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O come all ye faithful – the latest on good faith in English law

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Facts

Phones 4 U Limited ("P4U") entered into a contract with EE (a mobile network operator), which provided for P4U to act as a sales intermediary for EE (the "Contract").

Clause 13.11 of the Contract provided that:

> "*EE hereby undertakes and agrees with P4U that it will act in good faith and not carry out any activity designed to reduce or avoid the making of any Revenue Share Payment(s) to P4U as contemplated by this Agreement*"

Over a period, a number of the mobile networks within the UK notified P4U that they would be terminating their intermediary agreements with P4U, meaning that P4U's commercial position was very fragile.

On 12 September 2014, EE sent P4U a letter, stating that it would not be extending or renewing the Contract. This notification proved to be the straw which broke the proverbial camel's back and P4U subsequently entered into administration.

P4U argued that the issuance of this letter was in breach of an obligation of good faith, which EE was required to abide by, because EE had decided not to renew the Contract at the time the letter was sent, but sent it anyway, with the intention to drive P4U under.

An obligation of good faith under English Law

English law, unlike many other (particularly civil, but some common law) legal systems does not recognise a general duty of good faith. Parties are entitled to act in their own interests when performing contracts and are not required to take heed of the interests of their counterparts.

That notwithstanding - the "*sea of selfishness*" in English law, where contract law allows parties to act sharply and entirely in accordance with their own interests despite the impact this may have on other parties (provided they otherwise comply with the contractual requirements), contains an archipelago of good faith, with multiple distinct islands, where parties are constrained in how they can exercise their contractual rights. As Lord Hodge held in *Pakistan International Airline* v *Times Travel* [2021] UKSC 40, English law has "*relied on piecemeal solutions in response to demonstrated problems of unfairness*".

Insurance law

Under insurance law, the insured party is required to act "*uberrimae fidei*" (i.e. with the utmost good faith) and disclose any information known by them which might affect the decision of the insurer to offer insurance, even if not required by a contractual clause to provide such information (although most insurance contracts will expressly require such disclosure).

Breach of this obligation means that the insurance policy is voidable such that insurance contracts form the first of the islands within the archipelago of good faith.

An express obligation of good faith

Moving on to the second of the islands, English law recognises party autonomy and will generally give effect to their terms. Therefore, if parties agree to place themselves under an obligation of good faith, English law will recognise and give effect to this (although the exact scope of this duty may vary, see further below).

An implied obligation of good faith in relational contracts

As well as giving effect to express obligations, English law also gives effect to implied terms. An implied term must either be necessary to give business efficacy to the contract, or be so obvious that a reasonable onlooker would say "*of course*" such a term went without saying.

The genesis of the concept of a relational contract is typically ascribed to Leggat J (as he then was) in *Yam Seng* v *International Trade Corporation* [2013] EWHC 111 (QB), which concerned the operation of a long-term distributor agreement. Leggat J held that this agreement was "*relational*" and that, in such relational agreements, English law would be more willing to imply an obligation of good faith.

In *Bates* v *Post Office* [2019] EWHC 606 (QB), a part of the dispute between postmasters and the Post Office regarding the shortcomings in the Horizon IT system, which had resulted in a number of postmasters losing their jobs and/or going to prison, Fraser J set out a number of factors relevant to the determination of whether a contract is a relational one:

> "*2. The contract will be a* ***long-term*** *one, with the mutual intention of the parties being that there will be a long-term relationship.*
>
> *3. The parties must intend that their respective roles be performed with* ***integrity****, and with* ***fidelity to their bargain****.*
>
> *4. The parties will be* ***committed to collaborating*** *with one another in the performance of the contract.*
>
> *5. The spirits and objectives of their venture may* ***not be capable of being expressed exhaustively in a written contract****.*
>
> *6. They will each* ***repose trust and confidence in one another****, but of a different kind to that involved in fiduciary relationships.*
>
> *7. The contract in question will involve a h****igh degree of communication, co-operation and predictable performance*** *based on* ***mutual trust and confidence****, and* ***expectations of loyalty****.*
>
> *8. There may be a degree of* ***significant investment by one party (or both) in the venture****. This significant investment may be, in some cases, more accurately described as substantial financial commitment.*
>
> *9.* ***Exclusivity of the relationship*** *may also be present.*"

While these factors are not exclusive, and should not be slavishly used as a checklist, in light of the context sensitive nature of contractual interpretation, they offer a useful starting point for an analysis.

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What does an obligation of good faith entail?

Because English law does not recognise a general duty of good faith between contracting parties, but will give effect to a contractual term (either express or implied) requiring good faith, the content of the duty will fall to be decided by the scope of the term and so will vary from case to case.

That notwithstanding, there have been some useful indicators in the case law, where the courts have set out what such an obligation has required in specific circumstances, which give an idea as to what the duty entails.

In *Astor Management AG* v *Atalaya Mining Plc* [2019] EWHC 606 (QB) Leggat J emphasised that the obligation was "*a modest requirement ...* [which] *does no more than reflect the expectation that a contracting party will act honestly towards the other party and will not conduct itself in a way which is calculated to frustrate the purpose of the contract or which would be regarded as commercially unacceptable by reasonable and honest people*".

Cementing the limits of such an obligation, in *Gold Group Properties* v *BDW Trading* [2010] EWHC 1632 (TCC) it was found that an obligation of good faith did not require either party to give up valuable rights which they would otherwise have under the contract. Calver J in *Optimares* v *Qatar Airways Group* [2022] EWHC 2461 (Comm) similarly found that the obligation "*plainly does not*" apply to the exercise of a contractual right to terminate a contract for convenience.

The duty, where it does apply, is therefore not terribly demanding, in keeping with orthodox English law's sceptical view of such obligations.

Where the duty does bite, the Courts have generally used it to require a standard of honesty and "*up-front-ness*" – requiring the parties to place their cards on the table.

In *Yam Seng*, for example, Leggatt J suggested that one example of not acting in good faith would be deliberately not disclosing relevant information. In *Bates* as well, Fraser J, found that the Post Office was required to "*communicate, alternatively, not to conceal known problems, bugs or errors in or generated by*" the Horizon software and "*to disclose possible causes of apparent or alleged shortfalls (and the cause thereof) to Claimants candidly fully and frankly*".

This is not to say that this is necessarily the limit of the obligation – with Snowden LJ in *Re Compound Photonics Group* [2010] EWHC 1632 (TCC) emphasising that it is not English law that the duty is limited to the requirement to act honestly. As an illustration of this, the duty in *Bates* was also found to extend to not taking "*steps which would undermine the relationship of trust and confidence between Claimants and the Defendant*" and "*Not to exercise any discretion arbitrarily, capriciously or unreasonably*".

However, notwithstanding cases at the penumbra, it seems fair to say that the duty is generally a limited one and that the core instantiation of the obligation will typically involve an obligation of honesty and honest dealing.

Application to the facts in P4U

In the case of *P4U* v *EE* Roth J found that EE was not under any obligation of good faith, other than that expressly set out in Clause 13.11.

Firstly, the Court refused to find that Clause 13.11 imposed a general duty of good faith. While Clause 13 could, read extremely literally, be divided into two limbs as follows:

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> "*EE hereby undertakes and agrees with P4U that it will* [(1)] *act in good faith and* ([2]) *not carry out any activity designed to reduce or avoid the making of any Revenue Share Payment(s) to P4U as contemplated by this Agreement.*"

It was found that this was not plausible on the facts. The Contract had been professionally drafted, a general obligation of good faith could be expected to be set out more clearly and it was found to be "*inconceivable*" that such a duty would be placed upon EE, but not P4U (as P4U contended for).

Moving to consider whether an obligation of good faith could be implied, Roth J considered whether the Contract could be considered to be relational. While Roth J accepted that the Contract "*has some of the features of a relational contract*", being a long term agreement and one which required P4U and EE to "*collaborate with one another extensively in the performance*", the Court still found that it was not relational and there was no implied general duty of good faith upon EE.

The two main factors upon which the Court relied was the fact that the Contract was a lengthy document, prepared by lawyers, which attempted to comprehensively define the parties' obligations (unlike the short agreement in *Yam Seng*, which extended to only 8 pages and which was prepared without the assistance of lawyers). Where parties had comprehensively set out how they intended their bargain to operate there was simply no room for the court to interfere and imply a general duty of good faith.

Secondly, Roth J considered that it was a "*striking feature*" of the current case that EE was at all times in competition with P4U in seeking to supply its services to customers directly, without P4U acting as an intermediary. The 9th of Fraser J's elements from *Bates* was therefore not present and Roth J also considered that "*being in direct competition is a strong factor*" pointing *away* from finding that an agreement is relational.

As such, there was no basis upon which a general duty of good faith could be implied.

Finally, the Court also concluded that EE did not act in breach of any obligation of good faith when sending the letter notifying P4U that it would not be renewing the Contract – even if one could be implied. The court found that EE had decided not to renew the Contract with P4U at the time that the letter was sent, and there was no basis upon which it could be said that a duty of good faith required a party to *not* disclose relevant information (which would be in contradiction to Leggat's suggestion in *Yam Seng* that *non*-disclosure could constitute a breach of good faith).

Commentary

The Court's decision is surely correct in the circumstances, in light of the wary approach of English law to finding such an obligation, and reflects the English preference to allowing parties to define the scope of their own agreements, without the Courts helping out parties who transpire to have made poor bargains. See, for example, Lord Neuberger's emphasis in *Arnold* v *Britton* [2015] UKSC 36 that:

> "*It is not the function of a court when interpreting an agreement to relieve a party from the consequences of his imprudence or poor advice. Accordingly, when interpreting a contract a judge should avoid re-writing it in an attempt to assist an unwise party or to penalise an astute party*".

If you wish to ensure that your business partner is required to operate in good faith then you should therefore make sure that such an obligation, as well as the scope of such an obligation, is spelled out as precisely as possible within your contracts.

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Perhaps the most useful element of the decision, in terms of guidance for when a duty of good faith will be implied, is the clear guidance that it will be challenging to imply such a term where parties are in competition with one another.

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