Food and Grocery Code of Conduct.[1487] Where the regulator is given dispute resolution powers, generally, their deep understanding of the sector is considered a strength for efficient dispute resolution.[1488]

In the UK, the Competition and Markets Authority (CMA) is the primary competition and consumer authority.[1489] It is a non-ministerial body which regulates the market and tackles unfair behaviour. Its aim is 'to promote an environment where people can be confident they

[1485] Another example of a mandatory code of conduct which is supervised by the ACCC is the Horticulture Code of Conduct which applies between growers and traders of horticultural produce, regulated by the Competition and Consumer (Industry Codes—Horticulture) Regulations 2017 (Cth).

[1486] Another example of a voluntary code of conduct in the UK which is supervised by an institution is the Chartered Institute of Horticulture ('CIH'), 'Code of Professional Conduct of the Chartered Institute of Horticulture' <https://www.horticulture.org.uk/membership/criteria/code-professional-conduct/> accessed 3 April 2025. In response to the House of Lords' Horticultural Sector Committee Inquiry on the Horticulture Industry, the CIH submitted that there is a need for improving cross departmental collaboration to deliver dedicated governmental strategy for the industry, see CIH, 'House of Lords Horticultural Sector Committee' (Chartered Institute of Horticulture, February 2024) <https://www.horticulture.org.uk/news/house-of-lords-horticultural-sector-committee/> accessed 3 April 2025. Indeed, the lack of ministerial oversight for horticulture is recognised and clearly hampers the further development of a £5 billion worth industry, see House of Lords Horticultural Sector Committee, 'Sowing the Seeds for a Blooming Horticultural Sector in England' (UK Parliament, 6 November 2023) <https://ukparliament.shorthandstories.com/horticulture-sector-lords-report/> accessed 3 April 2025.

[1487] Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015 (Cth). The code has an explicit duty to act in good faith on the retailer or wholesaler towards the supplier (s 6b).

[1488] Ministry of Justice, Call for Evidence on Dispute Resolution in England and Wales, Summary of Responses, (*UK Government*, March 2022) <https://assets.publishing.service.gov.uk/media/62419499e90e075f11205805/dispute-resolution-in-england-and-wales-summary-of-responses.pdf> accessed 3 April 2025, 10.

[1489] The other institution responsible for enforcing consumer protection laws is the Trading Standards Services ('TSS') however their enforcement power is local, and focused on trading standards, environmental health and fire safety, whereas the CMA takes the lead role in cases involving market-wide issues, issues involving consumer choice and unfair contract term issues, see Nigel Parr, Christopher Eberhardt, 'Consumer Protection Laws and Regulations UK 2024' (ICGL, April 2024) <https://iclg.com/practice-areas/consumer-protection-laws-and-regulations/united-kingdom> accessed 3 April 2025.

are getting great choices and fair deals, competitive, fair-dealing businesses can innovate and thrive, and the whole UK economy can grow productively and sustainably.'[1490] The CMA regularly conducts a consultation on its annual plans and has recently published feedback from stakeholders.[1491] Its focus is on balancing priorities between innovative markets and those where consumers spend the most money and time.[1492] It has both formal and informal powers, such as advocacy, engagement, and information campaigns. Under the new DMCCA 2024, the CMA is gaining new enforcement powers; for instance, it can impose direct sanctions without involving the courts for certain breaches of consumer protection laws.[1493] It will be able to impose fines of up to 10% of annual global turnover.[1494] Previously, the consultation on reforming competition and consumer policy had revealed that there was no clear evidence whether other sector regulators, such as Local Authority Trading Standards Services ('LATSS'), should also have direct administrative powers, such as imposing monetary penalties, where consumer protection regulations were breached.[1495] However, the government responded that because LATSS consists of small number of qualified employees of a local authority who are authorised to enforce trading standards law, the 'diffuse structure lacks the institutional capacity of a regulatory authority to set rules, intervene in markets and adjudicate the law in the same style as a court.'[1496] Moreover, many stakeholders considered that direct administrative enforcement powers were crucial in effective protection against non-conforming parties because court action was not deemed to be effective, and the proposed penalties would provide stronger incentives to comply.[1497] Further, the government considered that dispute resolution had to be speedier to strengthen the enforcement of consumer protection

[1490] CMA, 'About Us' <https://www.gov.uk/government/organisations/competition-and-markets-authority/about>, accessed 3 April 2025.
[1491] Ministry of Justice (n 1487) 6.
[1492] CMA, 'Annual Plan 2024/25 Consultation, Summary of Responses' (*CMA*, 2024) <https://assets.publishing.service.gov.uk/media/65f19fa8133c22b8eecd38d3/___Consultation_response___.pdf > accessed 3 April 2025.
[1493] The new DMCCA 2024 has repealed the Consumer Protection from Unfair Trading Regulations 2008 and transposed some of its provisions into the new law.
[1494] UK Government, Department for Business, Energy and Industrial Strategy, 'Consultation Outcome, Reforming Competition and Consumer Policy: Government Response' (*UK Government*, 20 April 2022) <https://www.gov.uk/government/consultations/reforming-competition-and-consumer-policy/outcome/reforming-competition-and-consumer-policy-government-response> accessed 3 April 2025, Breaches of Consumer Protection Law.
[1495] ibid, Empowering the Sector Regulators to Enforce Consumer Law Directly.
[1496] ibid.
[1497] ibid, Strengthening Sanctions for Breaking the Rules, Non-Compliance with Information Gathering Powers. Also see Department for Business and Trade, Department for Science, Innovation and Technology, 'Strengthening Consumer Enforcement and Dispute Resolution: Policy Summary Briefing' (*UK Government*, 21 December 2023) <https://www.gov.uk/government/publications/digital-markets-competition-and-consumers-bill-supporting-documentation/strengthening-consumer-enforcement-and-dispute-resolution-policy-summary-briefing> accessed 3 April 2025.

law.[1498] Similarly, the effectiveness of financial penalties both by the CMA and the civil courts and the importance of a central authority in setting, applying and monitoring standards for compulsory alternative dispute resolution (ADR) services within the context of consumer law enforcement regime was explicitly recognised in the DMCCA 2024 reform of consumer law.[1499] Further, the government recommended that 'there is effective competition among ADR providers to ensure there is a downward pressure on costs and upward pressure on quality, and to encourage innovation.'[1500]

The CMA has one single clear statutory duty, which is to 'promote competition, both within and outside of the UK, for the benefit of consumers.'[1501] When businesses do not engage in a competitive market, the markets tend to be dominated by a small number of powerful companies, which also prevents access to other firms.[1502] This results in higher prices for consumers.[1503] Therefore, unfair practices between businesses are discouraged from a competition lens, due to their negative consequences for the consumers. Despite setting out a clear ambition for its 2023-24 annual plan to 'help people, businesses and the UK economy by promoting competitive markets and tackling unfair behaviour,' it is unfortunate that the new DMCCA 2024 has not considered whether to expand the powers of the CMA to unfair practices between businesses even where competition laws are not triggered.[1504] This was also reflected in the letter addressed by the chairman of the CMA to the Secretary of State for Business regarding legislative reform proposals.[1505] It stated that careful consideration had been given to 'changing the substance of competition law prohibitions, for example by introducing an explicit prohibition on unilateral conduct that exploits economic dependence or inequality of

[1498] Department for Business and Trade, Department for Science, Innovation and Technology, Strengthening Consumer Enforcement and Dispute Resolution: Policy Summary Briefing (n 1496).
[1499] ibid.
[1500] ibid para 15.
[1501] CMA, 'Department for Business and Trade Consultation: Smarter Regulation: Strengthening the Economic Regulation of the Energy, Water and Telecoms Sectors - Response from the Competition and Markets Authority' (*CMA*, January 2024) <https://assets.publishing.service.gov.uk/media/65face799316f5001164c3be/___CMA_response_to_DBT_consultation_Smarter_regulation_strengthening_the_economic_regulation_of_the_energy__water_and_telecoms_sectors__.pdf> accessed 3 April 2025, para 2.
[1502] ibid para 5.
[1503] ibid.
[1504] CMA, 'Annual Plan 2023 to 2024' (*CMA*, 23 March 2023) <https://www.gov.uk/government/publications/cma-annual-plan-2023-to-2024/cma-annual-plan-2023-to-2024> accessed 3 April 2025. The overarching purpose of CMA remains the same under its latest annual plan, see CMA, 'Annual Plan 2024 to 2025' (*CMA*, 14 March 2024) <https://assets.publishing.service.gov.uk/media/65f1a6f5981227a772f61377/CMA_Annual_Plan_2024-25.pdf> accessed 3 April 2025, para 3.1.
[1505] CMA, 'Rt Hon Lord Tyrie, Letter to the Rt Hon Greg Clark MP' (*CMA*, 21 February 2019) <https://assets.publishing.service.gov.uk/media/5c73d0e0ed915d3553eb4d77/Letter_from_Andrew_Tyrie_to_the_Secretary_of_State_BEIS.pdf> accessed 3 April 2025.

bargaining power, even in the absence of an established dominant market position (...).'[1506] However, the CMA's stance was that 'many of the concerns about the nature and scale of consumer detriment can be addressed through market tools', together with the new proposals if adopted, therefore it was deemed that it was sufficient to keep the topic under review.[1507] As such, the CMA recognises that the interests of businesses as business customers and those of consumers do not always align. The lack of any explicit governing principles in the new proposal further impedes the decision-making process of both the CMA in its regulatory actions and those of the market players in abiding by their regulatory obligations. This is because the arguments for market efficiency and fairness may be antagonistic in determining a specific course of action. The introduction of statutory good faith duties or the prohibition of unconscionable conduct, such as in Australia's Consumer and Competition Act 2010, would have helped to bridge the gap and regulate unfair trading practices not caught by the current consumer and competition regulations.[1508]

Ideally, the new DMCCA 2024 should have incorporated provisions to regulate opportunistic behaviour in contract performance. Indeed, enhancing competitiveness in the market, as accepted to be one of the CMA's regulatory roles, requires regulation that seeks to further this aim. Deterring commercial practices which negatively impact such competitiveness should be an important regulatory aim, in particular in areas where there is an inherent asymmetry of power in the type of business relationship.[1509] However, outside of such specific contexts, the open-textured nature of a good faith standard would better be suited to tackling opportunistic conduct than specific rules.[1510] A further step in the adoption of the DMCCA 2024 should have been to review the adequacy of the UCTA 1977 in today's market conditions, abolish the unnecessary provisions, and enact the remaining ones, together with a good faith standard as provided in chapter 6.4.2, into the DMCCA 2024.[1511] The opportunity has now

[1506] ibid 14, fn 23.
[1507] ibid.
[1508] The Australian Consumer Law was discussed in chp 5.4.2. It is acknowledged in literature that there is an increasing recognition of the need for 'closer interaction between competition and consumer law,' and that for instance a statutory intervention for regulating 'unconscionability' may be required in the context of defects on consent: see Saintier, 'Defects of Consent in English Law: Protecting the Bargain?' (n 561) 131.
[1509] Collins, Regulating Contracts (2002) (n 344) 282-283.
[1510] ibid 286.
[1511] The Law Commissions, in proposing the small business regime, had considered that a regulatory body for policing small business contracts could be useful, however, they could not identify a suitable enforcement body capable of meeting the cost and willing to take on the task, see Law Commission and Scottish Law Commission, *Unfair Terms in Contracts Report* (n 1422) para 5.95. The task would be in any event more suitable for the CMA, and the placement of the already established Small Business Commissioner within the CMA's structure would no doubt help save costs.

been missed, however, if and when a review of the UCTA 1977 and the DMCCA 2024 is undertaken in the future, the legislator should strive to amalgamate disparate pieces of legislation into one, and provide a more cohesive ensemble of rules and standards for market users, practitioners and judges. This is all the more necessary because the UCTA 1977 seeks to regulate *some* terms in *some* business contracts, not all, and is not concerned with *how* the parties perform their obligations. Therefore, it would be anomalous to have restrictions on the validity of certain types of business contract clauses and not on others, and not regulate the use of valid contractual terms by the parties in the course of their contractual performance, in particular where a general good faith duty is being imposed on all business contracts.

6.5. Conclusion

A parliamentary consultation process is an insightful one through which various stakeholders can voice their opinions in regards to a particular topic. It provides academics, practitioners, and legislators with valuable empirical information for future research and policy making. However, the legislative process is where policy is made, and there must be 'good reasons' to change the law for it to be a reasoned choice.[1512] The lack of general empirical evidence due to the private nature of commercial activity between businesses and that of alternative dispute resolution mechanisms that do not publish commercial decisions, which may aid in the development of the law, leaves us with the information which we can find in the case law.[1513] However, in addition to case law, certain industrial initiatives, such as in the franchising or construction fields, have shown that there is a need to self-regulate to curb opportunistic behaviour by publishing codes of conduct that include a good faith standard. Moreover, the government has also recognised the need to protect small businesses, either through establishing the SBC or by envisaging reform in regards to unfair contract terms in contracts with small businesses, which are yet to be enacted into law.

The failure of the DMCCA 2024 to consider and enact obligations of good faith into business contracts to curb opportunistic conduct is a missed opportunity. Although a good faith provision to that effect could be incorporated into the UCTA 1977, it would not be an ideal endeavour without a complete rehaul of its statutory purpose. More importantly, between

[1512] Richard Ekins, *The Nature of Legislative Intent* (Oxford University Press 2012) 115-116.

[1513] Mitchell, *Vanishing Contract Law - Common Law in the Age of Contracts* (n 76) 153, explains that disposing of legal disputes by way of private methods, such as settlement or alternative dispute resolution, has been increasingly popular, and can be explained by various factors, such as the proliferation of alternative dispute resolution in commercial disputes, and the civil procedure initiatives from Woolf reforms onwards facilitating and actively encouraging parties to engage in alternative dispute resolution.

consumer contracts on the one side and conduct that is caught by competition rules that ultimately impact consumers on the other, there remain B2B contracts that also form part of the equation, requiring legislative attention. Statutes such as the DMCCA 2024 are not of general application to all commercial contracts.[1514] Therefore an overarching duty of good faith can only operate either through a standalone piece of legislation encompassing all commercial contracts, or through an expansion of the scope of existing legislation, of which UCTA 1977 is currently the most relevant, which could be amended to incorporate a larger set of commercial contracts and parties, and provide for a standard in the performance of such contracts. Moreover, a statutory good faith provision, rather than an industry-specific approach, would provide regulators with a flexible foundation for designing tailored rules, ensuring that the regulation of commercial contracts aligns with market conditions and power dynamics. By fostering interpretive communities and allowing regulatory frameworks to evolve, such a provision would enhance compliance, reduce disputes, and promote fairness and trust in commercial dealings. In any event, any future rehaul of the commercial law instruments addressing unfairness or opportunistic conduct should aim to unify the fragmented pieces of legislation that currently deal with these issues.

[1514] DMCCA 2024's main focus is the regulation of competition in digital markets, see DMCCA 2024, s 1.

CONCLUSION

While contract law prioritises freedom of contract, the current piecemeal judicial approach to good faith creates inconsistency and uncertainty in contractual performance. A more coherent, statutory approach is needed to prevent opportunistic behaviour and provide clarity to commercial actors. The recognition of good faith as a foundational principle in commercial contracts is not merely a matter of legal refinement but an economic necessity. Indeed, commercial law provides economic value to society by supporting growth in commercial transactions and providing greater confidence between parties.[1515] A statutory duty of good faith would enhance commercial certainty, deter opportunistic behaviour, and foster a culture of fair dealing. By embedding this principle into the legal framework, the law can better serve the evolving needs of businesses, reinforcing trust and stability in commercial relationships for the future.

Commercial contract law seeks to uphold the reasonable expectations of honest businesspeople, thereby facilitating commercial exchange by providing efficient defaults. However, even where a contract is drafted carefully and extensively, the risk of opportunistic conduct remains a significant concern. Good faith's role is to deter such conduct, filling contractual gaps in instances where explicit deterrence mechanisms are absent. Good faith does not require a precise definition to function as a core principle of commercial law. It is a standard of conduct that is required of all commercial parties, generally understood as meaning conduct that is honest and loyal to the bargain. It does not require a party to subordinate its interests to those of the other. As a principle, however, it requires concretisation. For instance, where a party exercises a contractual discretion, good faith would require that it does not use it arbitrarily, capriciously, and more generally irrationally, against the business purpose of the contract. A clear example is when the contract makes the promisor's duty to perform contingent on its discretionary satisfaction with the promisee's performance; in such cases, the promisor cannot in good faith refuse to perform on a whim without any rational basis for such behaviour. To answer the question of the research as to whether there is a need for an overarching good faith principle in commercial contracts, the answer is affirmative. The current piecemeal approach is incoherent and affected by the same uncertainty criticism frequently raised against a general doctrine of good faith.

[1515] Oxera for LegalUK (n 12) part 2.

An obligation of good faith in the context of contract performance can arise in various ways. It can be an express term of the contract. It can be implied in fact to give business efficacy to the contract, or it can be implied in law as a necessary incident of the contract. Another possibility is for the obligation of good faith to serve as a principle of construction which is 'inherent in all common law contract principles,' eliminating the need for implication methods.[1516] The current approach of the judiciary is to uphold good faith as an express term, albeit restrictively or imply it only where necessary on an ad hoc basis. The implication of good faith in law is not consistently applied in the context of commercial contracts due to the difficulties presented by a relational classification of contracts. A revenue generating and sharing categorisation may better identify contracts grounded in a cooperative ethic. However, such categorisation comes with its own limitations. Indeed, a strict categorisation of contracts to which good faith applies as a default standard would restrict the application of a more general principle of good faith, which should apply to the performance of all commercial contracts.

Industry-led initiatives, such as those explored in the construction or franchise contexts, reveal a growing trend among commercial actors to establish a level playing field by imposing good faith requirements in the performance of contracts, in particular where there is an inherent imbalance in the commercial relationship. Franchising contracts are an ideal litmus test for assessing good faith in the context of contractual performance, as they are intended to be lengthy and they contain an informational and power imbalance in favour of the franchisor. The contract's limited capacity in addressing different types of issues that may arise during the lengthy course of the contract acts as a reminder that the parties' conduct should be informed by the cooperative nature of the performance rationally intended by the contract.

The current incohesive piecemeal solutions to problems of unfairness are further compounded by the oscillation between two views of good faith in case law, namely between strict applications of freedom of contract and a relaxed concept of morality.[1517] Although at times the courts emphasise freedom of contract, other times a contextual view of contracts allows for a more liberal incorporation of morality, expressed as fairness. Despite the inadequacy of the relational categorisation of contracts to imply good faith duties, there is a clear need to institutionalise a relational approach to give full effect to good faith in commercial contracts. Indeed, current judicial developments, such as those seen in cases like *Yam Seng* or

[1516] John W Carter, Elisabeth Peden and Greg J Tolhurst, *Contract Law in Australia* (5th edn, LexisNexis Butterworths 2007) 21.
[1517] ibid.

Bates, indicate a willingness to treat parties as presumed rational people assessing their conduct and determining breaches based on reasonable expectations.[1518] For instance, if a party is using a contractual discretion, this exercise will likely be assessed against the reasonable expectations of the parties involved. Clearly, there can be no strict separation between freedom of contract and fairness, and a view of good faith that recognises the former but not the latter in contractual performance is an anomaly which needs correcting. Given the reluctance of the courts to undertake such a task, the logical step is for Parliament to intervene.

The solution proposed by this research is a statutory duty of good faith in the performance of commercial contracts. An opportunity to address this issue was missed with the newly adopted DMCCA 2024. Indeed, the unfairness problems are either addressed therein at a consumer level, or at a competition level and do not make provisions for contracts which do not fall in either category. The Australian example of a statutory good faith in franchising and unconscionability prohibition in contractual performance between businesses has demonstrated that such defaults can be integrated into commercial contracts, without generating much-feared uncertainty and disturbance to the application of the law. Moreover, the effectiveness of these regulations depends on robust regulatory bodies capable of enforcing such standards, in particular where the regulator works closely with actors in its relevant field, engages in capacity building and implements alternative dispute resolution mechanisms. Although the courts are traditionally the ultimate dispute resolution forums, the role of industrial regulatory bodies, such as the Groceries Code Adjudicator, should not be underestimated, in particular when empowered to impose financial sanctions. A well-calibrated statutory approach allows for adaptability, enabling regulators to respond effectively to emerging risks and systemic challenges within their respective industries.

Good faith will undoubtedly remain a topic of discussion for many years to come. The various topics excluded from the scope of this research each deserve further investigation. For instance, examining pre-contractual good faith, or the role of good faith in the termination of contracts and its effects on remedies, would expand our understanding of its application across the entire lifecycle of a contract. Much of the research explored herein has focused on case law and doctrinal work, concluding with normative proposals. However, there is a notable lack of empirical research on the topic.[1519] In particular, understanding the practical needs of the

[1518] *Yam Seng* (n 3), *Bates* (n 48).
[1519] Research such as that of Perrigot, Terry, Di Lerna, 'Good Faith in Franchising -The Perceptions of Franchisees, Franchisors and Their Lawyers in the French Context' (n 1089) is a good example of how empirical

market actors would be vital in the development of the law.[1520] Although empirical evidence is not necessarily required for a general statutory duty of good faith in contract performance, it would be essential for determining more detailed applications in specific industries, such as franchising, where more precise legal approaches could be crafted.

Additionally, interdisciplinary research, such as socio-legal or socio-economic studies, would further help illuminate the risks of opportunistic behaviour where regulation would be most needed. For instance, while significant organisational and marketing research has been conducted on franchising, these insights are rarely examined from a legal perspective.[1521] More importantly, policy priorities of the elected officials, and therefore the allocation of resources to the creation or maintenance of regulatory bodies, as well as the size and the strength of industry bodies, are likely to influence the development of this area of law. Another area of further research in the context of England and Wales is to undertake a socio-legal analysis of the parliamentary process and regulatory options to uncover the reasons behind a lack of impetus on certain topics, such as the failure of enacting legislation against unfair contract terms for small businesses whilst approving the launch of SBC, or the interaction between enacting legislation and policy making, which undoubtedly requires empirical insight. Comparative studies on the topic are also helpful to an extent. For instance, some common law countries, such as the US or Canada, have recognised, either statutorily or through case law, an explicit good faith duty in the performance of contracts. However, they can only serve as an inspiration for the English law. Indeed, such countries are characterised by various levels of regulation across different states or provinces and territories, which can impact the uniformity in the application of the law.[1522]

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law can be conducted in the context of good faith. The research focused on the views of 18 franchisees, franchisors and lawyers specialising in franchising who explained how they define and understand good faith.

[1520] In increasing the attractiveness of English law, the Oxera report emphasises the need to further the 'network effect' whereby 'English law is used more and more, and the benefit by those who use English law (i.e. corporations and financial institutions) grows with the total number of uses,' see Oxera for LegalUK (n 12) 2. Recognising good faith can contribute to creating a more robust legal environment generating positive network effects by fostering a culture of integrity within the legal ecosystem.

[1521] Rozenn Perrigot, Begona López-Fernández, Guy Basset, '"Conflict-Performance Assumption" or "Performance-Conflict Assumption": Insights from Franchising' (2020) 55 Journal of Retailing and Consumer Services 1, 3-4, examples of conflict topics within the franchising relationship include lack of franchisor support, lack of effective communication or misrepresentation regarding use of advertising fees.

[1522] For instance, the UCC definition has not been uniformly adopted across all US states. For example, Maryland uses a subjective understanding of good faith and dispenses with the objective standard of reasonable parties, see Lisa Sparks, 'The Regression of Good Faith in Maryland Commercial Law' (2016) 47(1) University of Baltimore Law Forum 17, 17-22. More importantly, the doctrine has so far been used to develop issues relating to material breach, rather than serving 'some broader notion of fairness and justice in contracting,' see Emily MS Houh, 'The Doctrine of Good Faith in Contract Law: A (Nearly) Empty Vessel' (2005) Utah Law Review 1, 52.

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