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Not Keeping the Faith: A Critique of Good Faith in Contract Law in Australia and the United States

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Abstract

Good faith is a concept that should never have been introduced into Australian contract law. It is inconsistent with many Anglo-Australian legal principles and is, in some instances, already provided for with regard to well established Australian concepts relating to contractual relations. As a copy of the poorly established idea of good faith in the United States, the doctrine has little practical application in Australian law and so its hurried introduction into the Australian jurisdiction has been understandably met with criticism.

KEYWORDS: good faith, contract law, United States, Australia

*The Author would like to acknowledge Dr Stephen James, Lecturer of Law, Victoria University, for his guidance

NOT KEEPING THE FAITH: A CRITIQUE OF GOOD FAITH IN CONTRACT LAW IN AUSTRALIA AND THE UNITED STATES.

By Angelo Capuano[*1]

Introduction

Good faith is a concept that should never have been introduced into Australian contract law. It is inconsistent with many Anglo-Australian legal principles and is, in some instances, already provided for with regard to well established Australian concepts relating to contractual relations. As a copy of the poorly established idea of good faith in the Unites States, the doctrine has little practical application in Australian law and so its hurried introduction into the Australian jurisdiction has been understandably met with criticism.

Comparisons With the Duty to Cooperate and Act Reasonably

Setting aside the newly developed concept of good faith, it is evident that a duty to cooperate has been established in Australian contract law for over a century[2] and reaffirmed in modern Australian cases:

> … each party agrees, by implication, to do all such things as are necessary … to enable the other party to have the benefit of the contract.[3]

The duty to cooperate is said to be a 'universal term'.[4] In Australian contract law another 'generally implied term' is the duty to act reasonably. This duty imposes on parties a duty to comply with the 'reasonable' requests made by either party.[5] In particular, the view that the Australian form of cooperation[6] and acting reasonably is said to be 'essentially indistinguishable from the duty to act in good faith'[7] further promotes the notion that the application of 'good faith' in Australian

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* The Author would like to acknowledge Dr Stephen James, Lecturer of Law, Victoria University, for his guidance

1 Law Student, Victoria University.

2 *Butt v McDonald* (1896) 7 QLJ 68, 70-1 cited in *Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607.

3 *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607 (per Mason J, citing *Butt v McDonald).*

4 Seddon NC, Ellinghaus MP, *Cheshire & Fifoot's: Law of Contract* (8th ed, 2002), 414.

5 Ibid, 428.

6 Peter Heffey, Jeannie Paterson, Andrew Robertson, *Principles of Contract Law*, (2002), 264.

7 Seddon, above n 3, 429.

law has been unnecessary.[8] However, an outline of the newly forged Australian doctrine of good faith would be useful prior to more fully evaluating its legitimacy and usefulness in Australian law.

A. Good Faith in Australia

Good faith, introduced into Australian law via the case of *Renard Constructions (ME) Pty Ltd v Minister for Public Works*[9] as a universal term[10] is 'clearly becoming enshrined in Australian law'.[11]

In *Renard,* Priestley JA referred to an explanation of good faith 'given in the United States by Summers' who states that '[Good faith] is a phrase without general meaning'[12] as it is 'an excluder'. In other words, good faith 'serves to exclude heterogeneous forms of bad faith' ;[13] therefore, a party breaches a duty of good faith by acting in bad faith. With his approval of Summers' excluder argument, this was the closest that Priestley JA came to defining good faith.[14] However, further Australian cases have adopted good faith and, as such,

8 One clear definition of 'good faith' was set out by Thomas, Keith and Blanchard JJ of the New Zealand Court of Appeal who suggested that 'good faith' is basically 'faithfulness to an agreed common purpose and consistency with the justified expectations of the other party'. This is almost identical to Australian concepts of reasonableness. See: *Bobux Marketing Ltd v Raynor Marketing Ltd* [2002] 1 NZLR 506, 547. Some academics also describe it as acting 'reasonably' and 'honestly'. Also see: JW Carter, E Peden 'Good Faith in Australian Contract Law', (2003) 19 *Journal of Contract Law* 155, 155. These definitions as set in *Bobux* however have not been clearly or overwhelmingly accepted by the Australian judiciary.

9 (1992) 26 NSWLR 234, 257.

10 Seddon et al, above n 3, 419. Seddon et al nonetheless affirm that this idea of a universal term has not been followed by subsequent Australian cases.

11 Bremen J (1999) 'Good Faith and Insurance Contracts – Obligations on Insurers' 19 *Australian Bar Review* 89, 89. Also, Finn J in *Hughes Aircraft Systems International v Airservices Australia* (1997) 146 ALR 1 made this opinion quite clear: '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 expected to adhere throughout the live of their contracts'. Therefore, there exists little doubt that good faith is a term to be implied in all contracts. Also see: *Alcatel Australia v Scarcella* (1998) 44 NSWLR 349, 369.

12 Heffey et al, above n 5, 268.

13 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 266-7.

14 Baron A 'Good faith and construction contracts – from small acorns large oaks grow' (2002) 22 *Australian Bar Review* 54, 61. Nonetheless, in Canada 'bad faith' has been described as conduct 'that is contrary to community standards of honesty, reasonableness and fairness' See: *Gateway Realty Ltd v Arton Holdings Ltd* (1992) 112 NSR (2d) 180 (C.A), 212 cited in *Service Station Association v Berg Bennett* (1993) 45 FCR 84, 95.

additional explanations of good faith in Australia have branched out from the initial explanation made in *Renard*.

For instance, in the case of *South Sydney District Rugby League Football Club Ltd v News Ltd*[15] a 'core meaning' thesis of good faith was devised. Unlike the excluder thesis adopted by Priestley JA in *Renard,* Finn J in *South Sydney* expressed that acting in good faith was described in terms of 'loyalty to a contract'.[16] Furthermore, in *Far Horizons Pty Ltd v McDonalds Australia Ltd*[17] and *Burger King Corp v Hungry Jacks Pty Ltd*[18] the motives of the party alleged to be acting in bad faith were considered vital in determining whether good faith was breached. *Far Horizons* suggested that if there is a pursuit of legitimate commercial interests and there is no motive to harm the other party, then this does not amount to a breach good faith.[19] This idea that motive to harm is likely to establish a breach of good faith was concurred with in *Burger King*:[20] therefore one clear component of good faith is that to act with harmful intent is an example of acting in bad faith. Unlike the universal application of good faith intended by Priestley JA in *Renard, Burger King* also suggests that good faith is to be applied as a generic term implied into a particular class of contract.[21]

Therefore, many decisions not uniformly incorporating good faith give rise to questions regarding its introduction into Australia and the model on which it is based. However, in support of his introduction of good faith into Australian law, Priestley JA states that:

> … there has been little if anything to indicate that recognition of the obligation [of good faith and fair dealing] has caused any significant difficulty in the operation of contract law in the United States

Unfortunately, this could not be further from the truth.

B. US Good Faith: A Bad Import

The concept of good faith is yet to be clearly defined in the United States[22] and thus its application has been unpredictable and inconsistent among US state

15 [2000] FCA 1541.
16 Seddon et al, above n 3, 423.
17 [2000] VSC 310.
18 [2001] NSWCA 187.
19 Seddon et al, above n 3, 425.
20 Ibid, 427.
21 Ibid, 420, 431. This however was done 'not without equivocation'. Simply, this exemplifies the ambiguities relating to the 'good faith' in Australia.
22 Seth William Goren 'Looking for Law in all the Wrong Places: Problems in Applying the Implied Covenant of Good Faith Performance' (2003) 37 *University of San Francisco Law Review* 257, 257, 258, 267. In particular Goren stated that 'misapplication of contractual good faith' has led to 'irreconcilable decisions' which

Supreme Courts.[23] Such a belief is undoubtedly shown by a statement made by the Illinois Supreme Court where it was said:

> … what the term [good faith] means … remains somewhat of a mystery. Its meaning, moreover may change, depending upon the context in which it is used.[24]

Therefore good faith is a legal principle which has been described as a 'mystery', with its meaning being susceptible to 'change', as stated by a Supreme Court of a US state, shows that there is a lack of clarity in the definition of good faith. In fact, within the arguments of Priestley JA, citation is made of the work of Professor Farnsworth. However, according to Farnsworth, 'the doctrine of good faith has produced a tangled case law and has an uncertain development' in the United States.[25] As such, Australia should not adopt a foreign principle that has no solid meaning in its parent jurisdiction.

Further to this point, Priestley JA, with his adoption of US 'good faith', also neglected established US common law. In the Unites States implied terms of good faith 'fill the gap … [and] do not block the use of terms that actually appear in [a] contract'.[26] Nonetheless, Priestley JA, in 'blocking' the expressly provided provision to cancel the contract in *Renard* because it was unreasonable, contravened US case law. Therefore, his argument that US case law should be persuasive lacks credibility. However, the most direct inconsistency between Priestley JA's concept of good faith and US good faith was highlighted by a statement in the Oregon Supreme Court:

> …the duty of good faith cannot serve to contradict an express contractual term … The party invoking its express, written contractual right does not, merely by doing, violate its duty of good faith[27]

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have been 'subsequently reversed' or 'their conclusions overturned by statute'. Also see, William Deitrick, Jeffrey Levine 'Contractual Good Faith: Let the Contract, not the courts, define the bargain' 85 *Illinois Bar Journal* 120 (1997), 120 where it was stated that '[the law governing good faith] is confused and court decisions are inconsistent'.

23 Steven Burton, 'Breach of Contract and the Common Law Duty to Perform in Good Faith', (1980) 94 *Harvard Law Review* 369, 370. Even 12 years before *Renard* US good faith lacked consistency and definition, this surely raises questions about Prietley JA's allegations that US good faith had no serious problems.

24 *Watseka First International Bank v Ruda* 135 2d 140 (Ill, 1990), 145 cited in Deitrick n 28, 120.

25 Ian Stewart, 'Good Faith in Contractual Performance and in Negotiation', (1998) *Australian Law Journal* 370, 376. Also see, Dietrick et al, above n 28, 120.

26 *First Bank of Whiting v Kham & Nate's Shoes, No 2., Inc* 908 F2d, 1357 (NDIll, 1989), cited in Deitrick, above n 21, 122.

27 *Uptown Heights Associates v Seafirst Corporation* 891 P2d 639, 643 (Or, 1995), cited in Dietrick, above n 21, 122.

Therefore the party allegedly acting with bad faith in *Renard,* (by exercising their expressly provided power to cancel the contract) should not have been prevented from using their express contractual right merely because of the belief that doing so would contravene a duty of good faith.

Fundamental components of US good faith were therefore overlooked by Priestley JA, and his honour's decision purposely to select pieces of US law without reference to US case law as a whole should not result in an Australian doctrine of 'good faith' subject to the unwarranted and unsupported rules set by him. Furthermore, in attempting to promote the use of good faith in Australia, the research conducted by Priestley JA as to good faith in US law highlights its forced introduction into US common law by the legislature of the United States. The implied doctrine of good faith 'had become neglected'[28] in all but two US states until the enactment of the US Uniform Commercial Code was accepted in 49 US States by 1968.[29] Arguably, then, this may have been due to the fact that the US judiciary could not find a practical application of good faith and thus did not bother to use it. The judiciary in the United States therefore had little choice in accepting the application of good faith in US law. Arguably, without legislative intervention, the problematic implied duty may have disappeared from US common law altogether. This view is supported by decisions of the Oregon Supreme Courts which 'illustrate the courts disregard for both its own precedent and statutory law in erecting an analytic framework that renders the good faith doctrine ineffective'.[30] Despite legislative intervention, the judiciary has developed the common law in a way that can circumvent the statutory US good faith. Clearly, the judiciary cannot see a useful application for good faith and so chooses to eradicate it through the developments of US case law.

Moreover, Gummow J, in his analysis on the place of good faith in Australian law, clearly points out that 'Anglo-Australian law as to the implication of terms has … developed differently'[31] from US law. As such, a concept of good faith that may suit the US jurisdiction has no Anglo-Australian common law support or explanation besides its connection with Anglo-Australian ideas of cooperation and reasonableness in contract. Good faith in particular has little establishment in Australia, and, although analogous to reasonableness and cooperation in contract, good faith itself nonetheless derives from foreign common law. The ideas of good

28 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 264.

29 Ibid.

30 James Webster, 'A Pound of Flesh: The Oregon Supreme Court Virtually Eliminates the Duty to Perform and Enforce Contracts in Good Faith', (1996) 75 *Oregon Law Review* 493, 497.

31 *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 45 FCR 84, 95.

faith are merely 'borrowed'[32] from US law and as such do not have a legitimate position in Australian contract law as they deviate from the line of common law authority that has developed cooperation and reasonableness in contract. It would thus seem more appropriate for the Anglo-Australian principles of cooperation and reasonableness to have been built upon by Priestley JA rather than for him to simply import a foreign legal principle.

> Judges bring with them personal idiosyncrasies and prejudices … the law … can never be perfectly detached from a judge's own perception of right and wrong. But it must be as autonomous as it can be made. A judge must be able to say: 'it is not me who does this to you, it is the law. Look I will show you.[33]

Priestley JA, by importing good faith from the US rather than developing well established Anglo-Australian legal principles displays the fact that he used his personal discretion in deciding *Renard* rather than his judicial responsibility of interpreting the facts with reference to Australian precedents. Hence, considering that *Renard* was the principal case for Australian good faith, it was Priestley JA that imposed good faith upon the litigants in *Renard*, not Australian law.

C. Unclear Application in Australia

This unwarranted imposition of good faith by Priestley JA has therefore resulted in unclear applications of the doctrine in Australia. Although recent judgments incorporating the doctrine 'discuss it academically', they do not clarify the way in which it is to be implied[34]. Furthermore, until the decision in *Renard,* 'there had only been tentative acceptance in Australian jurisprudence of an implied term of good faith'. Thus it may be said that the duty's common law background is too weak for a solid application in Australian law,[35] and that a legal principle that cannot be clearly understood should not be applied.[36]

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32 Professor Allen E Farnsworth, 'The Concept of "Good faith" in American Law', (Speech delivered at the Centre for Comparative and Foreign Law Studies, Rome, April 1993) <http://www.crdcs.org/frames10.htm>.

33 James Edelman, 'Judicial Discretion in Australia', (2000) 19 *Australian Bar Review* 285, 299.

34 Bremen et al, above n 10, 90.

35 Baron, above n 13, 56.

36 The Hon. M H McHugh AC 'The Judicial Method' (Speech delivered at the Australian Bar Association, London, Monday 5 July 1998) - High Court of Australia. <http://www.hcourt.gov.au/speeches/mchughj/mchughj_london1.htm>, Also see: *Breen v Williams* (1996) 186 CLR 71, 115. 'Any changes in legal doctrine, brought about by judicial creativity, must "fit" within the body of accepted rules and principles'. It is clear that good faith does not neatly fit into Australian contract law and thus Priestley JA's act of creativity should not have become a legal principle.

Inexact and broad interpretations of the duty will inevitably result in inconsistent judicial decisions. Subsequent cases applying good faith since *Renard* have 'led contract law into a potentially disastrous situation' as, even now, the concept has many differing definitions attributed to it by Australian courts.[37]

Additionally, such unclear explanations of how the implied duty of good faith is to be applied in Australia may 'drive away' litigants who would prefer not to pursue legal action due to 'vague concepts of fairness which make judicial decisions unpredictable'. Therefore even if the outcome of disputes might be 'hard' on a party, '[then society regards] that as an acceptable price to pay in the interest of the great majority of business litigants'.[38]

As put by Sir Stephen Sedley:

> Law spends its life stretched on the rack between certainty and adaptability, sometimes groaning audibly but mostly maintaining the stoical appearance of steady uniformity which public confidence demands.[39]

The unpredictability of good faiths application by Australian courts will place considerable burden on litigants who cannot confidently understand their legal rights prior to litigation. Therefore, consistent judicial decisions with reference to an established and solid legal principle are for the common good as certainty, 'which is itself a material element of justice',[40] will act to reduce unnecessary litigation. Legal professionals should be able to advise parties to a contract of their legal position without the need to consult the interpretation of a judge and pursue costly legal action, or worse, have parties in dispute disregard their legal rights due to the prospect of unpredictable litigious outcomes. It is thus against justice that a vague concept of fairness such as good faith is allowed to deny contractors a right to confidently know their legal position before legal action takes place.

Hence, as depicted by the Illinois Supreme Court, and concurred with by various Australian judges, good faith lacks clarity in the United States, and we have already seen that this will certainly be carried on into Australian law through its introduction as a US model.[41]

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37 Carter, above n 7, 11, 14-16.

38 V*roon BV v Foster's Brewing Group Ltd* [1994] 2 VR 32, 67.

39 Gerard Brennan, 'Why be a Judge?', (1996) 14 *Australian Bar Review* 89, 91.

40 Ibid.

41 In *Service Station Association v Berg Bennett* (1993) 45 FCR 84, 92, 94; 117 ALR 393, 407 Gummow J makes reference to a trial and error scenario in the United States 'requiring repeated adjudication before an operational standard' may be 'articulated and evaluated'. He also suggests that adequate scrutiny is warranted before any unstable legal principles are to be 'imported' into Australia.

Furthermore, the way good faith was introduced into Australia through *Renard* is also valuable because the case itself is legally unclear.

D. 'Good Faith' in Renard

Foremost, Baron argues that Priestley JA's discussion of the concept of good faith 'was … clearly obiter',[42] and in many respects scrutiny of that concept is warranted.

In adopting the concept of good faith Priestley JA linked the well established Australian concepts of reasonableness to good faith used in the US and Europe. Thus, Priestley JA's characterization of the US and European notion of implied good faith as having 'much in common' with Australian idea's of 'reasonableness'[43] shows that his comments of good faith are statements used to explain why reasonableness should be used in Australian law.[44] As such, his discussion of good faith should not be strictly applied as ratio decidendi and is not the underlying principle of law to be applied in Australian contract law.

The misconstruction of Priestley JA 's observation as 'ratio decidendi' therefore brings forth the argument that the succeeding Australian decisions adopting good faith in Australian law have depended on a wrongful interpretation of Priestley JA's judgment. This is highlighted by the series of cases that decided to adopt the concept of good faith with the excuse that they were bound to follow such an idea set in a 'number' of Australian cases.[45] Therefore, the series of judgments that

42 Baron, above n 13, 60.

43 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 263.

44 S.E Marantelli, *The Australian Legal Dictionary*, (1985), 178. This dictionary states that 'obiter' refers to statements made 'incidentally' or on the way to legal reasoning or opinions of the judge made about law which 'he was not called upon to decide'. Further, the *Butterworths Australian Legal Dictionary* (ed) Peter Nygh, Peter Butt (1997), 807 states simply that 'obiter' is 'a remark in passing' that '[does] not form part of the reasoning of a case'. So, the statements of Priestley can therefore clearly be construed as obiter.

45 See: *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310,120, (Byrne J felt he was not 'at liberty to depart from the considerable body of authority in this country which has followed the decisions of the New South Court of Appeal in *Renard Construction (ME) Pty Ltd v Minister for Public Work*') Furthermore in *Garry Rogers Motors Aust Pty Limited v Subaru (Aust) Pty Ltd* (1999) ATPR 41-703 the court placed a great deal of emphasis on 'recent cases'. Therefore, the personal preferences of a handful of judges can be said to have begun a very persuasive precedent that has been fervently argued as being unnecessary by many academics and members of the judiciary.

have adopted good faith with reference to the supposed authority of *Renard* has precipitated an unjustified application of a concept that is arguably obiter.[46]

This has sparked an unwarranted application of the concept of good faith in Australia and highlights the questionable position of good faith in Australian contract law as displayed by members of the judiciary. For example, in applying his decision in *Hughes Bros Pty Ltd v Trustees of the Roman Catholic Church for the Archdiocese of Sydney,*[47] Kirby P (as he then was) declared that his application of the decision in *Renard* was made because of his 'judicial obligation', even if he were to 'disagree strongly with what was determined in *Renard*'.[48] Meager JA also indirectly displayed his dissatisfaction with the rule in *Renard*, stating that although he is bound by the decision in *Renard*, this was 'at least temporarily' the position.[49] Therefore, should good faith have been implied into the case of *Renard* at all?

E. Good Faith and the Rules Governing Implied Terms in Fact

As set in *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council,*[50] for an implied term in fact to be adopted into a contract it must:

(1) be reasonable and equitable to do so,
(2) must give the contract business efficacy,
(3) be so obvious that 'it goes without saying',
(4) be capable of clear expression and reasonably certain in its operation; and
(5) be consistent with the express terms of the contract.

With regard to these tests, Priestley JA in *Renard* stated that all five tests were satisfied.[51] However, these comments were opposed by Meagher JA in the same case[52] and fervently objected to by various academic writers, notably, Baron.

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46 Baron, above n 13, 58. Baron also suggests that the developments of a single Justice of the Sew South Wales court of appeal have created a 'legal leviathan' that is wrongly being applied as precedent in Australian law. Indeed, the judgment of Priestley JA being misconstrued by a single subsequent case has now created precedent that is difficult to question due to its application in the federal court of Australia. See: *Hughes Aircraft Systems International v Airservices Australia* (1997) 146 ALR 1, 36 where Finn J stated that 'its [good faith] more open recognition in our own contract law is now warranted'. His view that good faith is to have universal application 'to which all contracting parties are expected to adhere' furthermore displays that good faith is now a principle that lower Australian courts are now bound to adopt.

47 (1993) 31 NSWLR 91.

48 Ibid, 93.

49 Ibid, 104.

50 (1977) 180 CLR 266 cited in *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 66.

As suggested by Baron (1) 'it would be unreasonable for the courts to circumscribe [a party's express right to terminate a contract] by implication of a term of good faith'; (2) the contract in *Renard* was already 'commercially effective without the imposition of the term'; (3) in the pursuit of commercial interests, the implication of good faith would not have been obvious 'at the time of entry into contracting'; [53] (4) it has been argued by academics that good faith is 'too amorphous to be useful' and at the time of *Renard,* the implied term of good faith was not capable of clear expression, and; (5) the implied term of good faith was 'inconsistent with the rights and obligations expressed in the contract' .[54]

Baron's arguments show that good faith should not have been implied in fact into the case of *Renard*. As such, the reasoning of Priestley JA in applying good faith in *Renard* cannot be justified. Increased persuasiveness regarding Baron's arguments is displayed by Meagher JA's similar dissatisfaction with Priestley JA's reasoning. Meagher JA's view was that a limitation imposed by a duty to act reasonably in contractual dealings 'could only arise either from the express words of the contract or by way of an implied term'.[55] However, in making this suggestion he affirms that with regard to the case in question, no room existed in the contract to imply a term[56] as any attempt to do so 'would not survive the tests'[57] outlined as necessary in implying terms in fact. Thus, unless expressly provided for, good faith, according to Meagher JA, should not have been adopted in the case of *Renard* because the facts of the case did not warrant such an implication.

F. Good Faith and Express Terms

In *Renard,* the defendant could not exercise their express contractual right to cancel the contract because, according to Priestley JA, the act was done in bad faith. However, the defendant's act, irrespective of motive, could not be blocked as that power was provided under an express term of the contract. Thus, being an express term, it displayed the intentions of the parties and good faith should not

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51 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 257; all tests were satisfied clearly except business efficacy where 'minds may differ'.

52 Ibid, 275, Meagher JA states that the facts could not 'survive' the basic common law tests relating to applying terms by implication.

53 See: *Shirlaw v Southern Foundaries (1926) Ltd* [1939] 2 KB 206, 227. Although Baron makes no mention of this case, his ideas suggest that including implied duties of good faith with commercial contracts would not be so obvious that it 'goes without saying'.

54 Baron, above n 14, 78-81.

55 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 275.

56 Ibid.

57 Ibid.

have been implied to add 'a desirable improvement' to the contract.[58] In fact, overruling the express term agreed to by the parties in *Renard* contradicts the most basic principle in Australian contract law regarding implied terms; that principle postulates that courts imply terms in its traditional gap-filling role only where the implication is 'consistent with the actual terms of contract'.[59] Although it was suggested that express terms providing for the cancellation of a contract require such power to be exercised in a 'reasonable and honest state of satisfaction', enforcing this should not be via the 'implication of a further term'.[60] The application of what is reasonable should be determined in light of the 'express terms in the setting of the contract as a whole'.[61] Thus, acting in a manner of good faith may be forced into the contract if it is in 'accord with what is already standing' in the established contract. This is in contrast to the facts and ultimate decision in *Renard* where an express term was overruled by implying a duty of good faith. However, resolving *Renard* could have been accomplished in conjunction with Australian principles of contract law.

G. Alternative Resolutions in Renard

Other than Priestley JA, the remaining justices on the bench in *Renard* found solutions on grounds other than an implied duty of good faith. Notably, the views expressed by Meagher JA signify that an implied duty of good faith was not necessary to resolve the case in question. Meagher JA states where an act by a contracting party '[lacks] contractual justification',[62] then such should 'amount to a repudiation'[63] of the contact.

Similarly, an analysis of Handley JA's reasoning made clear that although aspects of well-enshrined common law principles of 'reasonableness' were present, no clear attempt was made to apply the US concept of good faith in contract.[64]

In essence, then, the majority in *Renard* (Priestley JA and Handley JA) arguably resolved the case with reference to the common law principle of 'reasonabless' in contract, with Meagher JA dissenting. The differing views on good faith in the case show that *Renard* should not be applied as precedent for good faith because it cannot make for clear and accurate law.

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58 *Poseidon Ltd v Adelaide Petroleum NL* (1991) 105 ALR 25, 44.
59 Seddon et al, above n 3, 30.
60 *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 117 ALR 393, 404.
61 Ibid, 404.
62 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 276.
63 Ibid, 276.
64 Ibid, 279.

These alternative solutions that could have been applied in *Renard* further display Priestley JA's inconsistency with United States case law. On appeal, the Wyoming Supreme Court reinforced the notion that:

> A breach of the covenant [of good faith and fair dealing] will generally be found only in cases involving egregious conduct that ordinary contract principles cannot remedy.[65]

Thus, as Meagher JA suggests, the ordinary and established contract principle of repudiation could have resolved the case. Also, discussions of the duty to act reasonably and with cooperation in contract in *Renard* suggest that such ordinary contract principles could have been used to remedy the alleged unfair conduct. Good faith was unnecessarily used given the abundance of alterative principles that could have been applied.

Therefore, such arguments show that the views in *Renard* should never have begun the idea of good faith that is currently being wrongly applied into many Australian contractual disputes.

H. Established Australian Law

Australian law contains concepts that ensure contracting parties act with cooperation and reasonableness; thus the incorporation of the concept of good faith into the Australian common law of contract is simply unnecessary. Specifically, acting fairly and justly with regard to contracting has legislative force in New South Wales[66] and to some extent, the Commonwealth.[67] In particular, s9(2)(c) of the *Contracts Review Act* 1980 (NSW) refers to whether it is practicable to reject a term of contract that seems unjust. In *Renard* the argument of good faith concerned whether it was unreasonable for the defendant to act as it did to terminate the agreement by virtue of the express provision of sub-clause 44.1 (which stated that the plaintiff could 'cancel the contract' if the defendant could not show 'cause … why [those] powers hereinafter should not be exercised').[68] In *Renard* the majority found that this was an unreasonable exercise of power,[69] however, no reference was made to the *Contracts Review Act* 1980 (NSW).

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65 *Worley v Wyoming Bottling Co.* 1.P3d 615 (Wyo, 2000), 656.

66 *Contracts Review Act* 1980 (NSW) s.9.

67 *Trade Practices Act* 1974 (Cth) pt IVA, V, VI; unconscionable conduct and consumer protection. Although not directly relating to 'fair dealing' in contracts, it nonetheless provides a framework where vitiating factors exist: See, Stewart, above n 51, 382.

68 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 234.

69 Ibid, see generally the judgments of Priestley and Handley JJA.

Such legislation is also complemented by common law principles that condemn conduct that is unjust or vitiating,[70] which, if made out, attract the remedy of rescission.[71] As such, where unjust acts exist in the formation of a contract, Australian law already provides the remedy to rescind the contract and excuse the aggrieved party from being obliged to partake in the contract as the existence of vitiating factors make the agreement void from the beginning.[72] Further, certain unfair practices in contract making also contravenes Australia statute.

Current paternalistic legislation such as the *Trade Practices Act* 1974 (Cth) and the *Contracts Review Act* 1980 (NSW) protects people from unjust conduct in commercial transactions. One of the main purposes of the *Trade Practices Act* 1974 (Cth) is to promote competition through provisions that make anti-competitive conduct illegal[73] as well as prohibit conduct that is unconscionable. In particular, the ever widening judicial application of unfair conduct by virtue of the *Trade Practices Act* 1974 (Cth) displays that a wide array contractors are adequately protected.[74]

It is commonly accepted that unconscionable conduct is shown by conduct that is taking 'unfair advantage … of serious inequality'.[75] However, more clearly, determining a breach of the *Trade Practices Act* 1974 (Cth), as an interpretation of *ACCC v No-Knead (Franchising) Pty Ltd*[76] suggests, is of 'no difficulty' when the conduct of the defendant is 'unreasonable, unfair, bullying and thuggish'.[77] Thus, a party who has been contractually outwitted or accepts a 'hard bargain'[78] cannot complain because the broad manner to which unconscionable conduct is applied to obvious acts of illegitimate pressure and unfairness displays that legitimately unfair conduct in contract making would be identified and dealt with under protective laws. Therefore, Griggs concludes that unconscionability 'is not to be

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70 *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 117 ALR 393, 401. Such as 'misrepresentation, presumed undue influence, or illegitimate pressure, or the like'.

71 Ibid, 406.

72 Seddon et al, above n 3, 33-7.

73 Philip Clarke, Stephen Corones, *Competition Law and Policy: Cases and Materials*, (2002), 82-3.

74 For instance, s.52 is not restricted to protecting 'consumers' only. However, one restriction is that misleading and deceptive conduct should generally occur in 'trade or commerce' for s.52 to take effect. See, *Concrete Constructions (NSW) Pty Ltd v Nelson* (1990) 169 CLR 594, 601, 605.

75 Ibid, 250.

76 (2000) 104 FCR 253.

77 Lynden Griggs, 'The Unconscionability Provisions of the Trade Practices Act 1974: Contrasting Judicial Developments', (2002) 9 *Competition and Consumer Law Journal* 241, 253.

78 In this context, it was stated by the Australian Federal Court that 'a distinction can be drawn between parties who adopt an opportunistic approach to strike a hard bargain and those who act unconscionably'. Ibid, 251.

read restrictively by way of confinement or nexus to the *Amadio* doctrine'.[79] It is to have a wider application, and, as the abovementioned cases show, judicial support for this opinion exists. Similarly, the *Contracts Review Act* 1980 (NSW) advances broad values of justice in contract making.[80]

In contrast, good faith in the United States is restricted in its application by the US judiciary.[81] In particular, Goren claims Texas, Pennsylvania and California have placed restrictions on the implication of good faith.[82] For example, in 2001, the Texas Court of Appeal stated:

> The duty of good faith exists only if intentionally created by express language in a contract or unless a special relationship of trust and confidence exists between the parties to the contract. The special relationship necessary to create such a duty … arises from an element of trust necessary to accomplish the contact, or has been imposed on the courts due to an imbalance of bargaining power.[83]

Therefore, good faith has been applied as a generic term to be implied only in cases of 'special relationship[s] of trust and confidence'. Further, if no such 'special relationship' exists then good faith will only be implied where its use is expressly provided for in the contract, or like unconscionability, if an 'imbalance of bargaining power' exists. The path of US good faith has thus taken a very different path from that universal application intended by Priestley JA.

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79 Ibid, 254. For those unfamiliar, Deane J states that unconscionability is satisfied where there is a 'special disability in dealing with the other party with the consequence that there was an absence of any reasonable degree of equality between them; and the disability was sufficiently evident to the stronger party. See, *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447, 474.

80 As noted by McHugh JA in *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610 at 710: 'The Contracts Review Act 1980 is revolutionary legislation whose evident purpose is to overcome the common law's failure to provide a comprehensive doctrinal framework to deal with 'unjust' contracts', cited in Griggs, above n 76, 244.

81 For example, the on appeal, the Supreme Court of Wyoming made specific restrictions to the application of good faith in employment contracts. As stated by Lehman CJ, 'A duty [of good faith] arises only where a special relationship of trust and reliance exists between the employer and the employee seeking recovery'. See: *Worley v Wyoming Bottling Co.* 1.P3d 615 (Wyo, 2000), 640.

82 Goren, above n 21, 296-300: although he criticizes such developments, it is nonetheless the law in these US jurisdictions. Also, some US jurisdictions have recognized that good faith is only to be implied as a generic term into cases of inequitable bargaining power.

83 *Re Marriage of Braddock* 64 S.W.3d (Tex. App. 2001), 586. Also, 'special relationship' 'such as that between an insured and his insurance carrier' has also been used to describe when an actionable duty of good faith will arise, *City of Midland v O'Bryant* 18 S.W.3d 209 (Tex. 2000) cited in Goren, above n 21 296.

The prohibition in the *Contracts Review Act* 1980 (NSW) against unjust conduct in contractual relations, together with the broad application of regulations within the *Trade Practices Act* 1974 (Cth), suggests that good faith is superfluous in preventing exploitation in Australian commercial practices. The widening scope of traditional Australian doctrines is much more effective than the narrowing and problematic US doctrine of good faith. This is especially so as the narrowing and diminishing application in the United States of the concept of good faith in contract law is an indicator of the direction that Australian good faith will pursue. In fact, this path towards restricting the application of good faith has already begun in Australia through the developments of 'legitimate commercial interests' in *Far Horizons* and good faith as a generic term in *Burger King,* discussed above.

Exploitation and unfair use of express contractual rights are unlikely to occur where both parties carefully scrutinize the express terms to which they ultimately agree. In the event that one of the parties does find such a term to be potentially hazardous, they are not forced to become legally bound. Simply, it is their own fault if they freely choose to be bound by unreasonable terms or broad terms that have the potential to confer a high degree of power on the other party. Significantly, Bigwood states that 'conscience does not operate simply to assist those who 'fail' the contractual game'.[84] In essence then, current doctrines of equity as well as paternalistic legislation preserve this idea of conscience while respecting the sanctity of contract. Ultimately, a harsh express term should not be considered to nullify a contract on grounds that it is in bad faith; this would merely reward the party who failed the 'contractual game'. Importantly then, current established Australian law already ensures that 'influence or power that each participant [of the market system] brings to a market interaction'[85] is not used improperly.[86] Therefore, current common law doctrines of equity in contract making and paternalistic legislation that regulate procedural deficiencies in contract making are sufficient to ward off exploitation and injustice. As such, it was unnecessary to introduce the concept of good faith into the Australian common law of contract in the interests of justice.

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84 Rick Bigwood, 'Conscience and Liberal Conception of Contract', (2000) 16 *Journal of Contract Law* 1, 11. Although, he also states that conscience 'does play an important role in defining the limits of the game itself'.

85 Charles Lindblom, *The Market System,* (2001), 187-8.

86 The ACCC states that 'being taken advantage of in a transaction in a way that offends the conscience is known as unconscionable conduct' therefore it is quite clear that those acts against 'conscience' warrant interfering with the sanctity of contract. Further, they advise that in order to avoid unfairness in contractual relations eventuating, contractors must take particular care to read the contract carefully and seek professional advice before making any agreement legally binding See: 'Unconscionable Conduct', Australian Competition and Consumer Commission <http://www.accc.gov.au/content/index.phtml/itemId/303748/fromItemId/6106> as at 01/08/04.

Democratic, Economic and Liberal Theories of Contract

Traditionally, Australians are a democratic people.[87] Plattner suggests that 'most people … today' class democracy and liberal democracy as the same thing.[88] Therefore, it is obvious that democratic people find freedoms to be of grave importance, specifically, those freedoms appertaining to liberal democracy. He goes on to say that 'the word liberal in the phrase liberal democracy refers not to a matter of who rules but how that rule is exercised'. [89] Foremost, Plattner states:

> The primacy of individual rights means that the protection of private sphere, along with the plurality and diversity of ends that people seek in their pursuit of happiness, is a key element of liberal political order.[90]

Therefore, private commercial negotiations freely agreed to by both parties should not be interfered with by legal authority.[91] Such interference – like the imposition of good faith in a privately formed contract – is a trespass of this 'private sphere' and so contravenes the liberal democratic right of Australian's to be free in their 'pursuit of happiness' – this may or may not include that common goal of profiteering.

Given that Australia is a liberal democracy, it incorporates the capitalist economic system.[92] As such, the democratic, economic and liberal schools of thought must be considered by the judiciary when formulating legal principles that may affect commercial dealings.

A. The Balance of Paternalism and Liberalism in Contract

Such liberalism in commercial dealings, however, promotes ideals of capitalist competitiveness, which attracts many rival opinions. In particular, critics of the

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87 For example, the preamble of the *Australian Citizenship Act* 1948 (Cth) states that anyone wanting to become a citizen of Australia must 'share … [the] democratic beliefs' of Australians. See: Tony Blackshield, George Williams, *Australian Constitutional Law and Theory,* (2002, 3rd ed.), 56.

88 Marc Plattner, 'Liberalism and Democracy: Can't have one without the other', (1998) 77(2) *Foreign Affairs* 171, 172.

89 Ibid.

90 Ibid.

91 In contrast, acting with unconscionable malicious intent in contractual dealings towards a weaker party – such as in duress, misrepresentation or unconscionability for example – deserves the attention and intervention of the state. These are acts against conscience and covered by the *Trade Practices Act* 1974 (Cth) as well as protective common law doctrines.

92 Capitalist economy is described as a 'role' in the success of democracy. See: Michael Novak, 'Democracy, Capitalism and Morality', (27/12/94) 224(124) *Wall Street Journal – Eastern Edition* 16, 16.

capitalist system cite reasons of inequality for being discontented with the economic model. Notably, capitalism has been quite commonly associated with exploitation.[93] Consequently, 'coercion in market relations because of inequality of position [within capitalist society is] … commonplace'.[94] Therefore, despite best efforts, unfairness and unconscionable conduct may at times be found within contractual formation. However, as shown, the ever broadening application of the *Trade Practices Act* 1974 (Cth)[95] as well as increasingly paternalistic legislative and common law frameworks in contract suggests that such exploitation in a capitalist market is severely reduced. Further, and most importantly, such legislation and common law doctrines of equity protect, whilst maintaining liberty throughout the life of the contract.[96] Given that the objectives of the *Trade Practices Act* 1974 (Cth) are to promote competition and restrict anti-competitive conduct,[97] liberal competition through paternalism is also achieved.[98] Therefore, it is important to balance the concepts of freedom of contract and liberty with other values that are in the interests of justice and fairness. Until the introduction of good faith however, this was highly achieved through paternalistic laws. Good faith has created an imbalance and is promoting simple fairness at the expense of liberal contracting and freedom to exercise ones expressed contractual rights. Hence, good faith serves no legitimate purpose and it is no surprise that its forced introduction into Australian law lacks the support of eminent legal figures.

B. The Socio-legal opinion

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93 Michael Novak, *The Spirit of Democratic Capitalism,* (1991), 31.

94 Lindblom, above n 94, 188: However 'coercion' of market position is dealt with under the common law principle of duress as well as statutory provisions such as the *Trade Practices Act* 1974 (Cth) as well the powers bestowed by the Australian Competition and Consumer Commission to investigate cases of unconscionable conduct, see: 'Unconscionable Conduct', Australian Competition and Consumer Commission <http://www.accc.gov.au/content/index.phtml/itemId/6106> as at 06/08/04.

95 For a general discussion, see: Griggs, above n 76, 246-257.

96 For example, the *Trade Practices Act* 1974 (Cth) Pt IV has 'enshrined' within in a 'policy of freedom of competition'. However, the courts will favour protecting rights under s.52 rather than allowing such 'freedom of competition' to prevail. This further exemplifies the protective nature of the Act thereby showing that good faith is unnecessary for protecting in relation to unfair commercial practices. See, *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 204-5.

97 The ACCC suggest that the *Trade Practices Act* 1974 (Cth) 'prohibits commercial conduct that substantially lessens competition in a market' as well as conduct that results with a misuse of market power or unfair practices such as 'third line forcing, boycotts, resale price maintenance … placing limitations on resellers' and exclusive dealing. See: 'Anti-Competitive Conduct and Restrictive Trade Practices', Australian Competition and Consumer Commission <http://www.accc.gov.au/content/index.phtml/itemId/259608/fromItemId/6106> as at 08/08/04.

98 Gibbs CJ has also stated that the outcome of Parts IV and V of the *Trade Practices Act* 1974 (Cth) is to protect competitors while enhancing competition. See: *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 204.

Within the socio-legal sphere, liberal contracting has been of fundamental significance in the preservation of justice and equitable treatment of litigants. As clearly stated in *Printing and Numerical Registering Co v Sampson,*[99] it is important for public policy reasons that 'men of full age and competent understanding'[100] are to have 'utmost liberty' in forming contracts, which, 'when entered into freely and voluntarily, shall be held as sacred and shall be enforced by the Courts of Justice'.[101] Therefore, where no vitiating factors exist and the requirement of capacity is satisfied, a contract should be a promise between two parties whose intentions are to gain what is promised by the other party, and should be enforced as such. Liberal contracting was reiterated in an Australian court where Rogers CJ stated that courts should not 'be eager to interfere' in commercial conduct of parties, especially when they are 'able to attend to their own interests'.[102] Thus, this concept is not outdated and so should be seriously considered when good faith seeks to strip the voluntarily accepted agreement formed by the parties of a contract.

As suggested in the classic case of *Dalrymple v Dalrymple,*[103] where parties have taken the time to provide consideration, 'it is said that [the contract] must be serious, so surely must all contracts' which must not be 'the sports of an idle hour and lack seriousness'.[104]

Therefore, such seriousness of contract should give rise to careful negotiations and protection of parties' best interests[105] where the pursuit of profits[106] should not be bound by a seemingly idealistic principle of good faith in commercial dealings. In fact, such extreme mothering of litigants via the imposition of good faith – in commercial dealings especially – would actually increase the possibility of carelessness in the formation of contract. Therefore, as succinctly put by many advocates of economic models of contracting, the law should not reward the careless contractor who places an avoidable burden on the economy.[107]

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99 (1875) LR 19 Eq 462 at 465 cited in Baron, above n 13, 75.

100 For example, contracting with a minor or intellectually impaired person will be invalid as they are not capable of defence or careful consideration of the terms to which they agree. See generally, Seddon, above n 3, 795-837.

101 *Printing and Numerical Registering Co v Sampson* (1875) LR 19 Eq 462, 465 cited in Baron, above n 14, 75.

102 *GSA Group Ltd v Siebe* (1993) 30 NSWLR 573, 579.

103 (1811) 161 ER 665.

104 Ibid.

105 Baron, above n 13, 75.

106 In fact, Meagher JA states that there 'is no reason why the principal should have any regard to any interests except his own', See; *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 275.

107 Michael J Trebilcock, 'An Introduction to Law and Economics', (1997) 23 *Monash University Law Review* 123, 142.

Furthermore, in *Biotechnology Australia Pty Ltd v Pace*[108] Kirby J states simply that the law of contract 'underpins the economy'[109] and thus capitalist ideals[110] and public interest should be held paramount in resolving contractual disputes. He goes on to state that contract law does not uniformly impose principles of fairness on litigants and insisted that 'it is the essence of entrepreneurship that parties will sometimes act with selfishness' .[111] Although conceding that the law would prefer honesty of dealings, it should not enforce a 'regime of fairness' on the majority of 'economic transactions' under contract law.[112] Therefore, for the interest of society and the economy as a whole, self-imposed contractual obligations must not 'entail the imposition of a conception of the good'.[113] This would simply reduce economic efficiency and defer use of resources from their most valuable and efficient economic uses;[114] affecting society and the economy negatively via the costs associated with litigation and lost productivity associated with less stable business transactions.[115]

Although some may find the pure capitalist and economic approach to contract draconian, on the contrary, however, the forceful application of good faith is in itself unfair. Parties of 'competent understanding' who expressly agree to particular terms should be bound by such terms and it would be unfair to deny them the benefit of such terms. The implication of good faith into such contracts overrules those express agreements, and, as no person with 'competent understanding' and sound mind[116] would expressly agree to terms which would treat them with bad faith, to imply a universal concept of good faith is not only unjust but unnecessary.

Conclusion

As shown, there had been no legal justification for Priestley JA to imply a term of good faith into the case of *Renard* – the case that began the idea of 'good faith' in Australia. Furthermore, the concept, lacking sufficient explanation within its jurisdiction of origin, is adequately covered by many established Australian legal

108 (1988) 15 NSWLR 130.
109 Ibid, 132.
110 Greed and selfishness are vital ingredients of capitalism. In capitalism, some profit at the expense of others, however this is at the benefit of total economic efficiency. To impose restrictions of the liberal rights of greed and selfishness would simply have a negative effect on economic efficiency and be unfair to society. See generally: John Stossel, 'In Defense of Greed', (Feb, 2004) 173(2) *Forbes* 36.
111 *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 133.
112 Ibid, 133.
113 Peter Benson (ed), *The Theory of Contract Law: New Essays*, (2001), 5.
114 Richard Craswell, 'Two Economic Theories of Enforcing Promises' in Peter Benson (ed), *The Theory of Contract Law: New Essays*, (2001), 19, 19-20
115 See Michael J Trebilcock, above n 106, 142-7.
116 In any case, the 'incompetent' and those of 'unsound mind' will not be legally capable of forming contractual relations: see generally, Seddon et al, above n 3, 795-837.

principles, and, its application contradicts basic philosophy underlying Anglo-Australian contract law. For these reasons, the concept of good faith in the common law of contract imported by Priestley JA from the United States should not be allowed to contaminate Australian law which has little need for the problematic doctrine.