



"Good faith": what does it mean?

Does the term "good faith" mean anything when used in a contract governed by English law? And, if so, what effect is a "good faith" obligation likely to have in practice?

Historically, the English courts have tended to be hostile to the concept of good faith. However, a duty of good faith has long been implied into contracts of partnership, agency and other agreements involving fiduciary obligations. More recently, the English courts have shown themselves willing to give effect to express obligations to act in good faith in a wider range of commercial contracts (see below). In some instances, they may even be prepared to imply such a duty.

For example, in *Yam Seng v International Trade Corporation (2013)*, the judge suggested that, in some cases, a duty of good faith might need to be implied into other commercial contracts, such as franchise, joint venture and long term distribution agreements where "a high degree of communication [and] co-operation" is required to make the relationship work.

What does good faith mean?

There is as yet no widely accepted definition of good faith in a contractual context, although the courts have often emphasised honesty and fair dealing and, in several cases, fidelity to the parties' bargain. Its meaning and effect are therefore likely to vary considerably depending on the context (see examples below).

Practical impact

In practice, good faith has generally had less of an impact where the contract clearly sets out the terms of the bargain struck between the parties. In *Gold Group v BDW (2010)*, which concerned a property development agreement, the court rejected arguments that an express obligation to act in good faith required the owner of the land to adjust the financial terms in the light of a significant fall in property prices. The judge noted that good faith "*does not require a party to give up a freely negotiated advantage clearly embedded in the contract.*" However, where contracts are less clearly drafted and/or there is evidence of dishonesty or unfair dealing, good faith may have a more significant impact. For example, the *Yam Seng* case mentioned above concerned a poorly drafted distribution agreement. To

An attempt to define good faith

In *CPC v Qatari Diar (2010)*, the court concluded that an obligation in a property joint venture to act in "utmost good faith" did not require one party to subordinate its interests to those of the other party, but was likely to require it to:

- avoid cynical resort to the black letter of the law;
- observe reasonable commercial standards of fair dealing;
- be faithful to the agreed purpose of the agreement; and
- act consistently with the justified expectations of the other party.

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make it work effectively, the judge considered that a broad duty to act in good faith needed to be implied. By knowingly providing misleading information, the supplier had breached the good faith obligation, entitling the distributor to terminate the agreement and claim damages.

Wide or narrow?

Much also depends on how widely the courts interpret any obligation to act in good faith. In *Mid-Essex Hospital Services v Compass (t/a Medirect) (2013)*, an NHS Trust demanded that a catering provider make significant payments for relatively minor failures to meet service levels, such as a payment of £98,430 in relation to butter sachets with no use-by date. In the High Court, the judge concluded that the agreement contained a broad express obligation to act in good faith. In his view, the NHS Trust had breached that duty by effectively ignoring the spirit of the agreement in its approach to the service levels scheme. The Court of Appeal agreed that a number of the payments demanded had been excessive. However, it found that the duty of good faith was much narrower and did not apply to the service levels scheme; as a result, the NHS Trust was entitled to hold the catering provider to the letter of the agreement.

How we can help

We advise on a wide variety of commercial agreements including joint ventures, outsourcing, distribution, franchising, supply, manufacturing and sponsorship. We attach great importance to understanding our clients' businesses and looking after their interests in the long term.

Key points

- The courts will generally enforce an express obligation to act in good faith – but the impact of such a term will vary, depending on context.
- Inserting a good faith obligation can be useful – but the courts are reluctant to give it a wide meaning unless it is clear that this is what the parties intended (and it is always better to spell out what the other party has to do rather than rely on good faith).
- Specifically excluding good faith altogether is not advisable because it arguably seeks to exclude any duty to act honestly.
- If you want to minimise the impact of any implied good faith obligation, make sure the contract is sufficiently detailed, so that there is no need for the courts to imply such a duty in order to "fill in the gaps."

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