GOOD FAITH: ENFORCEMENT IN AUSTRALIA

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This paper examines a series of recent decisions from a number of Australian jurisdictions where the courts were asked to consider good faith in commercial contracts. It presents a brief summation of the relevant facts and issues of each case together with the findings in respect of good faith that were made. As will be evident, the outcomes delivered demonstrate that choice of law, forum and drafting techniques all play a part when relief is sought on the basis of a breach of good faith. The absence of any definitive High Court decisions means that the uncertainty about the utilisation of good faith standards in commercial relationships, including franchising relationships, will remain.

Enforcement of good faith in Australia

The use of ‘good faith’ in commercial contracts is an area of law that has been developing in Australia over the past 20 years and remains unsettled due to the absence of any definitive High Court decisions.

Case law from respective Intermediate Courts of Appeal and Trial Courts has delivered judgements involving interpretation and application of ‘good faith’ to commercial relationships. Each of these decisions continues to explore the scope and application of good faith in various commercial contexts in an ad hoc and less than satisfactory manner slowly piecing together jurisprudence in this area.

Franchises, as commercial ventures, are captured by these developments. It has been suggested that the nature of the franchise relationship itself lends itself to be more susceptible to the imposition of good faith standards. What is increasingly evident in franchise litigation is the incorporation as an alternate cause of action upon which a court may grant relief a breach of good faith. Until a definitive High Court decision is handed down, or one of the States or Federal Parliament introduces legislation, the uncertainty generated around the utilisation of good faith will remain.

“... the nature of the franchise relationship itself lends itself to be more susceptible to the imposition of good faith standards.”

* The author takes responsibility for the content of this paper but notes that this is general discussion only on specific issues arising from the respective cases. No advice is provided. Consideration of the application of these cases to other specific factual circumstances should be undertaken with care and reference to the full judgments.

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Developments in case law

Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service

Facts

Macquarie International Health Clinic (Macquarie) entered into a heads of agreement with Sydney South West Health Service (SSWHS) for the development of a private hospital on land in the precinct of the Royal Prince Alfred Hospital (RPAH).

The land was owned by SSWHS.

It was a matter of much discussion prior to the entrance into the heads of agreement that a private hospital be built next to (co-located) and physically linked to the existing RPAH and that two private hospitals in the area would not be commercially viable.

The heads of agreement required the parties act in utmost ‘good faith’ in the performance of their respective duties, in the exercise of their respective powers and in their respective dealings with each other.

Subsequent to the execution of the heads of agreement six specific agreements including a Construction Deed, Car Park Lease, Car Park Sub-Lease, Hospital Lease were signed by the parties each also incorporating a similar express good faith clause.

SSWHS undertook an asset strategic plan for RPAH which did not propose any development consistent with the heads of agreement which it had with Macquarie. This was not disclosed to Macquarie by SSWHS at the time of its preparation and presentation of the asset strategic plan.

Development applications were obtained, negotiations for a smaller hospital were undertaken, construction began and practical completion reached on some of the structures.

SSWHS served notices of default, then termination on Macquarie and took possession of the sites.

At first instance Macquarie sought recovery of possession, relief against forfeiture and unjust enrichment with an alternative claim for damages for breach. Macquarie lost in first instance.

On appeal Macquarie’s primary relief claimed was that SSWHS had breached its obligations to act in good faith under the heads of agreement as it had failed to disclose the asset strategic plan which differed markedly to earlier discussion and had later actively supported the construction of another private hospital nearby.

Court findings

The New South Wales (NSW) Court of Appeal held with respect to good faith that:

− The context of the [good faith] clauses is to be understood by construing the language of the parties in the context in which the clauses appear. They are contractual terms to be construed like any other;2

− The notion of good faith in the performance of contracts is one established by a number of cases in this court and is well known to the law in both common law and civilian systems. It was part of the law merchant. It finds its place in international conventions;3

− The usual content of the obligation of good faith can be extracted from Renard Constructions (ME) Pty Ltd v Minister for Public Works …as follows:

− obligations to act honestly and with a fidelity to the bargain;

− obligation not to act dishonestly and not to act to undermine the bargain entered or the substance of the contractual benefit bargained for;


2 Ibid. at [8].

3 Ibid. at [11].
an obligation to act reasonably and with fair dealing having regard to the interests of the parties (which will inevitably, at times conflict) and to the provisions, aims and purposes of the contract, objectively ascertained.\(^4\)

None of these obligations requires the interests of a party to be subordinated to those of the other.\(^5\) It is important to recognise these obligations must be assessed and interpreted in light of the bargain itself and its contractual terms.\(^6\)

Whilst the cases in this court have tended to equate or incorporate reasonableness with or into fair dealing and good faith that is not without controversy … nevertheless, in these contracts, with express clauses of this width that have a necessary place in the working out and performance of contracts in some cases over many years, an objective element of reasonableness in fair dealing is appropriate, taking its place with honesty and fidelity to the bargain in the furtherance of the contractual objects and purposes of the parties, objectively ascertained.\(^7\)

The above expression of the matter is consistent with the content ascribed to the phrase, “good faith”, in persuasive cases in influential jurisdictions in the United States: for example, refraining from acting with subterfuge and evasion: \textit{Daitch Crystal Dairies Inc v Neislos} 190 NYS 2d 737 (Appeal Div 1959); \textit{Harbor Insurance Co v Continental Bank Corp} 922 F 2d 357 (7th Cir 1990) ….

In the court’s opinion the obligation of utmost good faith did require SSWHS to:

- disclose that planning processes were under way indicating that Macquarie could no longer reasonably expect that there would be substantial facilities co-located as originally envisaged…\(^8\)
- give Macquarie an opportunity to persuade SSWHS to take a different course in developing RPAH, and possibly also an opportunity to consider revising its own plans and/or withdrawing from the project, and seeking SSWHS consent to do so;\(^9\)
- not provide support to the establishment of a private hospital which would make Macquarie’s private hospital non-viable.\(^10\)

Although the Court considered that there was a breach of SSWHS’s obligation of utmost good faith, in its opinion this was not a fundamental breach that would justify the termination of the heads of agreement as the breach could not be considered to have been one which deprived Macquarie of substantial performance of the contract as the agreed infrastructure was still to be built just not as originally discussed.\(^11\)

“… an obligation to act reasonably and with fair dealing having regard to the interests of the parties (which will inevitably, at times conflict) and to the provisions, aims and purposes of the contract …”

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\(^4\) Ibid at [12].
\(^5\) Ibid at [13].
\(^6\) Ibid at [14].
\(^7\) Ibid at [15].
\(^8\) Ibid at [20 and 155]
\(^9\) Ibid at [157]
\(^10\) Ibid at [Headnote 26].
\(^11\) Ibid at [158].
Starlink International Group Pty Ltd v Coles Supermarket Australia Pty Ltd¹²

Facts

Starlink International Group Pty Ltd (Starlink) provided trolley collection services to Coles Supermarkets Australia Pty Ltd (Coles) and Kmart Australia Ltd (Kmart) pursuant to the terms of an Agreement.

Coles terminated the contract with Starlink pursuant to one of three termination clauses in the Agreement on the basis of continued underperformance by Starlink and allegations that Starlink engaged in improper and possibly illegal conduct.

The express wording of the termination clause used by Coles was:

“During the Term, Coles may terminate the Agreement at any time without reason by giving the Service Provider 45 days written notice.”¹³

The Agreement also contained a Dispute Resolution clause that provided a number of actions to be undertaken by the parties to resolve disputes culminating with:

“Once a Dispute Notice has been given under clause 18.1(c) the Chief Executive or Managing Director of each party (or their nominee or delegate) must attempt to resolve the Dispute in good faith, on the basis that the parties wish to retain a long term commercial relationship.”¹⁴

Starlink argued that Coles was not entitled to terminate the contract without informing Starlink of its reasons for doing so or giving Starlink a reasonable opportunity to rectify its conduct.

Starlink asserted that the Agreement between the parties included an implied term that Coles would act in good faith towards Starlink when exercising their power under the termination clause. The term being implied, as a matter of law, into the Agreement.

Starlink also claimed that Coles was estopped from relying on the termination clause as a result of a representation that it would not rely on that termination clause unless Starlink was guilty of poor performance. Starlink also sought a declaration that the Agreement was not validly terminated.

Coles argued that the express terms of the contract were quite clear enabling it to terminate the contract ‘at any time without a reason’ with the only prerequisite that the clause imposed on Coles was to provide 45 days written notice to Starlink.

Court findings

The New South Wales Supreme Court held that commercial contracts are not a class of contract that, as a legal incident, have an implied obligation of good faith and it will depend on the individual contract as to whether good faith is implied. The Court cited with approval the prior case of Insight Oceania Pty Ltd v Philips Electronics Australia Ltd¹⁵ in support of this position.

The Court then went on to state that:

“The Law of Victoria, as the governing law of the Agreement, includes the principle of contract law that before a term will be implied into a commercial contract it must be:

(i) reasonable and equitable;

(ii) necessary to give business efficacy to the contract so that no term will be implied if the contract is effective without it;

(iii) so obvious that “it goes without saying”; and

(iv) capable of clear expression; and

(v) must not contradict any express terms of the contract.”¹⁶.

¹³ Ibid at [5]/
¹⁴ Ibid.
¹⁵ [2008] NSWSC 710
The Court confirmed that:

- the structure in the Agreement for dealing with a dispute imposed express obligations on each party to attempt to resolve it in good faith and also obliged them to act on the basis of their respective wishes to retain a long term commercial relationship;

- it was satisfied that the parties intended that any attempt to resolve a dispute would proceed in “good faith”, that is, they would attempt to resolve the dispute honestly and reasonably;

- these were commercial parties that had been engaged in a commercial relationship since 2005. Starlink had been willing to enter into the Agreement on the basis that the Coles had an entitlement to terminate it on 45 days written notice at any time without a reason. The implication of a duty to act in good faith in exercising rights under the termination provision would be to impose a condition on Coles inconsistent with the express terms of the Agreement. It would impose a condition on Coles that not only must they have a reason to exercise the termination right but that it must also be a good reason.

- There was no justification to imply a term of good faith as submitted by Starlink.

**Aquila Coal Pty Ltd v Bowen Central Coal Pty Ltd**

**Facts**

Aquila Coal Pty Ltd (Aquila) and Bowen Central Coal Pty Ltd (BCC) were joint venture partners in a coal mining venture. A clause of the joint venture agreement (JVA) required that the parties “act in good faith and in the best interests of the joint venture”.

A feasibility study was done which outlined two scenarios for the development of the mine. Scenario 1 envisaged project sanction before contracts for port and rail capacity were secured. Scenario 2 envisaged project sanction upon port and rail capacity being secured.

At a joint venture meeting Aquila voted to proceed on Scenario 2 and BCC voted to proceed on Scenario 1. If it came to a vote at a second meeting and the same outcome arose under the JVA BCC could trigger provisions to buy out Aquila’s interest in the JVA and had held meetings to discuss such an eventuality.

Aquila brought proceedings to restrain the holding of that meeting and consideration of the issue on a number of grounds including, that BCC’s conduct was a breach of the JVA clause to act in good faith and was not in the best interests of the joint venture.

This case involved the granting of interlocutory injunctions pending the resolution of the matter at trial and as such only assessed the submissions made on the basis of assessing whether a prima facie case existed to support the granting of injunctions.

**Court findings**

The Supreme Court of Queensland stated in respect to good faith that:

- For the present purposes, it is unnecessary to essay the law about the content of a contractual obligation to act in good faith. I respectfully adopt the observations of Hodgson JA... in Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service to the effect that a contractual obligation of good faith embraces no less than three related notions:
  - an obligation on the parties to co-operate in achieving contractual objects;
  - compliance with honest standards of conduct; and
  - compliance with standards of conduct that are reasonable having regard to the interests of the parties.18

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18 Ibid at [90].
Other authorities support the general proposition that a contractual obligation to act in good faith ordinarily would not operate so as to restrict decisions and actions, reasonably undertaken, which are designed to promote the legitimate interests of a party and which are not otherwise in breach of an express contractual outcome.19

One aspect of the duty to act in good faith, namely the requirement to co-operate in achieving the contractual objects, requires the parties to have due regard to “the legitimate interests of both parties in the enjoyment of the fruits of the contract as delineated by its terms”. Reference to the terms of the JVA is necessary to determine the interests of the parties and the aims and purposes of the contract, objectively ascertained. At a level of generality, the aim of the JVA is for the participants to co-operate to develop a viable project. However, neither party contracted to be in the commercial equivalent of a marriage, or not to exercise contractual rights that were to the financial disadvantage of the other. Acting in good faith and in the best interests of the joint venture might require a proposal for mining development to proceed that was not to the commercial advantage of one participant.20

Aquila submits that its case is that, in seeking to have Scenario 1 adopted, BCC has not acted in good faith or in the best interests of the joint venture, due to the absence of a commercial justification for wishing to undertake mine development in accordance with Scenario 1, as that scenario exposes the joint venture to extreme risk that the mine could be developed in circumstances in which there is no, or no adequate, port and rail capacity for the coal it produces.21

There is a substantial case that BCC has not acted in good faith or in the best interests of the joint venture in proposing Scenario 1 based on the evidence of the experts lead by Aquila...there is also a virtual absence of evidence, and no sworn evidence at all, that BCC believes that Scenario 1 is in the best interests of the joint venture.22

I [Applegarth J] am satisfied that Aquila has established a prima facie case in relation to a breach of the JVA clause requiring the parties to act in good faith and in the best interests of the joint venture.23

Oliver v Commonwealth Bank of Australia24

Facts

Oliver entered into a margin loan agreement ultimately with the Commonwealth Bank of Australia (CBA) governed by express terms and conditions. The global liquidity crisis hit and the loan to security ratio was exceeded. Pursuant to the terms Oliver was required to restore the ratio to the required levels which he did through the sell down of some shares.

“... a contractual obligation to act in good faith “ordinarily would not operate so as to restrict decisions and actions, reasonably undertaken, which are designed to promote the legitimate interests of a party and which are not otherwise in breach of an express contractual outcome.”

19 Ibid at [93].
20 Ibid at [95].
21 Ibid at [103].
22 Ibid at [105-107].
23 Ibid at [130].
However the liquidity crisis continued and instructions were given to sell all the shares to repay the debt allegedly as a result of an agreement between Oliver, his financial advisers and CBA.

This commenced but subsequently the Bank took steps to close one facility, charge a break fee, open another facility, sell the investments and credit any sales payments to that newly created facility.

Although this ultimately resulted in $193.93 being left to his credit Oliver commenced proceedings on the basis that it was not right that the CBA had sold his investments without first giving him a margin call, failing to abide by the agreed strategy, breach of the margin loan agreement by the closure of one facility and charging of a break fee and in various ways acting not in good faith and unconscionably. This paper only deals with the good faith aspect of the judgement.

The CBA submitted that the mere exercise of a contractual right or a breach of a contractual obligation can never, of itself, involve a breach of the implied obligation of good faith.

Court findings

The Federal Court of Australia stated that:

− The question is as a matter of law whether the CBA is correct to submit that a duty of good faith and reasonableness can never be breached by the exercise of some contractual right, or forbearance from taking some action, under a contract.25

− In the absolute form in which it was put forward, this submission cannot be what was actually held in Burger King. That case was concerned with the operation of cl 4.1 of the agreement under which Hungry Jack’s operated as a master franchisee for Burger King. Clause 4.1 specified, in great detail, the standard expected of Burger King restaurants. Burger King had purported to terminate the arrangement on the basis of breaches of cl 4.1 to which Hungry Jack’s had rejoined that Burger King’s reliance on cl 4.1 was not in good faith. … the Court accepted that the operation of cl 4.1 was subject to an obligation of good faith. …the term could still not be relied upon unless in good faith. That consequence is antithetical to the CBA’s submission and for those reasons I do not accept the authorities the Bank relies upon to justify the relief which it seeks.26

It is a general rule applicable to every contract that each party agrees, by implication, to do all such things as are necessary on his part to enable the other party to have the benefit of the contract… there may be much to be said for the view that it is this term – neither new nor unsurprising - which lies under the good faith term and that they should be co-terminous. Gummow J…at a time when the implication of the good faith term was not quite so entrenched at an intermediate appellate level as it presently is…suggested that the good faith term might consist of the negative implication in Mackay v Dick together with the negative covenant not to hinder or prevent the fulfilment of the purpose

“It is a general rule applicable to every contract that each party agrees, by implication, to do all such things as are necessary on his part to enable the other party to have the benefit of the contract ... “

25 Ibid at [29].

26 Ibid at 30-34]
of an express promise. Secondly he observed without criticism, Professor Farnsworth’s view that many of the uses “to which the new concept of good faith is put today do not go beyond those to which the traditional techniques of interpretation and gap filling were put in yesteryear”. On the other hand, recent authority [Macquarie International Health Clinic Pty Ltd] has suggested that the principle may be broader.

As this was an interlocutory application for summary judgement the Court simply noted that the matters raised “invite a consideration of aims and purposes of the contract which task is properly to be seen as a matter for trial.

Alstom Ltd v Yokogawa Australia Pty Ltd & Anor (No 7)27

Facts

The case involved a refurbishment and automation of a power station in South Australia. The power station owners, Flinders Power Partnership (FPP), entered into a contract with the head contractor Alstom Power Limited (Alstom) worth $148.5 million.

Alstom subsequently entered into a joint venture with Yokogawa Australia Pty Ltd and Downer EDI Engineering Pty Ltd (YDRML) which incorporated the terms of the head agreement and provisions that were expressed to take precedence over the head contract.

Delays occurred and Alstom was required to pay FPP compensation.

Alstom then commenced proceedings against YDRML claiming that they were responsible for the delay.

YDRML counterclaimed on the basis that Alstom had breached their contract by failing to provide certain information. YDRML claimed failure to provide the information breached implied obligations to:

− act in good faith;
− to co-operate; and
− not to hinder or prevent YDRML’s performance under the contract.

Court findings

The South Australian Supreme Court stated that:

− The implication of a term that the parties to a commercial contract agree to do all that is necessary to be done on their part to enable the other party to have the benefit of the contract is well recognised and is not controversial.28
− The implied duty to cooperate cannot overrule the expressed provisions of the contract.29
− Alstom should have provided YDRML with regular updates and electronic copies of its works programs which could have then been implemented into YDRML’s programs.
− While the question of an implied obligation to act reasonably and in good faith has not been the subject of consideration by the High Court, neither has it been condemned. Although issues respecting the existence an scope of an implied good faith doctrine seemed to have been argued in Royal Botanic Gardens & Domain Trust v South Sydney City Council their application by intermediate courts of appeal was recognised but it was considered that that case was “an inappropriate occasion” to consider them.

28 Ibid at [569].
29 Ibid at [571].
I [Bleby J] consider that the …contract was a contract in which there arose an implied obligation on parties to act in good faith as that term is discussed in [Renard, Burger King and others] above. I do so because I consider that it is a term to be implied in every commercial contract, despite doubt expressed in some earlier cases that it was to be implied unequivocally as a universal term. Universal implication is supported by the American Restatement (Second) of Contract (1981) and is a part of the law of contract in Europe, the United States, Canada, New Zealand, China, Japan, and other parts of the world. Two of these contending parties are subsidiaries of companies based in Europe and Japan. However, even if the term were not to be implied universally, this contract is one example of the type of contract where it must be implied. That is abundantly clear from the admission of Alstom’s chief executive… and from the very nature of the work required under the contract. The …refurbishment was a complex project involving thousands of interrelated activities to be conducted by these two parties. Their respective contractual and operational requirements demanded a high degree of co-operation and reliance upon the good faith of each other. Without that glue to cement the contractual terms their relationships were likely to, as they did, break down. That in itself is a compelling indication of the existence of an implied obligation to act reasonably and in good faith. 30

It was held that YDRML was unable to meet its obligations under the subcontract since Alstom failed to notify them of key dates and provide constant updates despite being asked on a number of occasions.

Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd

Facts

Cordon Investments Pty Ltd (Cordon) was a property developer and commercial builder, while the second and third appellants were directors of Cordon.

Lesdor Properties Pty Ltd (Lesdor) was the owner of premises proposed to be developed.

Cordon and Lesdor entered into a joint venture to develop Lesdor’s premises which was set out in a Deed of Agreement (JV) as later amended by the parties.

Disputes arose between the parties Lesdor purported to terminate the JV. Cordon asserted this was repudiation and brought the first instance proceedings. The Primary judge found that Lesdor was entitled to terminate the JV, but that it had not suffered the bulk of the damages that it had claimed. Both parties appealed.

There were several grounds relied upon in the appeal relating to construction of clauses of the JV, substantial performance of the JV and waiver however, for the purpose of this paper, grounds 15-18 will only be considered.

Under grounds 15-18, Cordon and its directors contended that:

- the JV contained an implied term that the parties would act in good faith and reasonably toward each other, as such a term was both reasonable and necessary as Cordon could only receive the benefit to which it was entitled with Lesdor’s co-operation;

30 Ibid at [595 – 597]

— the primary judge had erred in failing to hold that Lesdor had breached an implied obligation of good faith by Lesdor adopting a strategy aimed at thwarting Cordon’s right to the benefit of the residual lots in the development which it would have been entitled to if the JV had completed as originally contemplated.

Cordon asserted:

— Lesdor insisted on defect free completion before executing and delivering Strata Plans which was beyond the terms of the JV;

— Lesdor refused to identify the work or works it maintained were defective or incomplete prior to serving its notice of termination;

— Lesdor unreasonably refused to execute and deliver the Strata Plan in circumstances where it had taken the benefit of the works to which it was entitled under the JV; and

— Lesdor intermeddled and interfered with Cordon’s contractual relations with its financier, National Australia Bank.

**Court findings**

In relation to grounds 15-18 of the Appeal, Bathurst CJ of the New South Wales Court of Appeal stated:

— Lesdor did not dispute that this was a case where it was appropriate to imply an obligation of good faith, pointing out that it did not require a party to act in the interests of the other party or to subordiate its own legitimate interests to the interests of that other party.32

— A long line of decisions had established that an obligation to act in good faith could be implied in contractual agreements, this obligation did not require the party to act in the interest of the other party or subordinate its own legitimate interests but such a term does require a party however to have due regard to the rights and interests of the other party;33

— The necessity for the implication of such terms in commercial contracts has not been universally accepted…however it is not necessary to discuss the matter further in this present case.34

— Citing Mason35 and others, the Court agreed that the content of the obligation has commonly been held to embrace three related matters:

  — An obligation on the parties to co-operate to achieve contractual objectives;

  — Compliance with honest standards of conduct; and

  — Compliance with standards of conduct that are reasonable having regard to the interest of the parties.

Bathurst CJ said that he had difficulty in seeing that insistence on compliance with a contractual obligation for Cordon to provide defect free completion prior to Lesdor signing Strata Plans could amount to a breach of an obligation of good faith. In the circumstances he held that Lesdor had not breached the implied obligation to act in good faith as “an obligation to act in good faith does not extend to being required to agree to something other than actual performance of the contract.”.36

32 Ibid at [141].

33 Ibid at [144].

34 Ibid.


36 Ibid at [146 and 154].
In relation to the assertion of intermeddling and interference with Cordon’s relationship with its financier, the Court noted that Lesdor was the guarantor of Cordon’s loan facility which was secured against the property. Lesdor therefore had an interest to protect and its own interests to consider where Cordon indicated to its financier that it had no intention or ability to repay or refinance the loan facility. Lesdor was left with only two choices, accept Cordon’s proposal which was not in accordance with the JV or refinance itself. The Court found that the fact Lesdor chose to refinance did not mean that it failed to act in good faith.

Cordon’s and Lesdor’s appeals failed and were dismissed.

**Trans Petroleum (Australia) Pty Ltd v White Gum Petroleum Pty Ltd**

**Facts**

Trans Petroleum (Australia) Pty Ltd (TP) was the owner of land upon which was located a service station and a convenience store. White Gum Petroleum Pty Ltd (White Gum) was the licensor of the Peak system for the operation of convenience store businesses from service station sites.

Pursuant to a Lease Peak leases the land from TP. Pursuant to a Fuel Re-Selling Agreement, White Gum granted to TP a non-exclusive licence to operate a convenience store from the land using the Peak system.

After 2 years White Gum issued a termination notice of the Fuel Re-Selling Agreement to TP.

Proceedings were commenced with TP alleging amongst other submissions:

- the termination clause is ambiguous when read in context of other clauses and the agreement as a whole;
- the power of termination must be exercised in good faith;

“... the necessity for the implication of a duty of good faith in the context of commercial contracts, both in performing obligations and exercising rights, has not been accepted universally within Australia.”

- the requirement that the power of termination be exercised in good faith arises upon a proper construction of the agreement as a whole or alternatively is implied by law...38

White Gum submitted that the power of termination was not limited in the manner argued by TP.

**Court findings**

The Western Australia Court of Appeal stated that:

- The Court of Appeal of New South Wales has decided numerous cases that a duty of good faith, both in performing obligations and exercising rights, may by implication be imposed on the parties to a contract. 39
- However the necessity of the implication of a duty of good faith in the context of commercial contracts, both in performing obligations and exercising rights, has not been accepted universally within Australia. 40
- I will assume…that the line of authority in New South Wales reflects the law in Australia; it is unnecessary, in this appeal, to decide the point. ... An implied obligation of the kind sanctioned in the New South Wales cases, does not extend to the imposition of obligations on the parties to a contract that are, in effect, inconsistent with the terms of the bargain. 41

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38 Ibid at [132].
39 Ibid at [150].
40 Ibid at [151].
41 Ibid at [152 and 154].
In my [Buss J with whom Pullin and Murphy JJ concurred] opinion, a duty of good faith, in exercising termination rights, should not by implication be imposed on the parties. The implication would be inconsistent with the terms of the bargain agreed upon by the parties. 42

The parties to a contract may be under an implied duty to co-operate in the performance of contractual obligations… However, this duty does not rise above the promises made by the parties to the contract. 43

The Court found there was no basis to overturn the decision at first instance on the grounds pleaded relating to implying a term of good faith.

**Beerens v Bluescope Distribution Pty Ltd** 44

**Facts**

Bluescope Distribution Pty Ltd (Bluescope) and Griffiths and Beerens Pty Ltd (Company) were in a supply agreement where by Bluescope would supply steel products to the Company through credit arrangements.

A winding up application was brought against the Company by an unrelated party.

Under the terms of the credit arrangements this provided that Bluescope could stop supply to the Company and change its terms of supply. Bluescope stopped supply.

Bluescope then required Mr Beerens, who was a director of the Company, to give Bluescope a personal guarantee for the due and punctual payment of all debts and monetary liabilities of the Company to Bluescope and an indemnity from any loss suffered in relations to the non payment of those debts or monetary liabilities for supply to be re-established to the Company.

Bluescope told Mr Beerens if he did not provide the personal guarantee then not only would supply not resume but that Bluescope would support the winding up application to recover amounts owing to it.

After seeking legal advice and negotiating the terms of the guarantee to be provided, Mr Beerens reluctantly provided the guarantee requested to restart supply to the Company by Bluescope.

Subsequently the Company was placed into receivership and then was wound up for failure to comply with a statutory demand.

Bluescope relying on a clause in its credit agreement refused to extend further credit, and demanded immediate payment of all moneys due. Bluescope also brought proceedings for damages against Mr Beerens to enforce the Guarantee and Indemnity.

Mr Beerens argued that his personal guarantee was unenforceable as it had been obtained by use of illegitimate pressure amounting to economic duress. This argument was based on three related but separate claims being unconscionable conduct, breach of contractual obligations of good faith and knowingly assisting the breach of a fiduciary duty. For the purpose of this paper the submissions in relation to good faith only will be addressed.

BlueScope submitted the express terms of the credit agreement clearly permitted it to withdraw credit facilities and demand immediate payment in the event that a receiver or similar official was appointed over any of the assets of the company or the company was presumed to be insolvent.

**Court findings**

The Victorian Court of Appeal stated that:

- generally speaking, it is not improper pressure to threaten recovery proceedings, including bankruptcy and winding up proceedings, in good faith in order to persuade a debtor to pay what is due. 45

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42 Ibid at [155].
43 Ibid at [156].
45 Ibid at [43].
if a creditor makes a threat to bring a proceeding which the creditor knows to be groundless or for an improper purpose, the threat is improper and may impose improper pressure sufficient to vitiate a transaction or payment of which it is the substantial cause.\(^{46}\)

Bluescope’s threat was not shown to be other than a threat to invoke winding up process in good faith in order to recover amounts which were or would accrue due about which Mr Beerens sought legal advice and negotiated the terms of the Guarantee he executed.\(^{47}\)

The need for particularity in the content and application of an implied obligation of co-operation or good faith is especially important given that the High Court in *Royal Botanic Gardens and Domain Trust v South Sydney City Council*\(^{48}\) expressly left open the issues arising from ‘the debate in various Australian authorities concerning the existence and content of an implied obligation or duty of good faith and fair dealing in contractual performance and the exercise of contractual rights and powers’.\(^{49}\)

if there was an implied obligation of good faith and fair dealing in the credit arrangements not to exercise legal rights for an improper purpose, it certainly would not have operated so as to restrict decision and actions reasonably taken to promote legitimate interests of Bluescope as expressed in the terms of the credit arrangement.\(^{50}\)

Bluescope had every right consistent with its obligations of co-operation and good faith and fair dealing to invoke the clause to cease supply and to enforce its credit arrangements as it did.\(^{51}\)

Based on this, the Court observed that an implied term ought not be inconsistent with, or contradicted by, the express terms of the credit agreement.\(^{52}\)

*I [Tate, JA]* do not accept that, as the law currently stands, the content of any implied obligation or duty of good faith in the exercise of contractual rights and powers requires compliance with an overriding standard of reasonableness that would deny Bluescope the exercise of its contractual rights ... in the promotion of its legitimate commercial interests, when the conditions for the exercise of those rights are met.\(^{53}\)

No breach of a duty of good faith was found against Bluescope.

**Summation of trends identified**

Without doubt this area of law requires a cautious approach as consistency of outcomes and determinations vary between Australian State and Federal jurisdictions.

Trends that can be observed include:

- The judges of New South Wales are the lead Australian State proponent for implying good faith into commercial relationships and consequently the law of New South Wales has a series of precedent cases from its Court of Appeal which continue to be applied by lower courts;
- Concern has been expressed judicially and academically about the formulation and scope of good faith;
- The rules of interpretation of commercial contracts continue to apply particularly where the court is asked to imply good faith as a term of the contract. Clear drafting of express provisions of good faith will increase the prospects of application as drafted;

\(^{46}\) Ibid at [46].
\(^{47}\) Ibid at [48-40].
\(^{48}\) (2002) 240 CLR 45, 63 [40]
\(^{49}\) 2012] VSCA 209 at [162].
\(^{50}\) Ibid at [52 and 55]
\(^{51}\) Ibid at [57].
Breaches of good faith appear as an alternative cause of action in commercial litigation, generally as a fall back if an identified primary cause of action is unsuccessful due to the uncertainty surrounding its scope and application.

Clarification of the extent and application of good faith by the High Court will be welcomed when ultimately it considers the case law that has developed and resulted in the present diversity in judicial statements and application.

Franchising like every other commercial enterprise affected by the uncertainty currently in effect can only benefit from a clear pronouncement of the law in this field when it is delivered. As with all seminal legal developments however, no system wants theirs to be the test case and attempts to minimise risk as far as possible through its drafting of terms and early dispute resolution processes.

“Franchising like every other commercial enterprise affected by the uncertainty currently in effect can only benefit from a clear pronouncement of the law in this field when it is delivered.”

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