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Articles

'Implicit Good Faith' --

or Do We Still Need an

Implied Term of Good Faith?*

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Implied terms of good faith in relation to express contractual rights and discretions have been the focus of recent litigation in England and Australia. These rights and discretions appear in commercial contracts, where consumer legislation is not relevant and the only possible fetter on the exercise of these rights and discretions would be found in common law or equitable doctrines. From the recent cases, the two likely fetters on rights and discretions are good faith and reasonableness. With those two fetters seem to arise two areas of confusion.

First, there is the problem with the meaning of those terms. Recent Australian cases support the idea that 'good faith' is synonymous with 'reasonableness'[1] or that there are two co-extensive duties, one of good faith and the other of reasonableness. There is no judicial explanation of why good faith and reasonableness should become a restriction on rights (such as termination rights), and thus enter the territory of relief against forfeiture and unconscionability. Some cases even see a merging of equity and common law in the development of the fetter of the implied term of good faith.[2] It is therefore interesting that a different approach is being taken in decisions of the English Court of Appeal, where good faith is aligned with honesty and rationality, and distinguished from reasonable care or objective reasonableness.

The second problem is the method of incorporation of restrictions of good faith or reasonableness. In both England and Australia the approach is to imply a term requiring good faith or reasonable exercise of rights or powers.[3] If, as this paper suggests, good faith is implicit or inherent in the institution of contract law, then an implication of good faith is unnecessary and confusing. If the implication incorporates a higher obligation of objectively reasonable behaviour then a clear explanation would be expected, but has not been forthcoming from the courts. Furthermore, this paper suggests that any fetter on an express right or discretion can instead be achieved by construction, rather than implication of a term.

This paper uses the 2008 decision of the English Court of Appeal in *Socimer International Bank Ltd v Standard Bank Ltd*[4] as the vehicle for discussing these issues. In *Socimer*, the Court of Appeal decided that:

(1) Good faith is implicit in contracts.
(2) The meaning of good faith is honesty which operates to control issues of self-interest.
(3) Generally, discretions will be limited by good faith or honesty.
(4) A restriction on a discretion in the form of good faith or an obligation of reasonableness will be incorporated as an implied term.

Australian cases disagree with all except point 4. This paper agrees with the first three points, but not the fourth! These issues are dealt with below and the positions in England and Australia are compared.

Socimer International Bank Ltd v Standard Bank London Ltd

Socimer concerned a discretion in the context of a positive obligation to value assets. The facts briefly were these. Socimer and Standard were international banks, which had been trading together in emerging markets securities. Standard was the 'seller' and Socimer the 'buyer'. Socimer was failing. It was put into default and owed Standard US$24.5m in what were called 'Unpaid Amounts' in respect of a portfolio of forward sales of securities which it had bought. The 'termination date' was 20 February 1998. Under the agreement the 'Standard Terms for Forward Sale Transactions' the creditor bank, the seller, had to 'liquidate or retain' the buyer's portfolio (the 'Designated Assets') to satisfy the amount that the buyer owed it. The important clause was cl 14(a)(bb), which provided:

> The value of any Designated Assets liquidated or retained and any losses, expenses or costs arising out of the termination or the sale of the Designated Assets shall be determined on the date of termination by Seller.

Standard, the seller, did not in fact carry out a valuation under cl 14(a)(bb). Instead, it sold the parts of the portfolio that it could over months and years and credited the proceeds to the buyer 'in dribs and drabs'.[5]

Meanwhile, a few weeks after the termination date, on 3 March 1998, Socimer went into liquidation. Socimer's liquidator brought proceedings, arguing that Standard ought to have carried out the valuation at the termination date and, had it done so, Socimer would have had a surplus of US$13.8m. The trial judge, Cooke J held that:[6]

> [O]n the proper construction of the Agreement, Standard was obliged to value the Designated Assets as at the date of termination of the Agreement for the purpose of clause 14(a) of the Agreement and to bring into account the value as assessed as a credit against the amounts payable to Standard.

Following Cooke J's decision, the parties were still unable to agree on what the valuation of the portfolio ought to have been, had Standard valued the assets as required. The parties' calculations were over US$14m apart. Valuation issues were then addressed in court before Gloster J. Socimer convinced Gloster J that Standard was bound to take reasonable care in finding the true market value of the portfolio. This approach to the discretion was argued as a matter of contractual implication or as a matter of equity by analogy with the duties of a mortgagee with a power of sale.

Standard appealed to the Court of Appeal. The issue relevant here was whether Standard's valuation obligation was to carry out reasonable, objective valuation or only the honest, but otherwise subjective, valuation which Standard would have carried out if it had been aware of its contractual obligation to value. Rix LJ wrote the primary judgment, with whom Lloyd and Laws LJJ agreed.Lloyd LJ did add a few comments of his own.

Rix LJ spent some time methodically deconstructing the decisions of Cooke J and Gloster J. He further criticised Socimer's senior counsel for failing to plead the implied term argument about the limitation on the discretion, and for asking the court to disbelieve witnesses, whom he failed to cross-examine, merely because their evidence supported an approach different to his client's.[7]

The Court of Appeal held that the discretion to value had to be exercised in good faith, that is, honestly. This overturned the decision of Gloster J below who had required a reasonable valuation of the assets. In the context of this, Rix LJ stated:[8]

> In my judgment, the requirements of good faith and rationality are a sufficient protection. The danger to be guarded against ... is abuse caused by self-interest. That is precisely what implicit good faith deals with. Commercial contracts assume such good faith, which is why express language requiring it is so rare.

What is this idea of 'implicit good faith'?

Implicit Good Faith

Rix LJ is correct that good faith is 'implicit' in contract law. While there might be a suggestion that the word 'implicit'

merely means 'implied' and therefore requires an implied term, that does not do justice to the context of Rix LJ's use of that word. He speaks of 'assumed good faith', which is more consistent with the idea that his meaning of 'implicit' was 'naturally or necessarily involved in, or capable of being inferred from, something else'.[9] Thus, Rix LJ was referring to a concept of inherent good faith or honesty, which is the default standard of behaviour for contracting parties. Legal concepts that are applicable to all contracts are not achieved by implied terms, but rather through construction, as is discussed below.

Good faith can be seen in two facets of contract law. First, and on a very general level, every aspect of contract law is, or should be, consistent with good faith because good faith is the essence of contract. Second, good faith is seen in construction of contract and in defining the 'default standard' of behaviour required, which is where the implied term of good faith is said to operate.That 'default standard' of good faith should be seen as requiring honest adherence to the bargain.

Recent Australian cases unfortunately fail to acknowledge the good faith element of contract rules, the first aspect.[10] Elsewhere, Professor Carter and I have provided illustrations of how we see that contract law is underpinned with good faith.[11] We have pointed out that it is possible to find the operation of 'implicit' good faith in all aspects of contract law. A very quick summary of how good faith plays a role in various aspects of contract law follows:

- Formation: Good faith often requires communication.This is seen in the law's requirement that revocation of offers be communicated, despite the position that offers create no legal obligations and offers can be revoked at any time prior to acceptance.
- Implied terms: An explanation of the development of terms implied in law is that such terms are implied to ensure the parties behave in a manner consistent with good faith, where they have not provided for a particular issue themselves. Terms implied in law set a default standard that is consistent with good faith expectations of the parties' behaviour.
- Incorporation of terms: Where incorporation is by notice, the notice must be 'reasonable' in the circumstances, or require the party intending to rely on the notice to have made an appropriate (or good faith) attempt at bringing those terms to the attention of the other.
- Frustration: The default rule is not that parties are obliged to perform 'no matter what', but rather that they will be held -- in good faith -- to the obligations they agreed to, but not in situations where the obligations have become'radically different' because of some external and unforeseen event.[12]
- Mitigation: While not a positive 'rule', the principle behind mitigation is that a party in breach should not be liable for losses incurred because of the 'unreasonable' behaviour of the other party in failing to avoid that loss. The innocent party need not act in the best interests of the breaching party and, providing the innocent party has acted in good faith, then even if the loss is increased, the party in breach will be liable for that loss.

To this list can be added that good faith will also be seen in construction of contracts. Principles of what is known as 'commercial construction' ensure that effect is given to the intentions of the parties, and generally ensures that good faith considerations are given effect. This leads to the issue of the implied term of good faith.

In most Australian cases an implied term of good faith and reasonableness has been implied as an 'extra'. If good faith is implicit or inherent, then generally there would be no need for any good faith term to be implied. This may seem like a purely academic disagreement with methodology. Yet if courts take the view that good faith must be incorporated by an implied term, it provides some explanation as to why 'good faith' has been given a content more onerous than appropriate or necessary, and is arguably inconsistent with the modern operation of contract law.[13] If it is accepted that good faith is implicit, and will operate at the stage of construction of contracts to set a default standard of honesty, then it is not immediately obvious why good faith should *also* be incorporated as an implied term. Such implication only seems to be occurring where courts have decided that a discretion or termination right should not be allowed to be exercised without some control and where there is no acknowledgement of the implicit or inherent operation of good faith. These issues are now considered.

Implied Fetters on Discretions and Powers and the Meaning of 'Good Faith'

In *Socimer*, Rix LJ considered the existing English authority on the issue of the limitations that are placed on a party's contractual discretion to make decisions, including *Abu Dhabi National Tanker Co v Product Star Shipping Ltd (The Product Star) (No 2)*,[14] *Ludgate Insurance Co Ltd v Citibank NA*,[15] *Gan Insurance Co Ltd v Tai Ping Insurance Co Ltd (No 3)*[16] and *Paragon Finance plc v Nash*.[17] He concluded:[18]

> It is plain from these authorities that a decision maker's discretion will be limited, as a matter of necessary implication, by concepts of honesty, good faith, and genuineness, and the need for the absence of arbitrariness, capriciousness, perversity and irrationality.The concern is that the discretion should not be abused. Reasonableness and unreasonableness are also concepts deployed in this context, but only in a sense analogous to *Wednesbury* unreasonableness, not in the sense in which that expression is used when speaking of the duty to take reasonable care, or when otherwise deploying entirely objective criteria.

Rix LJ was critical of the approach taken by the first instance judge, Gloster J. She had concluded that 'Standard was obliged to act honestly and reasonably and to arrive at a value which properly reflected the actual value of the Designated Assets as at the termination date'.[19] She went on: [20]

> I do not view the obligation to act reasonably as anything in essence different from the obligation to use good faith: it is part of the good faith obligation that Standard should conduct the valuation process in a reasonable manner, to arrive at what objectively can be said to [be] a proper value of the Designated Assets at the termination date ...

This approach is very similar to that taken in Australian courts when dealing with implied terms of good faith, where generally no distinction is drawn between good faith and reasonableness.[21] By comparison, Rix LJ stated that the reference to objective standards 'plainly' go beyond concepts of good faith and rationality.[22]

Gloster J suggested during argument in court that there was perhaps a comparison to be made between Standard's obligation to value and a mortgagee's powers of sale, where in England, reasonable care must be exercised. Socimer's lawyers took up this suggestion and argued that Standard's discretion to value the assets was in a similar situation. This was rejected by the Court of Appeal on the basis that the analogy was not appropriate. Lloyd LJ concentrated on this point alone in his speech, in which he otherwise agreed with Rix LJ.[23] His view was that mortgagees have powers and obligations imposed by the law of mortgages. He compared a situation *not* involving a mortgage, where it is only possible to incorporate similar type obligations if the tests for implication of terms are satisfied. He was not convinced that the tests could be satisfied in the case and therefore agreed with Rix LJ. He states:[24]

> It seems to me ... that [Gloster J] was led by that similarity into drawing, and applying, an analogy with mortgage law, while overlooking, on the one hand, the need to justify the implication on the basis of conventional contract law and, on the other hand the fact that, in relation to a mortgage, the duties by reference to which she drew the analogy do not derive, and cannot be derived, from such a process of implication, but are imposed as a matter of general law, which does not apply in the present case because the transaction is not a mortgage.

This position can be contrasted with that in Australia, where it is well established that good faith has a role to play where a mortgagee has a power of sale. However, the meaning of 'good faith' in that context is not settled,[25] yet it does not require reasonable behaviour. Thus, in Australia while a mortgagee is not required to act reasonably when dealing with another's property, an innocent party will be required to exercise express rights to terminate reasonably, as evidenced by the decision in *Renard Constructions (ME) Pty Ltd v Minister for Public Works*,[26] which will be considered below.The opposite is the position in England, as evidenced by *Socimer*.

Finally, the method of incorporation of restrictions of good faith should be considered. Currently, the approach being taken in England and Australia is to imply a term when 'good faith performance' is required.

Implied Terms of Good Faith

Given that good faith as a concept or requirement underlies contract law and the recent statement of Rix LJ about 'implicit good faith' setting a default standard of honesty and rationality, it must be asked whether we need an implied term of good faith? Yet *Socimer* and *Renard* both proceeded on the basis of incorporating good faith with an implied term.[27] Courts (especially in New South Wales) seem to prefer the idea that the term requiring good faith and reasonableness should be regarded as one implied in law.[28] In England, while the meaning attributed to 'good faith' is the more defensible one of 'honesty', there is a preference for using a term implied in fact, as evidenced by *Socimer*.[29]

This paper argues that the 'implied term approach' is wrong. As good faith is already implicit in contract rules and construction principles, if a court implies a term of good faith the court is either implying a redundant term or implying a term which imposes a more onerous obligation. In some cases it *might* be appropriate to incorporate a requirement of a higher standard of behaviour than the law otherwise requires, but such a term must either be incorporated as a matter of construction or satisfy the rules for implication, which would be possible, but unusual. In relation to the cases which suggest that a term of good faith is implied in law, the problems are that:

(1) terms implied in law create default rules, and as good faith is already the default position, this adds nothing more; and
(2) terms implied in law are incorporated as default rules for contracts dealing with particular relationships, rather than all contracts, and therefore the implied term approach cannot be appropriate to incorporate good faith into every contract.[30]

Furthermore, using an implied term approach seems a 'backwards' step. A comparison can be made with other aspects of law that developed from an implied term approach, but moved away from that approach when it was acknowledged that such an approach was 'fictitious'.Anticipatory repudiation and frustration are examples. Courts should feel confident enough to recognise implicit good faith, without recourse to implied terms.

The problem of this approach is tied up with the meaning that is being given to 'good faith'. If courts are implying a term of 'good faith' which requires objectively reasonable behaviour, as did Gloster J in *Socimer* and as many Australian cases appear to do, then the courts are actually using good faith as a rationale for a specific implication that a party act reasonably when exercising an express right of termination or discretion to value. Of course, that specific implication would be difficult to reconcile with authority,[31] and the attraction of the language of 'good faith' is that it enables a judge to reach a result that authority would not otherwise permit.

In *Socimer,* the argument in favour of an implied term fettering the exercise of the discretion was that while Standard could be trusted to act in its own interest to get the best price when selling designated assets, this was not necessarily the case when valuing a retained asset. In that situation, Standard's interest was in conflict with the interests of the buyer, Socimer, because it would want to assign as low a value as possible so as to maximise potential profit on a later sale.[32] Gloster J held there should be an implied term that 'imposes on Standard a duty, in doing its valuation, to take reasonable precautions to value the Designated Assets at "the fair" or "the true market" or "proper" value'.[33]

While Rix LJ disagreed and held that the fetter was merely to behave honestly, it is interesting that he agreed that the fetter ought to be incorporated by implication of a term.[34] He highlighted the 'useful and authoritative modern restatement of the relevant principles upon which terms may be implied'[35] of *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd*,[36] which relied upon *BP Refinery (Westernport) Pty Ltd v Shire of Hastings*,[37] and the 'five point test',[38] which has been repeated in High Court decisions many times and is, in relation to contracts complete on their face, the standard authority for implication in fact in Australia.

Rix LJ states:[39]

> The courts' usual role in contractual interpretation is, by resolving ambiguities or reconciling apparent inconsistencies, to attribute the true meaning to the language in which the parties themselves have expressed their contract. The implication of contract terms involves a different and altogether more ambitious undertaking: the interpolation of terms to deal with matters for which, ex hypothesi, the parties themselves have made no provision. It is because the implication of terms is potentially so intrusive that the

> law imposes strict constraints on the exercise of this extraordinary power.

In relation to the implication of fetters on discretion he adds:[40]

> Implications of good faith and rationality, and lack of arbitrariness or perversity, are standard, for they represent the very essence of business (and other) relationships. Once one goes beyond them, however, the matter becomes much more uncertain.
>
> In my judgment, the requirements of good faith and rationality are a sufficient protection. The danger to be guarded against ... is abuse caused by self-interest.That is precisely what implicit good faith deals with. Commercial contracts assume such good faith, which is why express language requiring it is so rare.[41]

Having stated the law this way, it is not clear why then Rix LJ felt that the fetter on the exercise of the discretion needed to be achieved by an implied term. He had concluded that express terms requiring good faith were usually unnecessary in commercial contracts and that strict constraints are placed on courts wishing to imply terms. Furthermore, he applied the test of whether it was 'necessary' to imply a term requiring reasonable behaviour, and decided that the test could not be satisfied, as the term was not necessary. In his view, it ran against 'the vein of the agreement as a whole, which plainly gave the determination of value to Standard, in the exercise of its subjective judgment and subject to a wide discretion'.[42] Nevertheless, he decided that a term could be implied in fact that the discretion be exercised in good faith, that is requiring rationality etc, but without going through the same application of the test for implication in fact.

Might it not have been possible to conclude that as the 'vein of the agreement' only required good faith? That is, might it be said that Socimer's obligation to exercise the discretion to value in good faith was achieved through construction? Would that not have been, in Rix LJ's language, attributing 'the true meaning to the language in which the parties themselves have expressed their contract'?

With that in mind, what is the state of the law in Australia? In Australia, since the decision of *Renard* in 1992, there has been judicial support for the idea that rights of termination ought to be fettered with an implied term requiring good faith and reasonableness. The method of incorporation of the fetter is the same as that used in England, namely an implied term, yet the fetter is generally a more onerous obligation of objective reasonableness, rather than subjective honesty.

Construction

In contrast to the decision in *Socimer*, is the NSW Court of Appeal decision in *Renard*, which has led to numerous decisions implying terms of good faith and reasonableness. In *Renard* the ability of the principal under a building contract to rely on a show cause procedure was subjected by the NSW Court of Appeal to requirements of reasonableness. Priestley JA said:[43]

> The contract can in my opinion only be effective as a workable business document under which the promises of each party to the other may be fulfilled, if the subclause is read in the way I have indicated, that is, as subject to requirements of reasonableness.

This requirement of reasonableness now seems to be regarded as a main ingredient of good faith in Australian cases.[44]

Implicit good faith has already been recognised by the Australian High Court for some time, but perhaps forgotten. In 1953 in *Carr v J A Berriman Pty Ltd*,[45] the High Court resorted to construction and implicit good faith, without expressly referring to them, to resolve a dispute about the operation of a contractual discretion. The relevant clause entitled an architect to use his 'absolute discretion' to omit work from a building. The principal argued that this clause entitled it to omit steel fabrication work from the contract for the purpose of having the work done by a third party (presumably more cheaply). Fullagar J acknowledged that such a clause was common and had an obvious purpose of enabling the architect to manage the construction of the building as appropriate. However, he stated:[46]

> But [the words] do not, in my opinion, authorise him to say that particular items so included shall be carried out not by the builder with whom the contract is made but by some other builder or contractor. The words used do not, in their natural meaning, extend so far, and a power in the architect to hand over at will any part of the contract to another contractor would be a most unreasonable power, which very clear words would be required to confer.

Two points might be made from Fullagar J's judgment in *Carr v Berriman*. First, he was adopting what might be called a 'good faith interpretation', which was enough to determine whether the principal or architect was entitled to act in the way it had acted on the particular facts.

Second, in *Carr v Berriman* there was no recourse to implied terms to reach the result. The same might have been true in *Socimer*. However, the current approach taken in Australia and England appears to be a preference to incorporate good faith through an implied term. The difference between the approaches on either side of the globe is that the term being implied in England only requires honesty, and not reasonableness.

While the result in *Renard* is not problematic, the subsequent cases in which it has been applied have led Australian contract law into a peculiar situation. Commercial parties are now faced with the question of whether they dare to suggest in negotiations that they are not prepared to perform 'in good faith' as that may require reasonableness on their part. Alternatively, should they expressly state that they will not behave reasonably, or will that be a 'deal-breaker'?Arguably this was not an issue before *Renard*, as in the words of Rix LJ, 'commercial contracts assume good faith'.It is only now with the uncertainty that has arisen from *Renard* that contracting parties are left with the additional negotiation and drafting problem and possibly litigation.

It might be noted that there are two recent first instance decisions in New South Wales that question the validity of implying a term of good faith into contracts. In *Hunter Valley Skydiving Centre Pty Ltd v Central Coast Aero Club Ltd*47 Brereton J stated that 'the implication of a term that a contractual right will be exercised only in good faith does not fit neatly into the structure of Australian contract law'.[48] In *Agricultural & Rural Finance Pty Ltd v Atkinson*,[49] Young CJ in Eq expressed the view that there had only been a 'flirting' by courts with the idea of implying terms of good faith, an idea which he rejected in the case before him. So, while such decisions provide some hope, they are far outweighed by the number of decisions that take the '*Renard* approach'.

Conclusion

If the courts accepted that implicit good faith underlies contract law and is seen in principles of construction requiring honest adherence to the bargain, then the discretions or powers could be construed as requiring an exercise of good faith, which would be given meaning in the particular context. The standard of behaviour required by good faith would only be honesty, loyalty to the contract and, perhaps, a requirement to consider the interests of the other party. This would place contractual exercise of discretions in the same position as the general exercise of powers: they must be exercised for a 'proper purpose', within the context of the contract. This would remove the artificial reasoning concerning implied terms. [50] This approach uses construction of the contract and the particular power or discretion to determine the appropriate meaning, without drawing on implied terms and concepts of objective reasonableness. This furthers the argument that an implied obligation of good faith and reasonableness is unnecessary. Implicit good faith is enough.

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1 See *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234 and cases following that decision, such as *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15; *J K Keir Pty Ltd v Priority Management Systems Pty Ltd* [2007] NSWSC 789 per Rein AJ at [27]; *Mangrove Mountain Quarries Pty Ltd v Barlow* [2007]NSWSC 492 at [27] per Windeyer J. In *Nauru Phosphate Royalties Trust (Receivers and Managers appointed) & Business Australia Capital Mortgage Pty Ltd v Nauru Phosphate*

Royalties Trust [2008]NSWSC 916 at [43], where Einstein J states 'The effect of the Court of Appeal ... in *Burger King* [was to] ... collapse any distinction between contractual obligations of good faith and obligations of reasonableness ... '.

2 See eg *Harbourside Catering Pty Ltd v TMG Developments Pty Ltd* [2007] NSWSC 1375 at [52], where Palmer J states that the equitable principle controlling the exercise of contractual rights under the 'rubric' of unconscionable conduct has been 're-labelled' the duty to act in good faith; *Vodafone Pacific Ltd v Mobile Innovations Ltd* where Giles JA states: 'depending on how the content of the obligation of good faith becomes settled, if it does, contract may take over from equitable principle': [2004] NSWCA 15 at [217]. See also Elisabeth Peden, 'When Common Law Trumps Equity: the Rise of Good Faith and Reasonableness and the Demise of Unconscionability' (2005) 21 *JCL* 226.

3 See eg Elisabeth Peden, *Good Faith in the Performance of Contracts*, LexisNexis Butterworths, Sydney, 2003, Ch 6.

4 [2008] 1 Lloyd's Rep 558.

5 [2008] 1 Lloyd's Rep 558 at 560 per Rix LJ.

6 [2004] EWHC 1041 (Comm), quoted at [2008]1 Lloyd's Rep 558 at 560 per Rix LJ.

7 [2008] 1 Lloyd's Rep 558 at 582.

8 [2008] 1 Lloyd's Rep 558 at 588. Finn J has also expressed the view that there is an implied universal duty of good faith. For example, in *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151 at 192-3 he stated ' ... I consider a virtue of the implied duty to be that it expresses in a generalisation of universal application, the standard of conduct to which all contracting parties are to be expected to adhere throughout the lives of their contracts'.Finn J's method of incorporation of this 'universal duty' is as an implied term. See also *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL* [2005] VSCA 228 at [4]per Warren CJ.

9 *Oxford English Dictionary*, 2nd ed, OUP, Oxford, 1989.

10 For example, in *Insight Oceania Pty Ltd v Philips Electronics Australia Ltd* [2008] NSWSC 710, at [168]ff Bergin J's reasoning appears to be that 'implicit' good faith would not always accord with the parties' intentions and for that reason a term of good faith should be implied when necessary, as a term implied in fact. However, her Honour also states that 'good faith seems to me to subsume the obligation to act honestly' at [178]. With respect, if good faith merely requires honesty -- which seems correct -- then her Honour is at cross-purposes.The obligation to behave honestly cannot be excluded, just as fraud cannot be excused by agreement. An implied term is then *only* necessary if it imposes more than honesty and extends to reasonableness, which would rarely correspond with commercial parties' intentions, as Rix LJ correctly states.

11 J W Carter and Elisabeth Peden, 'Good Faith in the Australian Contract Law' (2003) 19 *JCL* 155;'A Good Faith Perspective on Liquidated Damages' (2007) 23 *JCL* 157.

12 See *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696 at 728-9. At 728 Lord Radcliffe stated: 'By this time it might seem that the parties themselves have become so far disembodied spirits that their actual persons should be allowed to rest in peace. In their place there rises the figure of the fair and reasonable man. And the spokesman of the fair and reasonable man, who represents after all no more than the anthropomorphic conception of justice, is and must be the court itself'.

13 See eg *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 186 ALR 289 at 311-12 per Kirby J.

14 [1993] 1 Lloyd's Rep 397.

15 [1998] Lloyd's Rep IR 221.

16 [2002] Lloyd's Rep IR 612.

17 [2002] 1 WLR 685.

18 [2008] 1 Lloyd's Rep 558 at 577.

19 See [2008] 1 Lloyd's Rep 558 at 578.

20 See [2008] 1 Lloyd's Rep 558 at 578.

21 See cases cited at n 1.

22 [2008] 1 Lloyd's Rep 558 at 578.

23 [2008] 1 Lloyd's Rep 558 at 594.

24 [2008] 1 Lloyds' Rep 558 at 594.

25 See eg *National Australia Bank Ltd v Sproule* (1989) 17 NSWLR 505 at 510; *Service Station Association Ltd v Berg Bennett& Associates Pty Ltd* (1993) 45 FCR 84; 117 ALR 393 at 401 per Gummow J.

26 (1992) 26 NSWLR 234. ('*Renard*').

27 See Elisabeth Peden, 'Incorporating Terms of Good Faith in Contract Law in Australia' (2001) 23 *Syd LR* 222; Elisabeth Peden, *Good Faith in the Performance of Contracts*, LexisNexis Butterworths, Sydney, 2003, paras 6.10-6.19.

28 See NSW Court of Appeal decisions, such as *Burger King v Hungry Jack's Pty Ltd* [2001] NSWCA 187 at [164]; *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349 at 369 per Sheller JA (with whom Powell and Beazley JJA agreed). Cf *Renard* (1992) 26 NSWLR 234 at 263 (where Priestley JA seemed to conceive of a 'hybrid' term); *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15. In *CGU Workers Compensation (NSW) Ltd (ACN 003 181 002) v Garcia* [2007] NSWCA 193 at [131]-[136] in the context of insurance, the NSW Court of Appeal did state that the law has not yet gone so far as to imply a term requiring good faith performance into all contracts, but did leave open that possibility. The court did not clarify the issue of the meaning of good faith and whether it includes reasonableness. First instance judges take differing approaches.For example, Einstein J prefers a term implied in law: see eg *PRP Diagnostic Imaging Pty Ltd v Pittwater Radiology Pty Ltd* [2008]NSWSC 701 at [99]-[104]. Compare Bergin J in *Insight Oceania Pty Ltd v Philips Electronics Australia Ltd* [2008] NSWSC 710 at [177] who preferred a term implied in fact.

29 [2008] 1 Lloyd's Rep 558.

30 See generally E Peden, *Good Faith in the Performance of Contracts*, LexisNexis Butterworths, Sydney, 2003, Ch 6.

31 See eg *Tanwar Enterprises Pty Ltd v Cauchi* (2003) 217 CLR 315; 201 ALR 399, where exercise of a right of termination for breach of an essential time clause was upheld as there was no unconscientious behaviour (and reasonableness was not considered); *Meehan v Jones* (1982) 149 CLR 571, where the High Court did not require reasonable behaviour of a purchaser given a discretion to find satisfactory finance; *White and Carter (Councils) Ltd v McGregor* [1962]AC 413, where the House of Lords did not require an innocent party to behave reasonably in deciding whether to exercise a common law right to terminate.

32 [2008] 1 Lloyd's Rep 558 at 583.

33 See [2008] 1 Lloyd's Rep 558 at 578-9.

34 Rix LJ points out ([2008] 1 Lloyd's Rep 558 at 587) that the implied terms contended for by the parties were different.

35 [2008] 1 Lloyd's Rep 558 at 585.

36 [1995] EMLR 472.

37 (1977) 180 CLR 266; 16 ALR 363.

38 See (1977) 180 CLR 266 at 283. '[F]or 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 it goes without saying; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract.'

39 [2008] 1 Lloyd's Rep 558 at 585.

40 [2008] 1 Lloyd's Rep 558 at 586.

41 [2008] 1 Lloyd's Rep 558 at 588.

42 [2008] 1 Lloyd's Rep 558 at 583.

43 (1992) 26 NSWLR 234 at 258.

44 See eg *Burger King Corp v Hungry Jack's Pty Ltd* [2001] NSWCA 187, reported in part (2001) 69 NSWLR 558 and cases following. See however *Hunter Valley Skydiving Centre Pty Ltd v Central Coast Aero Club Ltd* [2008] NSWSC 539 at [48].

45 (1953) 89 CLR 327.

46 (1953) 89 CLR 327 at 347. The other members of the High Court agreed.

47 [2008] NSWSC 539.

48 [2008] NSWSC 539 at [48].

49 [2006] NSWSC 202, reversed on other grounds: *Gardiner v Agricultural & Rural Finance Pty Ltd* [2007] NSWCA 235.

50 See eg the statement by Barwick CJ in *Pierce Bell Sales Pty Ltd v Fraser* (1973) 130 CLR 575 at 587. McTiernan J agreed, as did Gibbs J, adding some extra comments. This has been adopted by courts including the NSW Court of Appeal in *Alcatel Aust Ltd v Scarcella* (1998) 44 NSWLR 349 at 368 and *Vodafone* [2004]NSWCA 15, yet without a clarification of the modern idea of 'good faith' and reasonableness.

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