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THE ROLE OF GOOD FAITH IN COMMERCIAL CONTRACTS

CONTRACT DISPUTES PRACTICAL GUIDES
ISSUE 4: NOVEMBER 2019

This is the fourth in our series of contract disputes practical guides, designed to provide clients with practical guidance on some key issues that feature in disputes relating to commercial contracts under English law.

The traditional starting point in English contract law is that parties are free to do what they like so long as they do not breach the agreed terms.

But it is becoming increasingly common for parties to agree terms requiring them to act in "good faith", or similar. Even where no such term is expressed in the contract, courts and tribunals are increasingly being asked to imply good faith obligations.

As a result, commercial parties may be uncertain what is required of them.



Chris Parker, **Rachel Lidgate** and **Alex Kay** consider the circumstances in which parties may owe one another duties of good faith, what those duties may involve, and some practical steps that can be taken to minimise the risks.

Top tips to navigate good faith obligations:

- If there is an express obligation of good faith, DON'T ignore it – you will need to consider carefully what it requires
- DON'T assume that because the contract doesn't mention good faith, you're under no such obligation
- Since a good faith obligation may be implied, DO consider whether it is preferable to address the matter expressly
- If you agree a good faith obligation, DO consider specifying the actions that are (and are not) required to satisfy it
- DO consider excluding any obligation of good faith save as specifically set out in the agreement
- If you want an enforceable obligation to negotiate, DO include time limits / objective criteria
- DO remember good faith may be relevant if negotiating contracts in an international context

1. General principles

English law does not impose a general duty of good faith on contracting parties either in negotiating or in performing the contract. This is in contrast to many other legal systems. An obligation of good faith is recognised in most civil law jurisdictions (such as France and Germany) and in a number of other common law jurisdictions including the US, Canada and Australia.

Obligations of good faith can, however, come into play under English law in various circumstances. English law does imply obligations of good faith as a matter of course in certain types of contract, because of the nature of the relationship.

Some obvious examples are contracts of agency, partnership and employment. These are not considered further in this guide.

Concepts of good faith may also be introduced by statute. A good example is section 62 of the Consumer Rights Act 2015, which defines a term in a consumer contract as unfair if, "contrary to the requirement of good faith", it causes a significant imbalance in the parties' rights and obligations to the detriment of the consumer.

Parties may include express obligations of good faith in their contracts, which the courts will then have to interpret – see section 4 below. Or in some circumstances the courts may imply obligations of good faith into commercial contracts, applying ordinary principles governing the implication of contractual terms – see sections 5-7 below.

Particular considerations arise in the context of express obligations to negotiate in good faith – see section 8 below.

2. No general duty

As noted above, there is no generally applicable duty of good faith in English contract law. This long-standing principle was revisited by the High Court in a much-discussed decision in 2013, *Yam Seng Pte Ltd v International Trade Corp Ltd* [2013] EWHC 111 (QB) (see this post on our Litigation Notes blog).

The judge referred to a number of reasons for the "traditional English hostility" towards a doctrine of good faith: the tendency for English law to develop particular solutions in response to particular problems rather than enforcing broad overarching principles; the view that parties should be free to act as they wish so long as they do not act in breach of contract; and the concern that recognising a general requirement of good faith would create uncertainty.

"The starting point in English contract law is that parties are free to pursue their own self-interests, so long as they do not act in breach of contract. But that is not always the end point, so caution is needed."

He expressed the view that the resistance to a generally applicable duty of good faith is "misplaced" and that English law is "swimming against the tide" in this regard. However, he doubted that English law was ready to recognise a requirement of good faith implied by law into all commercial contracts, even as a default rule.

Instead he suggested that good faith obligations may be implied into commercial contracts based on the presumed intention of the parties. This is considered in section 5 below.

3. Meaning of good faith?

Because there is no universally accepted definition of good faith under English law, there is scope for argument about what an obligation of good faith actually involves, absent a clear contractual definition.

In general, a duty of good faith, whether express or implied, will not require a party entirely to subvert its own commercial interests to those of the counterparty, or to give up its express contractual rights. Beyond that, however, the content of the duty varies, depending on the particular contract and the surrounding context.

It is often said that the core of the duty of good faith is honesty. But as the judge in *Yam Seng* commented, even the core value of honesty is sensitive to context. It is invariably dishonest to deceive another person, with the intention that they rely on the false statement, but sometimes the requirements of honesty go further than that.

Depending on context, the judge noted, it may be dishonest to fail to correct a statement that is discovered to be false, or to be deliberately evasive. A duty of honesty may even extend, he said, to an expectation that the parties will share relevant information, so that a deliberate omission to do so may amount to bad faith, particularly in a long-term, "relational" contract (see section 6 below). The judge rejected as "too simplistic" the traditional dichotomy between fiduciary relationships, which involve duties of disclosure, and other contractual relationships in which no such duty is supposed to operate.

The duty of good faith is often said to include other generally accepted standards of commercial dealing – ie avoiding conduct which might be described as "improper", "commercially unacceptable" or "unconscionable", even if it is not actually dishonest. This has been referred to as a requirement of fair dealing, or integrity, or similar.

The other main aspect that is often cited is fidelity to the parties' bargain, or the agreed common purpose, or the justified expectations of the parties.

These concepts are not easy to pin down, particularly around the edges, and there is clearly scope to debate whether a particular duty of good faith includes one or more of them. As a result, even where a duty of good faith is established, whether particular conduct is or is not in breach of that duty is typically a hotly disputed question.

The upshot is that the meaning of good faith can best be explored by reference to particular cases, including those discussed in this guide.

"The term 'good faith' is often referred to, but less often defined. It can be difficult to know exactly what is meant by the term in any given situation."


Honesty
Commercial dealing
GOOD FAITH
Fair dealing
Fidelity to bargain
Integrity

4. Express obligations

A contract may, of course, include an express term requiring one or more parties to act in good faith, either generally in performing the agreement or in relation to particular matters.

Where an express term has been included, the court will need to interpret it to determine the scope and content of the obligation. The usual principles of contractual interpretation apply (see issue 2 of this series of contract disputes practical guides). The court's aim is to determine the meaning the contract would convey to a reasonable person with all the background knowledge available to the parties at the time the contract was made. As well as the words used and the relevant background, the court will take into account how the clause fits within the contract as a whole and considerations of commercial common sense.

The general trend in the case law seems to be in favour of giving a narrow interpretation to express contractual obligations of good faith. In addition, where a contract contains express obligations of good faith, the courts will tend to hesitate before implying further such obligations.

Where an express obligation of good faith is included in a contract, it is advisable to clarify both the scope and, if possible, the content of that obligation rather than leaving it for the courts to determine.

"Parties should think carefully before including a general, and potentially open-ended, obligation of good faith in their contracts. Parties may wish to consider additional terms defining the nature and extent of the obligation."

In *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200, an express obligation of good faith in a contract to provide hospital catering and cleaning services over a seven year period provided that the parties:

> "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 ... to derive the full benefit of the Contract."

The Court of Appeal held that the obligation to co-operate in good faith was not a general one, but was specifically focused on the two purposes identified.

The good faith obligation did not, therefore, apply to the Trust's powers to make deductions from monthly payments and award "service failure points" where the contractor failed to meet detailed service specifications. These powers were irrelevant to the two purposes identified in the clause.

The Trust's excessive deductions did not therefore constitute a breach of the clause.

The Court of Appeal also commented that, where a contract makes specific provision for particular eventualities, care must be taken not to construe a general and potentially open-ended obligation to "co-operate" or "act in good faith" as covering the same ground, which risks cutting across those more specific provisions and any limitations in them.

In *TSG Building Services PLC v South Anglia Housing Limited* [2013] EWHC 1151 (TCC) (see this post on our Litigation Notes blog) TSG contracted to provide a gas servicing and associated works programme to the housing stock of SAHL. The contract provided:

> "The Partnering Team members shall work together and individually in the spirit of trust, fairness and mutual co-operation for the benefit of the Term Programme, within the scope of their agreed roles, expertise and responsibilities ... and in all matters governed by the Partnering Contract they shall act reasonably and without delay."

A separate clause gave SAHL the right to terminate for convenience. A little over a year into the contract term, SAHL served a termination notice on TSG, without any explanation as to why it wished to terminate.

The court held that the obligations to co-operate and act reasonably related only to the provision of gas-related works. The parties had expressly limited the scope of these obligations to their "roles, expertise and responsibilities", so they did not apply to the right to terminate.

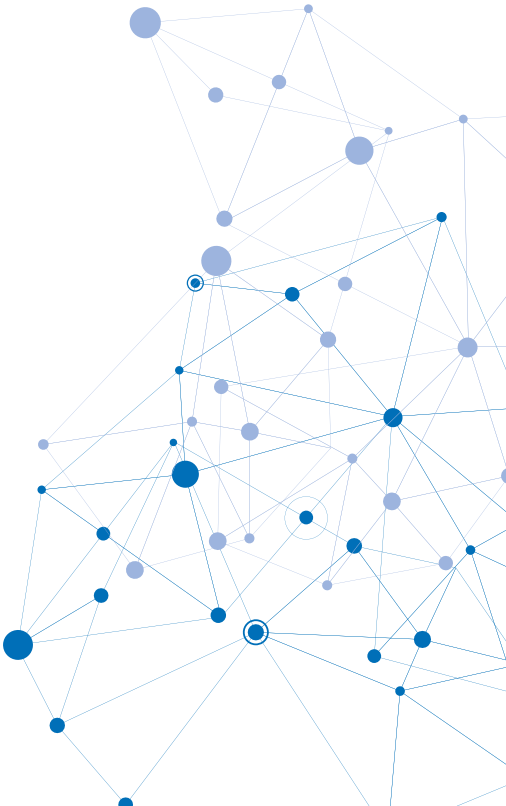
The court also refused to imply a term to this effect. The parties had already gone as far as they wanted in expressing terms about how they were to work together. Even if there was some implied term of good faith, it could not circumscribe what the parties had expressly agreed, which was a right to terminate at any time for no, good or bad reason.

BP Gas Marketing Ltd v La Societe Sonatrach [2016] EWHC 2461 (Comm) concerned a dispute over the allocation of costs under a contract jointly to import cargoes of liquefied natural gas. The contract contained an express term requiring the parties to perform their contractual obligations in good faith. The claimant (BP) sought to recover certain nitrogen costs from the defendant (Sonatrach), and Sonatrach alleged (among other things) that BP was in breach of its obligation of good faith in failing to agree an amendment to the contractual formula for calculating those costs.

The High Court rejected Sonatrach's argument. The contract only imposed an obligation on a party to act in good faith when performing its contractual obligations. There was no free-standing obligation of good faith. Sonatrach alleged that BP was contractually obliged to consider any proposed amendment raised before the Steering Committee, but there was no such obligation.

Further, to establish a breach of the good faith obligation, Sonatrach would have to establish not only that BP had to consider such an amendment, but that it had to agree an amendment even if it was contrary to BP's existing contractual entitlement. As the judge noted, good faith does not normally require a party to surrender contractual rights. Here, the judge held, far clearer words would have been needed for the parties to have contracted out of their right at common law to accept or reject any proposed amendment to a contract.

"A good faith obligation will only go so far. Ordinarily, at least, it will not mean a party having to give up its express rights under the contract."



5. Implied obligations

In *Yam Seng* (referred to above), the High Court took what was arguably a novel approach in implying a duty of good faith into an ordinary commercial contract, applying normal principles governing contractual interpretation and the implication of terms.

The judge referred to the two traditional criteria for implying a term into a contract, namely whether the term is: (i) so obvious that it goes without saying; or (ii) necessary to give business efficacy to the contract. He also referred to the Privy Council decision in *Attorney General for Belize v Belize Telecom Ltd* [2009] UKPC 10 which was, at that time, generally seen as the leading modern authority on implied terms – though its authority has since been doubted, and the traditional approach reaffirmed, by the Supreme Court in *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Limited* [2015] UKSC 72 (see issue 2 of this series of contract disputes practical guides).

In *Belize Telecom*, Lord Hoffmann said that the two traditional tests for implication of terms could be analysed as part of the exercise of construction of the contract: what would the contract, read as a whole against the relevant background, reasonably be understood to mean? In *Yam Seng*, the judge pointed out that the relevant background includes not only matters of fact known to the parties but also "shared values and norms of behaviour", which (he said) are taken for granted by the parties when making any contract without being spelt out in the agreement itself.

He then identified two overlapping "shared values and norms of behaviour" which informed interpretation of the contract:

- An expectation of honesty and the observance of other generally accepted standards of commercial dealing, ie avoiding conduct which might be described as (for example) "improper", "commercially unacceptable" or "unconscionable".
- Fidelity to the parties' bargain, so that the contract must be given a reasonable construction which promotes the values and purposes expressed or implicit in it.

As noted above, since the decision in *Yam Seng*, the Supreme Court in *M&S* has emphasised that *Belize Telecom* should not be taken as having watered down the traditional, highly restrictive approach to the implication of terms. It is clear from the *M&S* decision that a term can only be implied if a reasonable reader would consider it so obvious as to go without saying, or necessary for business efficacy.

Where does that leave the approach in *Yam Seng*? Although the judge's analysis starts from the (arguably) broader *Belize Telecom* approach of the reasonable reader, the judge stated that the same conclusion also follows if the traditional tests for the implication of a term are used. And the courts have followed *Yam Seng* to find implied duties of good faith in cases since the *M&S* decision, including in *Bates v Post Office Ltd* (see section 6 below).

There appears to be a consensus, however, that *Yam Seng* was not seeking to establish the general proposition that a duty of good faith should be implied into all commercial contracts, as opposed to certain types of contract – in particular "relational" contracts (see section 6 below). In *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200, for example, the Court of Appeal noted that there is no general doctrine of good faith in English contract law, citing *Yam Seng* for its discussion of good faith duties that are implied into certain categories of contract.

"The lack of any express duty of good faith does not necessarily mean good faith is irrelevant: the court may imply such a duty in some cases."

In *Yam Seng* (referred to above), ITC granted Yam Seng the exclusive rights to distribute certain fragrances in specified territories for approximately one year (later extended for a further eight months). After some 14 months, Yam Seng informed ITC it was terminating the agreement on the basis of ITC's alleged breaches.

The High Court (Leggatt J) held that ITC was in repudiatory breach of an express term, so Yam Seng was entitled to terminate. However, he went on to consider whether a duty of good faith should be implied. Interpreting the contract against the relevant background, including the "shared values and norms of behaviour" referred to above, he concluded that it should.

This case involved a distributorship agreement which required the parties to communicate effectively and cooperate in its performance. Yam Seng was arguably entitled to expect that it would be kept informed of ITC's best estimates of when products would be available, and any material changes. However, as Yam Seng's case was not advanced in that way, it was not necessary to decide whether, in this case, good faith included positive obligations of disclosure.

Instead, the court found that the content of the duty was captured by two more specific terms which should be implied, namely: (i) not knowingly to provide false information; and (ii) not to authorise sales of products that would undercut the prices specified in the agreement.

6. Relational contracts

As noted above, the decision in *Yam Seng* suggests that duties of good faith are more likely to be implied into so-called "relational" contracts – described as contracts which involve a longer term relationship between the parties in which they make a substantial commitment.

The judge in *Yam Seng* said that such contracts may require a high degree of communication, co-operation and predictable performance based on mutual trust and confidence, and involve expectations of loyalty which are not included in the express terms of the contract but are "implicit in the parties' understanding and necessary to give business efficacy to the arrangements". The examples he gave of such relational contracts were joint venture agreements, franchise agreements and (as in *Yam Seng* itself) long-term distributorship agreements.

A number of subsequent decisions have followed this approach in implying good faith obligations into contracts the court described as "relational", even though they did not fall squarely within the categories mentioned in *Yam Seng*.

The question of whether or not a contract is "relational" in this sense is obviously a rather loose concept; many contracts could potentially fall into this category, depending on where the boundaries are drawn. It is therefore difficult to predict the precise circumstances in which a duty of good faith is likely to be implied on this basis.

In *Bristol Groundschool Limited v Whittingham* [2014] EWHC 2145 (Ch) (see post), the High Court implied a duty of good faith into a long-term contract.

For approximately 10 years, the claimant (BGS) and one of the defendants (IDC) collaborated in producing electronic training manuals. IDC created the artwork. BGS provided the text, sold the manuals to students, and paid a specified sum to IDC for each manual sold. Ultimately they fell out and, as part of a broader dispute, IDC alleged that BGS had breached an implied duty of good faith by downloading materials from IDC's IT systems without authorisation.

Although the agreement did not fall squarely within the categories identified in *Yam Seng* – counsel for the defendant described it as a "hybrid" between a joint venture and product distribution agreement – the deputy judge found it was a "relational" contract of the kind referred to in that case, and contained an implied duty of good faith.

Good faith extended beyond, but at the very least included, the requirement of honesty. The relevant test was whether the conduct in question would be regarded as "commercially unacceptable" by reasonable and honest people in the particular context involved.

The court held that BGS's unauthorised downloading of material was commercially unacceptable and therefore BGS was in breach of the implied duty of good faith.

In *D&G Cars Ltd v Essex Police Authority* [2015] EWHC 226 (QB) (see post) the High Court implied a duty of honesty and integrity into a contract to recover vehicles for a police authority..

The contractor reported that a particular vehicle had been sent for crushing on the instructions of the police authority, but it was later discovered that it had instead been incorporated into the contractor's fleet following a body swap with another vehicle. Its explanation, which the court accepted, was that this had been done as a training exercise. However, the court held that the contractor was in breach of an implied term to act with integrity.

The existence of an implied term to act with honesty and integrity was (unusually) accepted by both parties, but the judge set out his view as to the proper legal basis for implying the term. The judge said he was using the term "integrity" to capture the requirements of fair dealing and transparency "which are no doubt required (and would, to the parties, go without saying)" in a contract of this sort.

The judge described the contract as a "relational contract par excellence", as it was for a relatively long period (initially five years) and would involve a very large number of individual transactions. The implied term was also justified by the nature of the contract, which involved dealing with recovered property of members of the public on behalf of a law enforcement agency.

In *Bates v Post Office Ltd* [2019] EWHC 606 (QC) (see post), the High Court considered implied duties of good faith in the context of group litigation between the Post Office and a large number of sub-postmasters ("SPMs") responsible for running local branches of the Post Office.

The court held that certain contracts between the Post Office and the SPMs were "relational contracts" and were therefore subject to an implied obligation to act in good faith.

In the court's judgment, whether a contract is a relational one depends on the circumstances of the relationship, defined by the terms of the agreement, set in its commercial context.

The court identified a number of characteristics relevant to that assessment, including, for example, whether the relationship is long-term, and whether the parties repose trust and confidence in each other in performing the contract. No single characteristic would be determinative, save that there must be no express terms in the contract which would prevent a duty of good faith being implied.

"Good faith obligations are more likely to be implied in long term contracts where the parties make a substantial commitment, as opposed to one-off dealings."

7. Contractual discretions

A good faith obligation may also be implied where a contract confers a discretion on one party to make a decision that affects the interests of both. The precise formulation differs between cases, but the essence seems to be a requirement to exercise the discretion honestly and in good faith, and not to act in an arbitrary, capricious or irrational manner.

This principle was discussed by the Supreme Court in *Braganza v BP Shipping Limited* [2015] UKSC 17. The court commented that a party who is charged with making decisions which affect the rights of both parties has a clear conflict of interest. To ensure that such powers are not abused, the courts have implied a term as to how they may be exercised.

In this context, a number of authorities distinguish between two sorts of contractual discretion:

- Where one party is to make an assessment or choose from a range of options.
- Where one party can simply decide whether to exercise an absolute contractual right.

It seems that in the first case, but not the second, a duty of good faith is likely to be implied – though of course the distinction is not always clear cut, and there may be room for debate as to which category a particular contractual discretion falls into.

To avoid this uncertainty, the prudent course is to address this issue specifically, either by including very clear words to exclude such a duty or by carefully defining the scope of the duty.

The extent to which a duty of good faith will be implied to regulate the exercise of a contractual discretion was also considered in the *Mid Essex* case (referred to above).

The case concerned a seven-year contract to provide hospital catering and cleaning services. It set out detailed service specifications and provided that, where relevant standards were not met, the Trust was entitled to make deductions from monthly payments and award "service failure points" which could ultimately give the Trust the right to terminate.

The Trust assessed the contractor's performance on what the Court of Appeal described as an "extremely harsh" basis. It made some assessments which were "absurd", such as awarding huge numbers of service failure points for out of date chocolate mousse and tomato ketchup.

The High Court had found an implied term that, in exercising its power under the clause, the Trust would not act in an arbitrary, capricious or irrational manner. The Court of Appeal overturned that finding. The contract contained precise rules for determining how many service failure points had been incurred. Determining the correct number was a matter of calculation, not discretion. The Trust's only discretion was whether or not to award those service failure points. That was a matter of deciding whether or not to exercise an absolute contractual right, and there was no justification for implying the proposed term.

A similar approach was followed in *Myers v Kestrel Acquisitions Ltd* [2015] EWHC 916 (Ch) (see post). The case involved two categories of loan notes, including one category (VLNs) issued to the claimants. The instrument creating the VLNs allowed the first defendant to "make any modification" unilaterally, as long as this was consistent with any modifications to the other category of loan notes.

Various modifications were made, with the effect that the repayment dates of the VLNs were postponed and they were subordinated to newly issued loan notes. The claimants argued that the right to amend was subject to an implied term that the amendments had to be made in good faith and for the benefit of the holders of the two categories of loan notes as a whole.

The court held that no duty of good faith should be implied. The contractual documentation was "extensive and detailed" and the parties were at arm's length. It was unlikely they had omitted an important term. That the parties had evidently considered protecting the claimants but had not included a duty of good faith suggested that no such duty was intended.

The court noted that the power in this case was akin to the claimant Trust's discretion in the *Mid Essex* case (referred to above). It was, in effect, a binary choice as to whether or not to exercise an absolute contractual right. The fact that the defendant had that contractual choice did not justify subjecting it to some kind of good faith obligation.

In contrast, in *Watson v Watchfinder.co.uk Ltd* [2017] EWHC 1275 (Comm) (see post) the High Court considered the terms of a share option which could be exercised only with board consent.

The court found that the board's right of veto was discretionary, rather than an unconditional right, as otherwise it would render the share option agreement meaningless.

Further, the court found that the board's discretion to refuse consent was subject to a qualification that it must not be exercised capriciously, arbitrarily or unreasonably. This was true whether the qualification was read into the clause as a matter of construction or by reason of an implied term.

Such a qualification was not inevitable in every case, the court said, but it was appropriate given that there was an obvious potential conflict of interest in this case (since the grant of further shares would dilute the existing shareholdings and restrict their availability for other investors).

"Just because the contract gives one party the power to make a decision, that doesn't mean its discretion is completely unfettered. The court may impose limits on how it must be exercised."

8. Negotiations

The starting point is that a bare agreement to negotiate is unenforceable in English law. It is likely to be, in essence, an "agreement to agree", which is too uncertain to form a binding contract. A duty to negotiate in good faith is also seen as unworkable because it is inherently incompatible with the adversarial position of a negotiating party. Enforcement is also problematic, as it is likely to be unclear whether negotiations have broken down because of a breach, and what the outcome would otherwise have been.

However, cases in more recent years suggest the courts may take a more liberal approach where parties have agreed such an obligation as part of a professionally drafted commercial contract, and where its content is subject to objective criteria.

In *Petromec v Petroleo Brasiliero* [2005] EWCA Civ 891, the Court of Appeal enforced an obligation to negotiate in good faith the extra costs of upgrading a vessel in accordance with an amended specification. If the parties could not reach agreement, the court could itself determine the reasonable costs; this was a matter that was capable of objective assessment.

The courts have also taken a more liberal approach in enforcing dispute resolution clauses: in *Emirates Trading v Prime Mineral Exports* [2014] EWHC 2104 (Comm), it was held that a clause requiring the parties to seek to resolve a dispute by friendly discussions, within a time limited period, constituted an enforceable condition precedent to arbitration.

Note that some legal systems may impose duties to act in good faith in negotiating contracts, which may apply if there is some connection with the jurisdiction in question (eg if negotiations are held there), even if the contract is ultimately governed by English law.

In *Shaker v Vistajet* [2012] EWHC 1329 (Comm) (see post), Mr Shaker sought the return of a US$3.55 million deposit paid pursuant to a Letter of Intent concerning the purchase and operation of an aircraft. It was accepted that the Letter of Intent was intended to be binding in respect of certain matters including the payment and refund of the deposit.

The Letter of Intent provided for the return of the deposit where "despite the exercise of good faith and reasonable endeavours" the parties failed to agree and execute the relevant transaction documents before a specified cut-off date. Vistajet argued that Mr Shaker was not entitled to the return of his deposit as he did not proceed in good faith or use reasonable endeavours to agree the relevant transaction documents.

The court held that, if the requirement to negotiate in good faith was a condition precedent to the return of the deposit, it was unenforceable. The position was different in *Petromec* because there were objective criteria to assess the relevant matters in the absence of agreement. Where, as here, there were no objective criteria, the court could not enforce the parties' agreement to agree and so the deposit was repayable. Caution should therefore be exercised when including obligations to negotiate in good faith in commercial contracts, and it will be only in rare situations where this will impose any binding obligations on the parties.

"An obligation to negotiate in good faith is unlikely to be binding unless it is subject to clear time constraints and/or objective criteria the court can apply to fill in the gap if there is no agreement."

9. Termination

The courts have been particularly reluctant to imply obligations of good faith in the context of contractual termination, whether they are considering the exercise of an express right to terminate (as in *TSG*, referred to in section 4 above, and *Ilkerler v Perkins*, below), or an innocent party's decision as to whether to affirm or terminate a contract following a counterparty's repudiatory breach.

In this latter context, in *MSC Mediterranean Shipping Company SA v Cottonex Anstalt* [2015] EWHC 283 (Comm), the High Court (Leggatt J, who also decided the *Yam Seng* case referred to above) suggested that an innocent party's decision whether to terminate or affirm the contract must be exercised in good faith (see post).

Leggatt J said he could not see any difference of principle between the exercise of a contractual discretion, which is subject to implied duties of good faith, and a choice whether or not to terminate in response to a repudiatory breach. The Court of Appeal, however, disagreed with that analysis (EWCA Civ 789 – although it upheld the first decision on other grounds - see post. In the Court of Appeal's view, good faith principles were not relevant in this context.

In *Ilkerler Otomotiv Sanayai ve Ticaret Anonim v Perkins Engines Co Ltd* [2017] EWCA Civ 183 (see post), the Court of Appeal held that the defendant did not have an implied duty of good faith when exercising contractual termination rights in a distribution agreement.

The agreement in question allowed the defendant to terminate for convenience, after the initial three year term of the contract, by giving at least six months' written notice. The claimant sought to rely upon the judgment of Leggatt J in *Yam Seng* to argue that an obligation of good faith or fair dealing should be implied. That suggestion was rejected by both the High Court and the Court of Appeal.

The Court of Appeal noted, in particular, that in *Yam Seng* Leggatt J was discussing requirements for communication and co-operation in the performance of a contract. He commented, "Requirements for communication and co-operation in relation to termination would take one into a different realm altogether."

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Notes

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