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A Scottish-Canadian comparison

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# **The Principle of Good Faith in Contractual Performance: A Scottish-Canadian Comparison**

*Hector MacQueen\**

*Shannon O'Byrne\*\**

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## A. INTRODUCTION

Unlike Continental European legal systems, English common law traditionally does not recognise good faith as a general principle informing contracts. Instead, the preferred approach is to develop “piecemeal solutions in response to demonstrated problems of unfairness.”<sup>1</sup> Courts and academics alike have identified numerous objections to the good faith principle, including its encroachment on freedom of contract<sup>2</sup> and disregard of the law’s “strong ethos” of individualism.<sup>3</sup> It is said to produce commercial uncertainty;<sup>4</sup> undermine

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\*Hector MacQueen, Professor of Private Law, Edinburgh Law School

\*\*Shannon O’Byrne, Professor of Law, Faculty of Law, University of Alberta

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<sup>1</sup> *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] QB 433, 439 (Bingham LJ).

<sup>2</sup> *Bhasin v Hrynew*, 2014 SCC 71, [2014] 3 SCR 494 at para 39 [*Bhasin* SCC]

<sup>3</sup> E McKendrick, “Good Faith in Performance of a Contract in English Law”, in L A DiMatteo and M Hogg (eds), *Comparative Contract Law: British and American Perspectives* (2015) 196 at 202, referencing a criticism identified by Leggatt J in *Yam Seng Pte Ltd v International Trade Corp Ltd* [2013] EWHC 111(QB), [2013] 1 All ER (Comm) 1321.

<sup>4</sup> M Bridge, “Good Faith in Commercial Contracts”, in R Brownsword, N J Hird and G Howells (eds), *Good Faith in Contract: Concept and Context* (1999), 143; J M Thomson, “Good Faith in Contracting: A Sceptical View” in ADM Forte (ed), *Good Faith in Contract and Property Law* (1999) 63 at 64-65, *Bhasin* SCC at para 39, McKendrick (n 3) at 202.

existing contractual terms;<sup>5</sup> and promote “judicial moralism or palm tree justice.”<sup>6</sup> In a common law system, it amounts to a contagion from civil law jurisdictions.<sup>7</sup> In short, the good faith principle is “unworkable”.<sup>8</sup> In modern times Scots contract law has generally followed English law in denying the concept of good faith any particular significance outside certain particular forms of contract such as insurance, partnership, and agency.

Since 2013, however, the English judge Sir George Leggatt (now a Lord Justice in the Court of Appeal) has developed both judicially and extra-judicially an argument that English law can and does recognise an obligation of good faith performance by way of terms implied into contracts, either in the facts and circumstances of the particular case or in general in types of contracts.<sup>9</sup> In this argument he has especially highlighted long-term or “relational” contracts (including employment contracts) in which the parties have a relationship requiring extensive cooperation between the parties continuing over many years. In such a case the parties may need to show flexibility and a willingness to adapt their behaviour if their joint venture is to succeed. ... [The relationship] involves

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<sup>5</sup> *MSC Mediterranean Shipping Company SA v Cottonex Anstalt* [2016] EWCA Civ 789 at para 45 identifies this as a “real danger.” See too *Bhasin SCC* at para 39.

<sup>6</sup> *Bhasin SCC* at para 70.

<sup>7</sup> See G Teubner, “Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences” (1998) 61 MLR 11.

<sup>8</sup> *Walford v Miles* [1992] 2 AC 128, 138 (Lord Ackner).

<sup>9</sup> See *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB), [2013] 1 All ER (Comm) 1321 at paras 120-153; Mr Justice Leggatt, “Contractual Duties of Good Faith”, lecture to the Commercial Bar Association 18 October 2016, available at <https://www.judiciary.uk/wp-content/uploads/2016/10/mr-justice-leggatt-lecture-contractual-duties-of-faith.pdf>; *Astor Management AG v Atalaya Minn Plc* [2017] EWHC 425 (Comm); [2017] 1 Lloyd’s Rep. 476, para 98; *Al Neyahan v Kent* [2018] EWHC 333 (Comm) at paras 167-176; Sir George Leggatt, “Negotiation in Good Faith: Adapting to Changing Circumstances in Contracts and English Contract Law”, Jill Poole Memorial Lecture, delivered at Aston University 19 October 2018, available at <https://www.judiciary.uk/wp-content/uploads/2018/10/leggatt-jill-poole-memorial-lecture-2018.pdf>.

expectations of cooperation and loyalty which are not (and perhaps cannot be) completely expressed in a formal document.<sup>10</sup>

But the obligation does not govern the negotiation and formation of contracts, since it arises only where there is a contract. Nor does it require a party to set another's interests above its own, and it is not capable of over-riding express contract terms. The concept can regulate the exercise of contractually conferred discretionary powers, however, with Sir George arguing that there is now an implication of law that such discretions will be exercised honestly and in good faith, not arbitrarily, capriciously or unreasonably.<sup>11</sup>

These arguments are of course controversial, and have not yet received the seal of approval from appellate courts.<sup>12</sup> The academic response in the UK has also been variable, not least with regard to the use of the idea of relational contracts. While Hugh Collins has identified distinguishing features by which a relational contract might be given specific legal definition and effects (not necessarily including a good faith performance rule), others have tended to agree with the US scholar Melvin Eisenberg that “the general principles of contract law can and should be formulated to be responsive to relational as well as discrete contracts.”<sup>13</sup> But there has been significant movement in other jurisdictions which had

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<sup>10</sup> Leggatt, “Contractual Duties of Good Faith” (n 9) at para 28. As Leggatt acknowledges, the term ‘relational contract’ is usually associated with the work of US scholar Ian Macneil (for which see D Campbell (ed), *The Relational Theory of Contract: Selected Works of Ian Macneil* (2001)).

<sup>11</sup> Leggatt, “Contractual Duties of Good Faith” (n 9), paras 44-56.

<sup>12</sup> For lack of approval at Court of Appeal level see *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200; *MSC Mediterranean Shipping Company SA v Cottonex Anstalt* (n 5). For first instance cases applying the Leggatt approach see *British Groundschool Ltd v Intelligent Data Capture Ltd* [2014] EWHC 2145 (Ch); *D&G Cars Ltd v Essex Police Authority* [2015] EWHC 226 (QB).

<sup>13</sup> See H Collins, “Is a Relational Contract a Legal Concept?” in S Degeling et al (eds), *Contract in Commercial Law* (2017) 37-59; M A Eisenberg, “Relational Contracts”, in J Beatson and D Friedmann (eds) *Good Faith and Fault in Contract Law* (1995) 291-304 (quotation at 304). For other discussion in UK publications of Macneil’s (and, latterly, Leggatt’s) concepts of relational contracts, see E McKendrick, “The Regulation of Long-term Contracts in English Law”, also in Beatson and Friedmann, *Good Faith and Fault*, 305-333;

hitherto generally followed the traditional English approach.<sup>14</sup> In particular, the Supreme Court of Canada (SCC) in *Bhasin v Hrynew* in 2014 broke with the past and formally acknowledged good faith as a general organising principle of contractual performance at common law. After a multi-jurisdictional survey, the court rejected English recalcitrance and, instead, concluded that recognising a good faith principle makes “the common law less unsettled and piecemeal, more coherent and just”.<sup>15</sup> *Bhasin*’s other remarkable contribution is to recognise, for the first time, a general duty of honesty in contractual performance which is derived from the good faith principle. This duty means, as the SCC explains, “simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract”.<sup>16</sup>

The purpose of this article is to assess what Scots law can learn from Canadian law on good faith. Part B begins with Canadian law, providing an overview of *Bhasin* and briefly describing the new principle of good faith. Several post-*Bhasin* cases concerning implied terms and contractual discretion (areas in which the good faith principle has considerable presence) are analysed and the new duty of honesty explored. Part C considers the failure of the Scottish courts to develop “the broad principle in the field of contract law of fair dealing in good faith” identified by the House of Lords in 1997,<sup>17</sup> while also noting the incoherent use of “equitable” controls (which may be seen as good faith in disguise) available in remedies for breach of contract. Part D assesses the difference between the current Canadian and the Scottish positions, appraising the extent to which recognition of a general good faith

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D Campbell, “Good Faith and the Ubiquity of the ‘Relational’ Contract” (2014) 77 MLR 475; H Beale, “Relational Values in English Contract Law”, in D Campbell et al (eds), *Changing Concepts of Contract: Essays in Honour of Ian Macneil* (2013, pbk 2016), 116-137; D Campbell, “Adam Smith and the Social Foundation of Agreement” (2017) 21 Edin LR 376; S Saintier, “The Elusive Notion of Good Faith in the Performance of a Contract: Why Still a Bête Noire for the Civil Law and the Common Law?”, [2017] JBL 441.

<sup>14</sup> See e.g. on developments in Australia and Singapore (as well as Canada) J M Paterson, “Good Faith Duties in Contract Performance”, (2014) 14 *Oxford University Commonwealth Law Journal* 283, DOI: 10.1080/14729342.2015.1047655.

<sup>15</sup> *Bhasin* SCC at para 33.

<sup>16</sup> *Ibid* at para 73.

<sup>17</sup> *Smith v Bank of Scotland* 1997 SC (HL) 111, 121 (Lord Clyde).

principle can make the law more coherent and responsive to real problems while also requiring appropriate safeguards against excessive judicial empowerment to be put in place. *Bhasin* may provide inspiration here, although change in the Scottish courts' approach seems unlikely unless and until the English courts do so too.

## B. CANADIAN LAW

### (1) *Bhasin v Hrynew*: An Overview

The plaintiff, Mr Bhasin, and the defendant, Canadian American Financial Corp (Can-Am) were parties to a commercial dealership agreement whereby Bhasin's agency sold Can-Am's education savings plans to investors. The non-renewal clause provided that either party could terminate their contract on six months' notice upon expiry of the first three-year period. When a Bhasin competitor, Mr Hrynew, joined Can-Am, he pressured Can-Am to force a merger with Bhasin. Can-Am complied, triggering its non-renewal clause by giving Bhasin proper notice of termination and then merging Bhasin's agency with Hrynew's. Bhasin sued, *inter alia*, for breach of contract.<sup>18</sup> Notwithstanding an entire agreement clause which would generally operate to prevent the court from implying terms in this case,<sup>19</sup> the trial judge implied a term that Can-Am could only trigger the non-renewal clause for good faith reasons.<sup>20</sup> Though recognising that implying such a term was contrary to the entire agreement clause at bar, the court ruled that the clause was of no effect since Can-Am had exercised its non-renewal power "unfairly or abusively",<sup>21</sup> Bhasin was not sophisticated,<sup>22</sup> and it would be unjust or inequitable to allow Can-Am to rely on the non-renewal clause as written.<sup>23</sup> The trial judge also went on to find that Can-Am had breached an implied term of good faith on various occasions, including when it acted dishonestly in not advising Bhasin that a merger

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<sup>18</sup> *Bhasin v Hrynew*, 2011 ABQB 637 at para 47, [2012] 9 WWR7 [*Bhasin* QB].

<sup>19</sup> The entire agreement clause was as follows: "This Agreement expresses the entire and final agreement between the parties hereto and supersedes all previous agreements between the parties. There are no representations, warranties, terms, conditions or collateral agreements, express, implied or statutory, other than expressly set out in this Agreement." See *Bhasin* QB at para 110.

<sup>20</sup> *Ibid* at para 104.

<sup>21</sup> *Ibid* at paras 117, 118.

<sup>22</sup> *Ibid* at para 115.

<sup>23</sup> *Ibid* at paras 117-118. See also paras 246-247.

decision had been taken<sup>24</sup> and “equivocated” in response to Bhasin’s question as to whether a merger of the agencies would take place.<sup>25</sup> She awarded over \$380,000 in damages for, *inter alia*, loss of income and business.<sup>26</sup>

On appeal, the trial decision was reversed in its entirety. The court concluded that a good faith term could not be implied because it would conflict with an express term; violate the parol evidence rule;<sup>27</sup> and be contrary to the entire agreement clause.<sup>28</sup> On a related front, the lower court’s determination that the contract could only be terminated for good faith reasons “flatly” contradicted the words of the non-renewal clause.<sup>29</sup>

On further appeal, the SCC found for Bhasin but on entirely new grounds. It identified, for the first time, the good faith principle informing contractual performance and explained how Can-Am was in breach of the new duty of honesty that underlies all contracts. These matters are discussed in more detail below.

## **(2) Bhasin’s Good Faith Principle: Reasonableness and Honesty**

According to the SCC, Canada’s good faith principle states that parties must generally perform their contracts “honestly and reasonably and not capriciously or arbitrarily”.<sup>30</sup> It noted that the principle reflects “the notion that, in carrying out his or her own performance of the contract, a contracting party should have appropriate regard to the legitimate contractual interests of the contracting partner.”<sup>31</sup> This, in turn, “merely requires that a party not seek to undermine those interests in bad faith”.<sup>32</sup> Beyond this, “appropriate regard” is cast as a variable whose meaning is contextual and tied to the relationship or situation at bar.<sup>33</sup>

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<sup>24</sup> Ibid at paras 258 and 260.

<sup>25</sup> Ibid at para 247 and as emphasised by *Bhasin* (SCC) at para 100.

<sup>26</sup> *Bhasin* QB at para 527.

<sup>27</sup> Unlike in Scotland, the Canadian spelling of ‘parol’ does not include an ‘e’ at the end of the word.

<sup>28</sup> *Bhasin v Hrynew* 2013 ABCA 98, 362 DLR (4<sup>th</sup>) 18 at paras 29-30 [*Bhasin* CA].

<sup>29</sup> *Bhasin* CA at para 33.

<sup>30</sup> *Bhasin* SCC, para 63.

<sup>31</sup> Ibid at para 65.

<sup>32</sup> Ibid.

<sup>33</sup> Ibid.



Having referred amongst many other sources to Sir George Leggatt's views on good faith in English law, the SCC remarked:

Good faith may be invoked in widely varying contexts and this calls for a highly context-specific understanding of what honesty and reasonableness in performance require so as to give appropriate consideration to the legitimate interests of both contracting parties. For example, the general organising principle of good faith would likely have different implications in the context of a long-term contract of mutual cooperation than it would in a more transactional exchange ...<sup>34</sup>

The good faith principle does not, on its own, operate as a contractual term, implied or otherwise, or found any cause of action.<sup>35</sup> Rather, the principle is a *standard*, underpinning, uniting, and organising those aspects of contract law which, as described by the SCC, require “honest, candid, forthright or reasonable contractual performance”.<sup>36</sup> For example, the good faith principle is the source of the long-standing doctrine of unconscionability because it expressly considers “the fairness of contractual bargains”.<sup>37</sup> As another example, the good faith principle can be a basis for implying contractual terms that regulate the defendant's freedom of action.<sup>38</sup>

The good faith principle has a twofold purpose. First, it is the source of and justification for certain existing contract rules or elements.<sup>39</sup> Second, it is the foundation for the judicial promulgation of new contract rules or elements, albeit on a cautious, restrained, incremental and precedent-respecting basis.<sup>40</sup> As a post-*Bhasin* court has observed, *Bhasin* is

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<sup>34</sup> Ibid at para 69. For reference to Sir George Leggatt, see *ibid* at para 57.

<sup>35</sup> See *McDonald v Brookfield Asset Management*, 2016 ABCA 375 at para 57.

<sup>36</sup> *Bhasin* SCC at para 66.

<sup>37</sup> Ibid at para 43. See J D McCamus, *The Law of Contracts*, 2<sup>nd</sup> edn (2012) 426 as to when a contract can be set aside for unconscionability.

<sup>38</sup> *Bhasin* SCC at para 44.

<sup>39</sup> Ibid at para 33.

<sup>40</sup> Ibid at para 66.

not to lead to “the creation from whole cloth” of contractual obligations “which the parties have not provided for or have addressed in a fashion which one party regrets in hindsight”.<sup>41</sup>

### **(3) Good Faith as Reasonableness**

Though the line between honesty and reasonableness in the good faith principle is not airtight, neither are they synonyms. This is particularly so given that reasonableness incorporates the idea of honesty but not necessarily the other way around. Accordingly, sometimes contract rules or elements are emanations of the higher, *reasonableness* standard associated with the principle of good faith – such as the implication of contractual terms by operation of law, as discussed below. At other times, the emanation is from the lower, *honesty* standard associated with the principle of good faith. For example, when an employer terminates an employee’s contract, Canadian law requires that the manner of dismissal – how the employee is treated at the time of discharge – meets a good faith standard, with honesty being a “key component” according to the SCC in *Bhasin*.<sup>42</sup>

While the *Bhasin* decision is complex and its articulation of the good faith principle broad, manifestations of the principle are reasonably easy to pin down. In relation to *reasonableness*, the good faith principle largely denotes good faith as a contractual term. More specifically, in certain kinds of contracts (unhelpfully described as “types of relationships” by the court), good faith is a term implied by operation of law. In these specific kinds of contracts, a good faith term is a legal incident recognised, not based on the parties’ contractual intent but, as Professor John McCamus notes, “to ensure that the agreement between the parties is, in the court’s view, a fair and reasonable one”.<sup>43</sup> *Bhasin* offers the following list of contracts where parties are bound by a good faith term: employment,<sup>44</sup>

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<sup>41</sup> *Addison Chevrolet Buick GMC Ltd v General Motors of Canada Ltd*, 2015 ONSC 3404 at para 119, reversed on other grounds (2016) ONCA 324 and cited by several courts including *Angus Partnership Inc v Salvation Army (Governing Council)*, 2018 ABCA 206 at para 71.

<sup>42</sup> *Bhasin* SCC at para 73.

<sup>43</sup> McCamus, *Contracts* (n 37) 775.

<sup>44</sup> *Bhasin* SCC at para 44.

insurance,<sup>45</sup> landlord-lessee,<sup>46</sup> and franchise.<sup>47</sup> Additionally, good faith “will generally be implied in fact” in the tendering context.<sup>48</sup>

A good faith term can also be implied in fact, following the officious bystander and business efficacy tests.<sup>49</sup> That is, courts are to deploy the principles of contractual interpretation and, as observed in *Bhasin*, “give effect to the intentions of the parties at the time of the contract formation”.<sup>50</sup> The good faith principle supports the interpretive content of this exercise because, as the court observes, parties “may generally be assumed to intend certain minimum standards of conduct”.<sup>51</sup> But the matter nonetheless comes down to contractual intention in the specific instance. Furthermore, the exercise of implying terms in fact turns on the presumed intentions of the parties as understood in a very limited way. Courts are to imply a given term only if it is necessary or is “in some sense, obvious from the circumstances of the particular transaction”<sup>52</sup> and only when to do so does not contradict an express term.<sup>53</sup> With these ground-rules in mind, a good faith term implied in fact exists because the parties have implicitly chosen that term for themselves.

Hence, when courts talk about a party owing a good faith *duty* in this context, properly speaking, they are generally referring to a good faith *term* based on principles of contractual interpretation.<sup>54</sup> As understood by the SCC, the duty of good faith does not operate as an actionable, abstract presence. Rather, the duty of good faith raises a term<sup>55</sup> – whether implied in fact or implied by law. The conclusion is also confirmed by Karakatsanis

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<sup>45</sup> Ibid.

<sup>46</sup> Ibid.

<sup>47</sup> Ibid at para 23.

<sup>48</sup> Ibid at 56.

<sup>49</sup> Ibid at para 48 and 50. See, for example, *MJB Enterprises Ltd v Defence Construction (1951) Ltd* [1999] 1 SCR 619 at 635, 1999 CanLII 677 (SCC).

<sup>50</sup> *Bhasin* SCC at para 45.

<sup>51</sup> Ibid.

<sup>52</sup> McCamus, *Contracts* (n 37) 774.

<sup>53</sup> Ibid.

<sup>54</sup> This statement should be read subject to *Bhasin*’s creation of the duty of honesty discussed *infra*.

<sup>55</sup> *Bhasin* SCC at para 74.

JA (as she then was) in a pre-*Bhasin* decision which still appears to state the law: “In order for a claim for a breach of a duty of good faith to survive, such a duty must be an express or implied term of the contract and there must be a tenable cause of action for breach of contract”.<sup>56</sup>

The good faith principle is also the source of contractual doctrines, including those going to implied terms.<sup>57</sup> But the principle itself cannot directly insert content into a contract because, as the court in *Bhasin* emphasised, the good faith principle is “not a free-standing rule”.<sup>58</sup> Taking a particularly firm position on this point, a majority of the Alberta Court of Appeal stated as follows:

The principles set out in *Bhasin* (and any extension of it) do not enable either party to insist on covenants and provisos that are not set out in writing in the agreement, nor do they allow the parties to ignore the plain wording of the agreement ... [nor insert] provisions inconsistent with the actual terms of the contract.<sup>59</sup>

In short, the *Bhasin* principle of good faith does not change the fundamentals of contract law. It merely explains and moors them.

But with all that said, a momentous and even startling 2018 decision from the influential Ontario Court of Appeal follows a contrary path by seeming to regard good faith as a free-standing rule. In *Mohamed v Information Systems Architects Inc*,<sup>60</sup> at issue was whether the defendant, Information Systems Architects Inc (ISA), had an unfettered power to terminate its contract with the plaintiff, Mohamed, or was required to exercise that power in good faith. Mohamed, described in the contract as an independent contractor, was assigned to provide technological services to one of ISA’s customers, Canadian Tire Corporation (Canadian Tire) in 2015. Soon thereafter, Canadian Tire asked that the plaintiff be replaced when it learned that Mohamed had been convicted of assault with a weapon some 15 years

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<sup>56</sup> See *Jaffer v York University*, 2010 ONCA 654 at para 49. What a court means by the duty of good faith is context specific, of course.

<sup>57</sup> *Bhasin* SCC at para 44.

<sup>58</sup> *Ibid* 64.

<sup>59</sup> *Styles v Alberta Investment Management Corporation*, 2017 ABCA 1 at para 64, leave to appeal to SCC dismissed, [2017] SCCA No 76.

<sup>60</sup> *Mohamed v Information Systems Architects Inc*, 2018 ONCA 428 [*Mohamed* CA].

previously and while in high school.<sup>61</sup> Note that Mohamed had been entirely open with ISA, having advised ISA of his criminal record in advance of signing the contract with them.<sup>62</sup> But in light of Canadian Tire's concern, ISA replaced Mohamed and chose to rely on that action as grounds to terminate his contract altogether. ISA invoked Clause 11 of their contract which provided for the contract to end when, *inter alia*, "ISA determines that it is in ISA's best interest to replace the Consultant for any reason."<sup>63</sup>

The appellate court affirmed the motion judge's finding that ISA was bound by a good faith standard when electing to terminate, stating that the judge below had accepted evidence of Mohamed's "understanding" that there would be "an element of good faith in the exercise of the provision by the appellant, and found that this understanding was supported by the law from the *Bhasin* decision of the Supreme Court."<sup>64</sup> Most significantly, the appellate court went on to state:

... although the appellant had a facially unfettered right to terminate the contract, it had an obligation to perform the contract in good faith and therefore to exercise its right to terminate the contract only in good faith.<sup>65</sup>

ISA, in turn, was in breach of this obligation for failing to make efforts "to secure Canadian Tire's agreement to the respondent continuing on the project" and not offering Mohamed the chance to work on another consulting project.<sup>66</sup> Mohamed was awarded damages represented by the balance owed under his fixed term contract.<sup>67</sup>

*Stare decisis* dictates that for Mohamed's "understanding" to be enforceable, it must somehow form part of the contract. On the facts, his understanding could not be imported as an implied-in-fact term because that would be inconsistent with the intention of ISA, was not necessary in the sense of being obvious, and would contradict an express term. Beyond this,

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<sup>61</sup> *Mohamed v Information Systems Architects Inc* 2017 ONSC 5708 para 1 [*Mohamed* SC].

<sup>62</sup> *Mohamed* CA at para 2.

<sup>63</sup> *Ibid.*

<sup>64</sup> *Ibid* at para 17.

<sup>65</sup> *Ibid* at para 18 ("facially" here meaning, "on the face of the contract").

<sup>66</sup> *Ibid* at para 19.

<sup>67</sup> *Ibid* at 30.

the contract contained an entire agreement clause,<sup>68</sup> though the appellate court was entirely silent on its import. But regardless of the reason, neither level of court raised the possibility of implying a term. While there is precedent for treating a contractual *discretion* clause as embodying a good faith standard (as discussed below), these cases were not raised by the courts either. This is likely due to the SCC's finding in *Bhasin* that a termination clause is not properly regarded as a discretion clause importing good faith.<sup>69</sup> It would seem that faced with closed doors, the motions judge and appellate court have taken the novel step of imposing a good faith standard as an at-large, free-standing requirement such that Mohamed's understanding of when the clause would be deployed was accorded legal consequences. *Bhasin* emphasises that good faith claims will generally not succeed unless they fit with existing doctrine,<sup>70</sup> but does expressly instruct lower courts to develop, on rare occasions, the good faith principle incrementally "where existing law is found to be wanting".<sup>71</sup> If incremental change was the path that the appellate court was travelling, it really should have expressly identified itself as doing so. As it stands, the decision proceeds with no recognition of or accounting for its novelty. Even in a subsequent decision distinguishing *Mohamed*, the Court of Appeal does not explain itself.<sup>72</sup>

It is difficult to accept *Mohamed* as an accurate application of the law as traditionally understood. Instead, and as good faith sceptics have worried would happen post-*Bhasin*, the Ontario Court of Appeal essentially rewrote the contract to assist a sympathetic plaintiff whose high school criminal record was 15 years in the past and whose treatment at the hands of ISA was perhaps less than equitable. The court's rewriting, however well intentioned, comes at a price. This includes murkiness over exactly *why* it did not enforce the contract as written (including the express allocation of risk of summary termination onto the independent contractor); when future courts should impose the good faith standard on the exercise of an

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<sup>68</sup> *Mohamed* (SC) at para 10: "This Agreement contains the entire agreement between the parties. No change or modification of this Agreement shall be valid unless it be in writing and signed by both parties".

<sup>69</sup> *Bhasin* SCC 71 at para 72. See too discussion below, text accompanying nn 74-84.

<sup>70</sup> *Bhasin* SCC at para 66.

<sup>71</sup> *Ibid.*

<sup>72</sup> The Court of Appeal in *CM Callow Inc v Zollinger* 2018 ONCA 896 judicially considered *Mohamed* but tersely and without expansion, at para 20.

express contractual power; and how to approach the question of whether the good faith standard has been fulfilled or not.

Returning to *Bhasin*'s assessment of when a good faith term should be implied under the reasonableness arm, the SCC invokes the influential lead of McCamus, who identifies three "situations" on this front:

- (1) where the parties must cooperate in order to achieve the objects of the contract [such as where the court implies a term that the vendor must take all reasonable steps to complete the subject sale, at para 49];
- (2) where one party exercises a discretionary power under the contract [for example, in setting a price]; and
- (3) where one party seeks to evade contractual duties [as when a party relies on a contractual power to repudiate but based on circumstances he has himself created].<sup>73</sup>

For example, the law in relation to situation (2) gives a nod to contractual intention<sup>74</sup> but essentially starts with a presumption that contractual discretions will be exercised reasonably,<sup>75</sup> honestly, and in good faith.<sup>76</sup> This judicial approach amounts to a much stronger affirmation of the good faith principle than the simple implication of terms discussed previously. In short, courts will implicitly recognise<sup>77</sup> a reasonableness standard in the discretion clause absent explicit language to the contrary or "a clear indication from the tenor of the contract or the nature of the subject matter".<sup>78</sup> The presumption in these cases tilts strongly towards good faith by requiring the other side to dislodge it and by permitting judicial review of *how* the contractual discretion is exercised.

Accordingly, whether the clause in question goes to a discretion or not is an important battleground. For example, at issue in *Styles v Alberta Investment Management*

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<sup>73</sup> *Bhasin* SCC at para 47.

<sup>74</sup> *Greenberg v Meffert* (1985) 50 O.R. (2d) 755, 1985 CanLII 1975 (ON CA) at 762, leave to appeal dismissed 1985 CanLII 114 (SCC).

<sup>75</sup> *Ibid* at 764. See too *Filice v Complex Services Inc* 2018 ONCA 625 para 38, citing *Greenberg* on this point.

<sup>76</sup> *Greenberg* at 764.

<sup>77</sup> McCamus, *Contract* (n 37) 849.

<sup>78</sup> *Greenberg* at 762.

*Corporation*,<sup>79</sup> was whether the plaintiff was entitled to a bonus when he had not met the express vesting conditions specified in the contract. The trial judge ruled in his favour, concluding that the employer had a discretion to award the bonus or not and furthermore, that such a discretion had to be exercised in good faith.<sup>80</sup> A majority of the Court of Appeal reversed on several grounds, including because the subject contract did not actually even contain a discretion clause. As the majority stated, while it is true that one party (here, the employer) can decide against insisting on the strict written terms of a contract (that is, award a bonus even though it has not vested), such a waiver “is not ‘discretion’ in performance granted by the contract”.<sup>81</sup> The court continued:

‘Giving up rights’ is not properly described as a ‘discretion’, much less one that can be reviewed by the court; the court cannot require one party to give up its contractual rights under the guise of regulating the exercise of a discretion: *Bhasin* at para 73.<sup>82</sup>

The majority went on to rule that the contract “left no doubt”<sup>83</sup> that the plaintiff was ineligible for a bonus, adding that “*Bhasin* does not permit the respondent to simply ignore that provision in the contract because he wishes, with hindsight, that he had made a different bargain”.<sup>84</sup>

The trial level decision in *Styles* mentioned above is one that would cause concern to good faith sceptics. This is because, *inter alia*, the trial judge disregarded an express term in favour of holding the defendant to a good faith standard. More specifically, the trial judge held that the defendant had a discretion to award the plaintiff an unvested bonus but recognised that the entire agreement clause would otherwise prevent her from importing a good faith obligation.<sup>85</sup> As a work-around, the trial judge relied on *Bhasin*’s statement that,

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<sup>79</sup> *Styles v Alberta Investment Management Corporation*, 2017 ABCA 1, 408 DLR (4th) 725 [Styles CA], leave to appeal to the SCC dismissed [2017] SCCA No 36.

<sup>80</sup> *Styles v Alberta Investment Management Corporation*, 2015 ABQB 621, [2016] 4 WWR 593 para 130 [Styles QB].

<sup>81</sup> *Styles* CA at para 29.

<sup>82</sup> *Ibid.*

<sup>83</sup> *Styles* CA at para 6.

<sup>84</sup> *Styles* CA at para 64. See *Bhasin* SCC at para 72 for discussion of what counts as a discretion.

<sup>85</sup> *Styles* QB at para 55.



albeit rarely, the “application of the organising principle of good faith to particular situations should be developed where the existing law is found to be wanting.”<sup>86</sup> The trial judge then proceeded to find a *new* duty which apparently *requires* good faith in the exercise of contractual discretion (as an emanation of the *Bhasin* principle),<sup>87</sup> which duty cannot be excluded by an entire agreement clause.<sup>88</sup> In short, the court went well beyond the discretion cases recognised by *Bhasin* – which functionally regards good faith as presumption which *can* be disclaimed – to casting a new duty of good faith in the exercise of discretionary powers that *cannot* be.

On appeal, this innovation was thoroughly rejected for being inconsistent with *Bhasin*. According to the appellate court: “*Bhasin* is not to be used as a tool to rewrite contracts, and award damages to contracting parties that the court regards as being ‘fair’, even though they are clearly unearned under the contract.”<sup>89</sup> It should be emphasised, though, that the appellate court was not challenging the discretion cases recognised in *Bhasin* but the trial judge’s radical expansion of those cases from one identifying good faith as default standard to one which apparently posits good faith an invariable and mandatory one. Like *Mohamed* discussed earlier, it would seem that the trial judge was intent on assisting a party whom she regarded as meritorious but unfairly shut out of a bonus by the strict terms of the contract.

#### **(4) Good Faith as Honesty**

This section turns briefly to the honesty arm of the good faith principle and in particular, the SCC’s recognition of the new duty of honesty which informs all contracts. As previously noted, this duty is a “simple requirement not to lie or mislead the other party about one’s contractual performance”.<sup>90</sup> *Bhasin*’s rationale for such a duty is as follows:

Commercial parties reasonably expect a basic level of honesty and good faith in contractual dealings. While they remain at arm’s length and are not subject to the

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<sup>86</sup> Ibid para 62, quoting *Oracle* which was quoting *Bhasin* SCC.

<sup>87</sup> Ibid at 63.

<sup>88</sup> Ibid at para 64.

<sup>89</sup> *Styles* CA at para 54.

<sup>90</sup> *Bhasin* SCC at para 73.

duties of a fiduciary, a basic level of honest conduct is necessary to the proper functioning of commerce....<sup>91</sup>

While breach of the duty of honesty is independently actionable, the court insists that it is *not* an implied contractual term<sup>92</sup> nor is it a tort, for that matter. Rather, the duty of honesty is a hybrid on several fronts. Looking at it from the perspective of contract law, the duty of honesty is *like* the doctrine of unconscionability because it inures in all contracts<sup>93</sup> and cannot be broadly disclaimed.<sup>94</sup> Yet it is like a *term* because its violation is subject to a contractual measure of damages, not the rescissionary remedy associated with unconscionability.<sup>95</sup> From the perspective of tort law, the duty of honesty is *like* the tort of fraudulent misrepresentation (as the court readily acknowledges<sup>96</sup>) since it ordinarily involves a false statement; but it is distinct because, in the SCC's words, it does not require that the defendant "intend that the false statement be relied on, and breach of it supports a claim for damages according to the contractual rather than the tortious measure".<sup>97</sup> Entire agreement clauses would not generally impact on the duty because, like unconscionability, it cannot be excluded.<sup>98</sup> However, parties are entitled to "relax the requirements of the doctrine so long as they respect its minimum core requirements".<sup>99</sup>

The creation of a duty of honesty was indispensable to Bhasin's win before the SCC. This is because the defendant's decision to terminate could not itself be successfully impeached. In short, the SCC ruled that the contract gave the defendant an unfettered power to end the contract on notice; an entire agreement clause apparently meant that there could be

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<sup>91</sup> Ibid at para 60.

<sup>92</sup> Ibid at para 74.

<sup>93</sup> Ibid. For a brief account of unconscionability, see *McCamus Contract* (n 37) 426.

<sup>94</sup> *Bhasin* SCC at para 77.

<sup>95</sup> *Bhasin* SCC at para 88.

<sup>96</sup> Ibid.

<sup>97</sup> Ibid at para 88, citing *Bruno Appliance and Furniture, Inc v Hryniak*, 2014 SCC 8, [2014] 1 SCR 126, at para 19.

<sup>98</sup> *Bhasin* SCC para 75. For discussion on contracting out of the duty of honesty, see S O'Byrne and R Cohen, "The Contractual Principle of Good Faith and the Duty of Honesty in *Bhasin v Hrynew*" (2015) 53 Alberta LR 1.

<sup>99</sup> *Bhasin* SCC at para 77.

no implied terms restricting the right to terminate for good faith reasons only.<sup>100</sup> Nor did counsel for Bhasin plead the tort of deceit or fraud, so that avenue of liability was closed. What mattered, in the end, was an entirely different point, namely that the defendant had lied to Bhasin or otherwise “equivocated”<sup>101</sup> about its intention to terminate. The SCC ruled that this conduct was a breach of the new duty of honesty<sup>102</sup> and accepted, controversially, that the defendant’s denials caused the plaintiff’s loss of his agency.<sup>103</sup>

A duty of honesty is also at the core of certain pre- and post-*Bhasin* cases regarding the obligation to negotiate in good faith. Some Canadian courts have opined that an agreement committing parties to negotiate in good faith (whether under an express or implied term) is unenforceable due to uncertainty and incompatibility with the adversarialism informing the negotiation process.<sup>104</sup> But there have also been judicial assessments supportive of such a duty.<sup>105</sup> Furthermore, several pre-*Bhasin* courts enforced an agreement to negotiate in good faith where: (a) the negotiations are pursuant to an *existing* contract (for example, as in a lease’s renewal clause); (b) good faith in negotiations is the standard consistent with the parties’ intention—whether by express or implied term; and (c) there is an objective benchmark against which the court can assess whether the party in question is in breach of the good faith duty or not (i.e., the clause does not fail for uncertainty).<sup>106</sup> In this

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<sup>100</sup> Ibid at para 72.

<sup>101</sup> Ibid at para 100.

<sup>102</sup> Ibid at para 103.

<sup>103</sup> See Joseph Robertson, in “Good Faith as an Organizing Principle in Contract Law: *Bhasin v Hrynew* – Two Steps Forward and One Look Back” (2015) 83 Can Bar Rev 809, at 863.

<sup>104</sup> For discussion, see T Buckwold, “The Enforceability of Agreements to Negotiate in Good Faith: The Impact of *Bhasin v Hrynew* and the Organizing Principle of Good Faith in Common Law Canada” (2016) 58 Can Bus LJ 1 at 24-25. Sir George Leggat’s Jill Poole Lecture 2018 (n 9) argues for the enforceability of such agreements.

<sup>105</sup> *Lac Minerals Ltd v International Corona Resources Ltd* (1989), 61 DLR (4<sup>th</sup>) 14 (SCC) at 14 and quoted by McCamus (n 37) at 139.

<sup>106</sup> Such a contract was enforced in *Empress Towers Ltd v Bank of Nova Scotia*, (1990) 73 DLR (4<sup>th</sup>) 400, 50 BCLR (2d) 126 (BCCA), leave to appeal to SCC refused, [1990] SCCA No 472, 79 DLR (4<sup>th</sup>) vii (SCC) at 404-405. *Empress Towers* was recognised in *Mannpar Enterprises v HMTQ* (1999) 173 DLR (4<sup>th</sup>) 243, 1999 BCCA 239 (CanLII) and Supreme

very important sense, the duty to negotiate in good faith is enforceable because it is the standard of *performance* contracted for. Tamara Buckwold shows that *Bhasin* has bolstered such a view over its alternatives because it holds that the good faith standard *is* capable of definition.<sup>107</sup>

Where courts have found a breach of a good faith duty to negotiate, the defendant's conduct has been seriously deficient and functionally dishonest. A common feature of the caselaw – whether pre or post-*Bhasin* – involves obvious stonewalling by the defendant as so to terminate the parties' contractual relationship based.<sup>108</sup> Bargaining with no intention of reaching an agreement is a breach of the duty to bargain in good faith.<sup>109</sup>

*Bhasin*'s recognition of a duty of honesty seems both helpful and harmless. At least in abstraction, it is helpful in identifying a rock bottom standard of contractual performance, while being harmless since the duty seems to cover much the same terrain as civil fraud would in any event.<sup>110</sup> It is also helpful to hold accountable those who negotiate dishonestly in the context of an enforceable duty to the contrary. This is because the innocent party has paid for a benefit (an option to renew, for example) and is being shammed out of it.

However, the duty of honesty is also problematic since it apparently covers more than fraud or lying. This is because the SCC seemed to impeach Can Am for also having “equivocated”<sup>111</sup> in response to *Bhasin*'s queries about its intentions regarding his agency. As McCamus notes, the apparent inclusion of equivocation in the duty of honesty “may complicate the task of advising clients with respect to communications relating to termination or renewal rights and perhaps other aspects of contractual performance such as the exercise of

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Court of Canada in *Mitsui & Co (Canada) Ltd v Royal Bank of Canada* [1995] 2 SCR 187 at para 13.

<sup>107</sup> Buckwold (n 104) at 9. For the court in *Empress Towers*, *ibid*, good faith means best efforts.

<sup>108</sup> For a pre-*Bhasin* example, see *Empress Towers*. For a post-*Bhasin* example, see *0856464 BC Ltd v TimberWest Forest Corp*, 2014 BCSC 2433.

<sup>109</sup> See J D McCamus, “Good Faith Obligations in Contract Law” (paper presented to the Ontario Bar Association Continuing Legal Education seminar) (1 October 2007), cited with approval in *TimberWest* at para 173.

<sup>110</sup> *Empire Communities Ltd v HMQ*, 2015 ONSC 4355, at footnote 1 of the judgment.

<sup>111</sup> *Bhasin* SCC at para 100.

other types of options and contractual discretionary powers”.<sup>112</sup> Beyond this, and as retired appellate judge Joseph Robertson observes, there is a “fine line between a failure of one party to respond to questions fully and a party’s right not to disclose information with respect to future intentions”.<sup>113</sup>

### C. SCOTS LAW

#### (1) Overview: *Smith v Bank of Scotland; the bird that never flew?*<sup>114</sup>

The lack of any Scottish equivalent to *Bhasin* means that the discussion of Scots law can be briefer than the Canadian account just given. With regard to more general duties of good faith in contractual performance outside the contracts *uberimae fidei*, Lord Glennie articulated the general understanding when he stated in 2011: “[i]t is, of course, no part of Scots law that, in the absence of agreement, parties to a contract should act in good faith in carrying out their obligations to each other”.<sup>115</sup> In *Macari v Celtic FC*, where an employer gave instructions to an employee which the former was entitled to give under the contract, it was held that the employee’s non-compliance justified his dismissal and any bad or malicious motive of the employer was irrelevant.<sup>116</sup>

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<sup>112</sup> J McCamus, “The New General Principle of Good Faith Performance and the New ‘Rule of Law’ of Honesty in Performance in Canadian Contract Law” (2015) 32 J Contract L 103 at 114 and quoted in Robertson (n 103) at 862.

<sup>113</sup> *Ibid.*

<sup>114</sup> The reference here is to the ancient armorial bearings of the City of Glasgow: the bird that never flew, the tree that never grew, the bell that never rang, and the fish that never swam. But “never” turned out to be wrong in all four instances thanks to Glasgow’s founder and patron St Mungo. See the City Council’s website:

<https://www.glasgow.gov.uk/index.aspx?articleid=17325>.

<sup>115</sup> *EDI Central Ltd. v. National Car Parks Ltd.* [2010] CSOH 141 para 23. Prior to the passage of the Insurance Act 2015 s 12, the duty of good faith in insurance was held to extend to post-formation conduct so as to apply to an insured’s fraudulent claims: see *Fargnoli v G A Bonus plc* 1997 SCLR 12.

<sup>116</sup> *Macari v Celtic FC* 1999 SC 628, 634-7 (Lord President Rodger). See further W W McBryde, *The Law of Contract in Scotland* (3rd edn, 2007), para 17.32 (citing also *Brown v Edinburgh Magistrates* 1907 SC 256).

In 1997, however, Scots law had a possible “*Bhasin* moment” when the House of Lords decided *Smith v Bank of Scotland*.<sup>117</sup> A series of previous cases had established that the creditor in a cautionary obligation (guarantee) had no obligation to disclose to the prospective cautioner (guarantor) information that it held about the debtor.<sup>118</sup> In *Smith* a wife had acted as guarantor of her husband’s business debts to the creditor bank. It was held that where the relationship between the debtor and the prospective cautioner would lead a reasonable person to suspect that the cautioner’s consent to the arrangement had not been freely given, the creditor was under a duty to warn the cautioner about the risks of the transaction and suggest that she obtain independent legal advice before concluding it. Giving the leading speech in the case, Lord Clyde placed the source of this duty, not upon any equity of constructive notice,<sup>119</sup> but rather on “the broad principle in the field of contract law of fair dealing in good faith”.<sup>120</sup>

Unlike the court in *Bhasin*, Lord Clyde did not elaborate very much upon the “broad principle” beyond deciding the *Smith* case in favour of the wife. He probably did not intend his comment to have any wider significance than that; and over the ensuing two decades so it has proved to be. In another House of Lords case in 2004 Lord Hope of Craighead remarked that “Good faith in Scottish contract law ... is generally an underlying principle of an explanatory and legitimating rather than an active or creative nature”.<sup>121</sup> A leading textbook glosses this as meaning that “the concept underpins existing rules of law and otherwise exists more to exclude bad faith than independently to impose standards of conduct beyond the scope of those existing rules”.<sup>122</sup> Good faith thus does not impose standards of performance in contracts.

In *Smith* itself, however, the concept appeared to be used in an “active or creative” manner with regard to parties’ pre-contractual interactions. But the case has been treated

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<sup>117</sup> *Smith v Bank of Scotland* 1997 SC (HL) 111.

<sup>118</sup> *Young v Clydesdale Bank* (1889) 17 R 231; *Royal Bank of Scotland v Greenshields* 1914 SC 259.

<sup>119</sup> As held in the earlier English case of *Barclays Bank v O’Brien* [1994] 1 AC 180.

<sup>120</sup> *Smith v Bank of Scotland* 1997 SC (HL) 111, 121.

<sup>121</sup> *R v Immigration Officer at Prague Airport, ex parte European Roma Rights Centre* [2004] UKHL 55, [2005] 2 AC 1, para 60.

<sup>122</sup> *Gloag & Henderson The Law of Scotland* (14<sup>th</sup> edn, 2017), para 3.03.

very narrowly in subsequent decisions of the Court of Session. While Scottish judges have not been attracted by the approach set out for English law in *Royal Bank of Scotland v Etridge (No 2)*<sup>123</sup> (giving a detailed list of steps to be taken by the creditor if the transaction is to be valid), preferring the broader approach provided by good faith, that actually tends to favour the creditor inasmuch as any failure to follow one of the *Etridge* steps will not necessarily entail the avoidance of the cautionary obligation.

In *Royal Bank of Scotland v Wilson* in 2003, the Second Division of the Court of Session set out its understanding of the law post-*Smith* in some detail. The good faith requirement applies only in cases where the cautionary obligation is granted gratuitously. The challenging cautioner must claim and, if necessary, prove that the debtor had made a relevant misrepresentation or used undue influence (which is not presumed in Scots law). This suggests that it is the third party's wrongful behaviour, not the creditor's, which is the major reason for any invalidity of the cautioner's obligation.<sup>124</sup> Further, where the creditor knows that the cautioner had received legal advice, it is entitled to assume that the professional adviser had acted properly. The court held that *Smith* had not changed the law to impose any obligation of disclosure on the creditor, who remained obliged only to answer truthfully questions about the debtor's position put to it by the prospective cautioner. The fact that the guarantee granted was of much wider scope than needed for the immediate purposes of the debtor's borrowings was irrelevant to the question of good faith.

There has been little sign since *Wilson* of any doctrine of good faith jumping out of the confines of cautionary obligations and into the mainstream of general contract law in Scotland. The lack of sympathy which modern Scottish courts have for good faith militates against recognition of any general requirement in contracts. For example, the continuing authority of the (mainly nineteenth-century) cases used to support the argument for a liability where a party in bad faith breaks off pre-contractual negotiations before a contract is formally concluded by the parties has been strongly doubted by an Extra Division of the Court of

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<sup>123</sup> *Royal Bank of Scotland v Etridge (No 2)* [2001] UKHL 44, [2002] 2 AC 773. For Scottish rejection see *Clydesdale Bank v Black* 2002 SC 555.

<sup>124</sup> Compare *Trustee Savings Bank v Balloch* 1983 SLT 240 (loan to husband and wife jointly held void for duress against wife, not by creditor bank, but by husband).

Session.<sup>125</sup> Such lack of sympathy for good faith ideas is apparent even when contracting parties impose upon themselves obligations of good faith in their negotiations. Thus at first instance in *Beaghmore Property Ltd v Station Properties Ltd*, Lord Hodge considered an express obligation to act in good faith in pre-contractual negotiations too uncertain to be enforceable.<sup>126</sup> This was so even although at much the same time he held in another first instance case that an agreement to use reasonable endeavours was enforceable.<sup>127</sup> It may be that the authority of the *Beaghmore* decision is undermined to some extent by a further subsequent judgment in the Inner House that terms allowing the parties to renegotiate a contract and requiring them to do so in good faith were enforceable.<sup>128</sup> But, as Martin Hogg points out, “the expressly provided for renegotiation process was to be regulated by the provisions of a [different] clause of the contract”, and this made it difficult to hold the obligation too uncertain in content for specific enforcement.<sup>129</sup>

Examples of the now not uncommon practice of parties agreeing expressly to act towards each other in good faith in the performance of their contract can be found in the case law, but there is little substantive judicial discussion of what such obligations might mean for

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<sup>125</sup> See *Khaliq v Londis Holdings* [2010] CSIH 13, 2010 SC 432, criticised by M Hogg and H MacQueen, “Melville Monument Liability: Some Doubtful Dicta”, (2010) 14 Edin LR 451. See further H L MacQueen, “Good Faith in the Scots Law of Contract: An Undisclosed Principle?”, in Forte (ed), *Good Faith*, 5 at 22-37; and H L MacQueen, “Good Faith”, in H MacQueen and R Zimmermann (eds) *European Contract Law: Scots and South African Perspectives* (2006), 43 at 59-60.

<sup>126</sup> *Beaghmore Property Ltd v Station Properties Ltd* [2009] CSOH 133. Contrast Sir George Leggatt’s arguments in his Jill Poole Lecture 2018 (n 9) and the Canadian cases discussed above, text accompanying nn 105-110.

<sup>127</sup> *R & D Construction Group Limited v Hallam Land Management Limited* ([2009] CSOH 128, affirmed [2010] CSIH 128, 2011 SC 286.

<sup>128</sup> *G4S Cash Centres (U.K.) Ltd v Clydesdale Bank plc* [2011] CSIH 48.

<sup>129</sup> M Hogg, “The Implication of Terms-in-fact: Good Faith, Contextualism, and Interpretation’ (2018) 85 *George Washington LR* 1660-1691, 1686.



the parties.<sup>130</sup> In the commercial leases case of *Grove Investments Ltd v Cape Building Products Ltd* Lord Drummond Young, writing for an Extra Division, struck a Leggattian note when he said:

A contract is a co-operative enterprise, entered into by parties for their mutual benefit. It is intended to achieve objectives that are common to both parties; ... a contract should normally be construed in such a way as to avoid arbitrary or unpredictable burdens or impositions, and conversely arbitrary or unpredictable benefits, in the nature of windfalls; to do otherwise would frustrate one of the most elementary commercial objectives.<sup>131</sup>

But this passage, and the outcome of the case, were heavily criticised,<sup>132</sup> and subsequently the First Division said this of Lord Drummond Young's dictum:

[T]he general observations in *Grove Investments* ought not, we consider, to be taken as indicating that the considerations of co-operation and mutuality that would be appropriate to, say, partnership or joint venture apply across the board. Commercial contracts may, equally, be hard fought with each party intent on securing their own particular objective. As senior counsel for the respondents accepted in the course of discussion, parties enter into contracts for their respective benefit.<sup>133</sup>

## **(2) Defining good faith in Scotland**

Given all this, there is unsurprisingly little attempt in either Scottish cases or juristic writing to define good faith in performance, whether in terms of honesty or reasonableness or any other quality. The only specifically Scottish attempt of which we are aware is by Hogg:

The duty to act honestly and openly in one's dealings with the other party, which includes (but is not limited to) not seeking to take undue advantage of the other party,

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<sup>130</sup> See e.g. *Pip 3 Ltd v Glasgow City Council* [2015] CSOH 119; *JH & W Lamont of Heathfield Farm v Chattisham Ltd* [2018] CSIH 33, 2018 SC 440; *Agilisys Limited v CGI IT UK Limited* [2018] CSOH 26, para 123.

<sup>131</sup> *Grove Investments Ltd v Cape Building Products Ltd* [2014] CSIH 43, [2014] Housing LR 35, para 11.

<sup>132</sup> See e.g. L Macgregor, "Crossing the Line between Business Common Sense and Perceived Fairness in Contractual Interpretation" (2015) 19 Edin LR 378.

<sup>133</sup> *@SIPP Pension Trustees v Insight Travel Services Ltd* [2015] CSIH 91, 2016 SC 243, para 44.

disclosing all such information to the other party the failure to disclose which would distort an honest and open relationship, and treating the other party not simply as an adversary but as a co-operative agent.<sup>134</sup>

In a subsequent careful review of the relevant authorities (English as well as Scots), Hogg concludes (consistently with *Bhasin*) that good faith so defined is not a basis by itself for implying terms in fact into contracts. While good faith may be implied as a substantive obligation especially in long-term (or relational) contracts, the implication remains dependent on the traditional tests of “necessity” and “business efficacy”.<sup>135</sup> There is accordingly no general implication of good faith as a matter of law, as distinct from in the facts and circumstances of particular cases. Since the article was written, a commercial judge, Lady Wolffe, has addressed an argument that an obligation of good faith could be implied in a particular contract financing a property development, but declined to offer an opinion on the general question, on the basis that the term proposed in the particular case (i.e. a term to be implied in fact) would anyway fail the tests of “necessity” or “obviousness”.<sup>136</sup>

On the other hand, the doctrine of terms implied in law includes some which may be implied in contracts generally and which look very like aspects of good faith. Thus parties may be compelled to co-operate to ensure that the contract is carried out, to perform within a reasonable time, to exercise discretionary powers under the contract reasonably, and not to prevent another party from performing or to do anything else to derogate from the contract.<sup>137</sup> But, unlike the good faith of continental European systems, these implied terms can of course be over-ridden by express contractual provision to opposite effects. An “entire agreement”

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<sup>134</sup> M A Hogg, *Obligations* (2nd edn, 2006), para 1.83.

<sup>135</sup> Hogg, “Implication of Terms-in-Fact”, 1668-73. Note that in *Timeshare Management Services Ltd v Loch Rannoch Highland Club* [2011] CSOH 23 it was accepted without significant argument or discussion that obligations of good faith could be implied in a contract to manage a members' club. The management services included some elements of agency, however (para 82).

<sup>136</sup> *Unicorn Tower Ltd v HSBC Bank plc* [2018] CSOH 30, paras 38-43, 69-72 (noted by P C Corcoran, “*Unicorn v HSBC*: Good Faith Returns to Scotland?” (2018) 22 Edin LR 380-386).

<sup>137</sup> See the authorities cited in McBryde, *Contract* (n 116) paras 9.13 (reasonable time), 9.22 (discretionary powers), 9.36 (co-operation); H L MacQueen and J Thomson, *Contract Law in Scotland* (4th edn, 2016), para 3.34.

clause will not necessarily over-ride the implication of terms, however; all depends upon how the clause defines “entire agreement”.<sup>138</sup>

Fritz Brand and Douglas Brodie have argued in greater detail, partly based on a comparison of South African with Scots law, that express discretionary powers in a contract are increasingly subject to implied considerations of good faith.<sup>139</sup> That argument left open, however, the question of how far such implicit restraints might be overcome by express contractual provision. In *Glasgow West Housing Association Ltd v Siddique* the view was taken that, while an expressly “absolute” discretion could not be overcome by the implication of terms, it might still be possible to challenge its non- or “wholly unreasonable” exercise. But the legal basis for such a challenge would not be an implied term, albeit no alternative was specified by the court.<sup>140</sup> In *Bradford & Bingley Building Society v Thorntons plc* the exercise of a landlord’s power to apportion “an equitable share” of repair costs was held not invalid only by choice of an alternative more to the landlord’s advantage; but it was open to challenge where it was not one a landlord acting equitably could have made.<sup>141</sup> The Scottish courts may find more persuasive than a good faith approach that of the UKSC in *Braganza v BP Shipping Ltd*, holding that the exercise of a contractual discretionary power could be impugned, not only where it was one that no reasonable decision-maker could have reached, but also where the decision-making process failed to exclude extraneous considerations or to take account of all obviously relevant ones.<sup>142</sup> But whether such a public law approach is appropriate in the context of private or commercial relations can be doubted.<sup>143</sup>

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<sup>138</sup> See Scottish Law Commission Discussion Paper No 147 on Interpretation of Contract (February 2011), paras 3.15-3.19 (with particular reference to the Contract (Scotland) Act 1997, s 1).

<sup>139</sup> F Brand and D Brodie, “Good Faith in Contract Law”, in R Zimmermann, D Visser and K Reid (eds), *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004), 94-116 at 109-112.

<sup>140</sup> *Glasgow West Housing Association Ltd v Siddique* 1997 SC 375.

<sup>141</sup> *Bradford & Bingley Building Society v Thorntons plc* 1998 GWD 40-2071.

<sup>142</sup> *Braganza v BP Shipping Ltd* [2015] UKSC 17; [2015] 1 WLR 1661.

<sup>143</sup> See C Himsworth, “Transplanting Irrationality from Public to Private Law: *Braganza v BP Shipping Ltd*”, (2019) 23 Edin LR 1.

There has been no discussion of whether a contractual right to terminate falls, as in *Bhasin*, to be distinguished from a more general contractually conferred discretion; but it has been said that “[a] right to terminate [under an express provision] may, as a matter of construction, not entitle a party to act arbitrarily or unreasonably.”<sup>144</sup> A 2018 decision is of interest in this context in confirming that the court will control what it sees as unreasonable or capricious exercise of even the seemingly absolute discretion to terminate. In *Iftikhar v CIP Property (AIPT) Ltd* the purchaser of commercial property was obliged to provide a deposit and certain “know your customer (KYC)” information to the vendor, who was entitled at its “sole discretion” to deem the deposit not paid and so to treat the contract as repudiated by the purchaser if the KYC information was not received by a certain date. The purchaser provided the requested KYC information on time, but the material, when coupled with a late request that the sale be made to a nominee of the purchaser, raised suspicions in the vendor about a possible money-laundering dimension to the transaction, and it requested further information about the purchaser’s source of wealth but without setting any specific deadline for its submission. In reply the purchaser’s solicitors appeared to prevaricate; and the vendor then purported to terminate the contract. But the purchaser intimated a wish to continue, and the vendor provided a further opportunity for the supply of information, this time with a seven-day deadline. The vendor was again dis-satisfied with the information supplied, and once more declared the contract at an end. The purchaser sought implement of the contract. Reversing the commercial judge at first instance, the First Division held that the minor issues with the initially submitted KYC information probably did not entitle the vendor to treat the contract as repudiated but that it was legitimate under the contract for it to request further information. Giving the second opportunity to provide further information was also legitimate. However, the court held, in language redolent of good faith, that the vendor was not entitled to rescind the bargain suddenly and without warning only three days later. Doing so without warning and on the stated basis, which concerned only the absence of the source of funds information, amounted to an unlawful repudiation of the contract.<sup>145</sup>

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<sup>144</sup> McBryde, *Contract* (n 116) para 20.95 (citing *Gordon DC v Wimpey Homes Holdings Ltd* 1991 SLT 883; *Rockcliffe Estates plc v Co-operative Wholesale Society Ltd* 1994 SLT 592; *Palmer v Forsyth* 1999 SLT (Sh Ct) 93; but contrasting *Prentice v Scottish Power plc* 1997 SLT 1071). For *Bhasin*’s approach, see text accompanying nn 74-84.

<sup>145</sup> *Iftikhar v CIP Property (AIPT) Ltd* [2018] CSIH 44, 2019 SCLR 118, para 34.

The purchaser's consequent entitlement to implement of the contract was however still subject to his providing the KYC information reasonably required by the vendor and paying the price.

Three other rules of Scots contract law associated with breach of contract can also be taken as relating to contractual performance and yet enforcement is subject to "equitable" considerations which might be (but presently are not) presented as aspects of good faith in contractual performance: (1) the right to claim specific implement (performance) of a contract's non-monetary obligations;<sup>146</sup> (2) anticipatory or anticipated breach (where if a party refuses to perform a contract, or gives notice that it will not perform when the time comes, the other party is not bound to terminate but may instead elect to continue performance on its side of the bargain and claim payment therefor);<sup>147</sup> and (3) mutuality of contract (where a party is entitled to exercise the self-help remedy of mutuality retention by with-holding or suspending performance due under the contract until the other party cures or remedies its breach of reciprocal obligations under the contract).<sup>148</sup> In each case there are equitable controls upon the innocent party's right to claim the other's performance and its freedom to perform or not to perform, as the case may be. Here, we will focus most on (2) and (3), merely noting in passing that in each there may be something to be learned from the equitable constraints on specific implement, which include the court's consideration of the order's practicability, exceptional hardship for the defender, and the reasonable availability to the pursuer of alternative sources of supply.<sup>149</sup>

In the anticipated breach case the innocent party's freedom to perform is said to be constrained by two considerations: that its ability to do so is not dependent upon the other party's active co-operation, and that the innocent party has a "legitimate interest" in continuing to perform.<sup>150</sup> These constraints have been less deployed in Scotland than in

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<sup>146</sup> McBryde, *Contract* (n 116) ch 23.

<sup>147</sup> *White & Carter (Councils) Ltd v McGregor* 1962 SC (HL) 1; McBryde, *Contract* (n 117), paras 20.37-20.41.

<sup>148</sup> McBryde, *Contract* (n 116), paras 20.44-20.73.

<sup>149</sup> McBryde, *Contract* (n 116), paras 23.15-23.22.

<sup>150</sup> *White & Carter (Councils) Ltd v McGregor* 1962 SC (HL) 1, 13-14 (Lord Reid).

England,<sup>151</sup> where the judicial consensus appears to be that a commercial party always has a legitimate interest in performing the contract except in cases of absolute unreasonableness.<sup>152</sup> It is therefore difficult to see either consideration as currently active requirements of good faith in performance. Matters would be different, however, if, as one recent commentator has suggested, the innocent party had to demonstrate its legitimate interest in performance rather than have it assumed.<sup>153</sup> But in 2018 the Scottish Law Commission decided not to recommend reform in this area to prevent unreasonable conduct by the innocent party, instead encouraging the Scottish courts to give greater consideration to the “co-operation” and “legitimate interest” constraints.<sup>154</sup> A consideration relevant to good faith might be whether the court would grant the second party an order for specific implement against the first party, especially if alternative sources of supply were reasonably available to the former.

More judicial attention has been given recently, however, to the explicitly equitable control of the innocent party’s deployment of mutuality retention of performance. There had been little modern discussion until *Inveresk plc v Tullis Russell Papermakers Ltd* in the House of Lords in 2010, when Lord Rodger embarked upon a characteristically thorough

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<sup>151</sup> For a full (and critical) review of the English cases, see J O’Sullivan, “Repudiation: Keeping the Contract Alive”, in G Virgo and S Worthington (eds), *Commercial Remedies: Resolving Controversies* (2017), ch 3. Note that Lord Sumption’s powerful dissent in *Soci t  Generale, London Branch v Geys* [2012] UKSC 63, [2013] 1 AC 523 is based in part on Lord Reid’s co-operation qualification as well as the wrongfully dismissed employee’s inability to obtain an order for specific performance against the employer. In Scotland the “legitimate interests” exception is accepted by Lord President Emslie in *Salaried Staff London Loan Company v Swears and Wells Limited* 1985 SC 189 at 193, as (arguably) is the “co-operation” one in *AMA (New Town) Ltd v Law* [2013] CSIH 61, 2013 SC 608 (a decision of an Extra Division).

<sup>152</sup> See e.g. *MSC Mediterranean Shipping Company SA* (n 5).

<sup>153</sup> M P Gergen, “The Right to Perform after Repudiation and Recover the Contract Price in Anglo-American Law”, in DiMatteo and Hogg (eds), *Comparative Contract Law*, ch 16. David Campbell provides a response to Gergen’s analysis, questioning the result in *White & Carter* itself on the basis of the ‘legitimate interest’ test (ibid, at 338-341).

<sup>154</sup> Scottish Law Commission Report on *Review of Contract Law: Formation, Interpretation, Remedies for Breach, and Penalty Clauses* (Scot Law Com No 252, 2018), ch 12.

analysis of one aspect of the topic.<sup>155</sup> He highlighted a line of authority under which the court has an equitable power to allow a party to withhold payment of a debt otherwise fixed in amount and presently payable (i.e. “liquid”) on the basis of a claim not so fixed or due (i.e. “illiquid”, e.g. a damages claim) but shortly to be decided by the court, in order for set-off—or, in the traditional language of Scots law, compensation—to extinguish the two debts to the amount of whichever is the lesser. This rule has been dubbed “special retention”, to contrast it with the withholding/suspending nature of “mutuality” retention. The crucial point of distinction is that while the withholding or suspension of performance in mutuality retention tends to look to the eventual performance of the contract (or a substitute therefor), special retention is a step on the road to the extinction of its obligations by compensation. This tempers the strictness of the still-extant Compensation Act 1592, by which extinctive compensation takes place only between two liquid claims (although not necessarily arising from the same source of obligation). The court must be satisfied, however, that allowing special retention is equitable.<sup>156</sup>

As Lorna Richardson has shown, equity enjoys a different role in mutuality retention,<sup>157</sup> which, it is suggested here, reflects requirements of good faith in controlling abuse of rights. A party may withhold performance of its own liquid obligation until the other party performs in accordance with the contract, but a court can disallow this if the retention is inequitable. Giving the leading opinion for the Extra Division in *McNeill v Aberdeen City Council*, Lord Drummond Young stressed the court’s equitable power to prevent retention becoming an “instrument of abuse”,<sup>158</sup> which in his view might occur when it is used otherwise than to secure future performance by the contract-breaker. In the most recent case, the owners of 73 acres of land granted developers an option to purchase it in return for two

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<sup>155</sup> *Inveresk plc v Tullis Russell Papermakers Ltd* [2010] UKSC 19, 2010 SC (UKSC) 106.

<sup>156</sup> L Richardson, “Examining ‘Equitable Retention’” (2016) 20 Edin LR 18; L Richardson, “Set-off – a Concept Divided by a Common Language?” [2017] LMCLQ 238.

<sup>157</sup> See further L Richardson, “The Scope and Limits of the Right to Retain Contractual Performance”, [2018] JR 209, 218-219, 222-228,

<sup>158</sup> *McNeill v Aberdeen City Council (No 2)* [2013] CSIH 132, 2014 SC 335 para 30 (commented upon by D Cabrelli, “The Mutuality of Obligations Doctrine and Termination of the Employment Contract: *McNeill v Aberdeen City Council (No 2)*” (2014) 18 Edin LR 259).

non-refundable payments. The ultimate aim was a private residential development, and if sales were arranged by the developers the owners had an obligation to convey the land to the purchasers. The parties also provided for a security to be granted in favour of the developers, covering sums to be paid to the latter in the event of their being able to organise these sales. The development never took place, and the owners terminated the agreement by valid notice. But the developers refused to discharge the security and counterclaimed for losses suffered as a result of alleged breaches by the owners. The First Division held that the refusal was not a valid exercise of the remedy of retention, which could not be used to compel performance of reciprocal obligations which were no longer extant by virtue of the contract's valid termination.<sup>159</sup> The principal other ground for refusal was that the obligations in question were clearly not reciprocal under the contract, so that one could not be withheld in respect of any failure on the other side. But the First Division, with Lord Drummond Young again stressing the need to prevent abuse of the power to retain, also highlighted the inequity of allowing the remedy when the developers' allegations of breach against the owners were vague and non-specific and when they had available to them another remedy (diligence on the dependence) by which the owners' power to deal with the land could be restricted until satisfaction of the claims against them.<sup>160</sup> This last smacks somewhat, however, of the much-criticised approach in the law of unjustified enrichment whereby the equitable remedy cannot be exercised where another exists at law.<sup>161</sup> Like claims in unjustified enrichment, mutuality retention is a matter of right, not equity, and the court's power is only one to regulate abuse of that right. The mere existence of another, different right capable of having an equivalent effect should not matter in that question.<sup>162</sup>

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<sup>159</sup> *JH & W Lamont of Heathfield Farm v Chattisham Ltd* [2018] CSIH 33, 2018 SC 440, 2018 SLT 511 (critically reviewed by L Richardson, "What Do We Know about Retention Now?" (2018) 22 Edin LR 387). It is understood that the decision is being appealed to the UK Supreme Court.

<sup>160</sup> *JH & W Lamont of Heathfield Farm v Chattisham Ltd*, paras 24 (Lord President Carloway), 43-46 (Lord Drummond Young), and 60 (Lord Malcolm).

<sup>161</sup> For discussion of the position in enrichment law see R Evans-Jones, *Unjustified Enrichment: Enrichment by Deliberate Conferral: Condictio* (2003), paras 2.20-2.39.

<sup>162</sup> Richardson, "Scope and Limits", 218.



This equitable power therefore does not imply that the performance withheld should bear a close relationship in value to the non-performance on the other side, or to the adverse effects actually suffered by the innocent party as a result of the non-performance.<sup>163</sup> Additional light is thrown on the equitable control of retention by the equitable control of the closely related right of lien, “a real right to retain property until the discharge of an obligation or certain obligations, the property not having been delivered to the retaining party for the purpose of security.”<sup>164</sup> The classic example in the contractual context is where the creditor gains possession of the debtor’s property in order to carry out work upon it, such as repair, and is not paid for that work. The equitable control of lien consists in the court’s capacity to prevent abuse and unfair oppression of the contract-breaker.<sup>165</sup> Examples from the case law include that party’s need to have the property back for some other pressing reason, such as completing a tax return or for business requirements, and its re-delivery to that party only upon the latter finding other security (such as consigning in court the amount said to be due) for payment or performance of the disputed obligation.<sup>166</sup> The control is thus not one of generalised fairness, and the legitimate interests of the retaining party are fully recognised and protected in their turn. There lurks here, in other words, hints of good faith *Bhasin*-style.

#### D. CONCLUSIONS

While *Smith v Bank of Scotland* has not led to any renewal of a general notion of good faith in the Scots law of contract, it is clear that tools do exist through which the Scottish courts can address issues of honesty, reasonableness and equity in the performance and enforcement of contracts. That these tools have not been systematically taken up leads to a question: would Scottish law benefit from the approach taken by the SCC such that aspects of the

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<sup>163</sup> MacQueen and Thomson, *Contract* (n 137), para 5.21; Richardson, “Scope and Limits”, 211. The Scottish courts hold that hardship must be exceptional before it can ground refusal of an order for specific implement: see *Highland & Universal Properties Ltd v Safeway Properties Ltd (No 2)* 2000 SC 297.

<sup>164</sup> A J M Steven, *Pledge and Lien* (2008), para 9.01. Lien is generally understood to be an aspect of the law of mutuality and retention possessing the additional feature that the party retaining may go on to realise the value of the property retained (McBryde, *Contract*, para 20.74).

<sup>165</sup> Steven, *Pledge and Lien* (n 164), para 15.05.

<sup>166</sup> *Ibid*, para 15.05; McBryde, *Contract* (n 116), para 20.77.

Scottish common law are formally recognised under the banner of a good faith principle *Bhasin*-style?

Adopting a good faith law principle would present both opportunities and dangers for the Scots law of contract. Fears include an increase in litigation<sup>167</sup> as well as a reduction in commercial certainty and freedom of contract, because the good faith principle would overwhelm the enforcement of express contractual terms.<sup>168</sup> But while there has been an undoubted increase in litigation in Canada as *Bhasin* settles into the common law,<sup>169</sup> courts have decisively followed the SCC's warning that claims of good faith will generally fail unless they fit within existing doctrines.<sup>170</sup> They have respected the SCC's admonition that the principle may be developed incrementally but only on an exceptional basis and only in a way "consistent with the structure of the common law of contract [that] gives due weight to the importance of private ordering and certainty in commercial affairs".<sup>171</sup> The trial judge in *Styles* thought she had that exceptional case but this was reversed on appeal. The 2018 decision from the Ontario Court of Appeal in *Mohamed* may be that exceptional case but the court never claimed as much and currently remains an outlier in permitting an express term to be overridden by virtue of the good faith principle. While *Mohamed* was not appealed further, another case potentially raising a similar issue is pending before the SCC<sup>172</sup> and may indirectly reveal whether *Mohamed* is correctly decided.

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<sup>167</sup> See, for example, the assessment of practitioners S H Bower, D J Bell, P D Banks, R K Agarwal, R J Kruger and W A Bortolin in their short article "New Good-Faith Duty of Honesty in Contractual Performance Recognized" (25 November 2014) Bennett Jones online: <https://www.bennettjones.com/en/Publications-Section/Updates/New-Good-Faith-Duty-of-Honesty-in-Contractual-Performance-Recognized-by-Supreme-Court-of-Canada>.

<sup>168</sup> For discussion, see Robertson (n 103) at 844.

<sup>169</sup> As of March 27, 2019 *Bhasin* SCC had been judicially considered 507 times but, in many instances, cursorily and inconsequentially.

<sup>170</sup> *Bhasin* SCC at para 66.

<sup>171</sup> *Ibid.*

<sup>172</sup> *Ocean Nutrition Canada Limited v David Matthews*, 2018 NSCA 44, leave to appeal to the SCC granted, 2019 CanLII 5975 (SCC).

In this and related ways, therefore, *Bhasin* poses no danger because it articulates a light version of a good faith principle, having regard for common law traditions going to respect for private orderings and concern that courts be not given the means to “veer” into “ad hoc judicial moralism”.<sup>173</sup> The SCC was certainly aware of the perils traditionally associated by Common (and many Scots) lawyers with over-arching notions of good faith in contract, and put control mechanisms in place to guard against them. Accordingly, and unlike civil law jurisdictions, the good faith principle does not have an overriding influence on the content of a contract. With the exception of the uncontroversial new duty of honesty, the contract’s content is established as it always has been - according to doctrines regarding implied terms (as illustrated in the context of contractual discretions).<sup>174</sup>

Good faith was also carefully defined by the SCC to distinguish it from fiduciary obligations and avoid any suggestion that it entailed putting another party’s interests ahead of one’s own. The implications of the good faith principle are also highly context-specific, varying from case to case according to facts and circumstances, including in relation to the express and implied provisions of the contract in question.

As a result of the limits and confines placed on the good faith principle by the SCC, its potential adoption in Scotland would offer more opportunity than risk. Jeannie Paterson is right to say that explicit recognition of a good faith principle is unnecessary where there is already recognition of more specific obligations such as loyalty or fidelity to the contractual relationship, primarily by requiring honesty and cooperation in contract performance and by precluding the exercise of discretionary contractual powers in a manner that is unreasonable or outside the proper purposes of the power.<sup>175</sup> Scots law certainly already does accept these more specific duties, albeit in a somewhat subdued manner.<sup>176</sup> However, there is also something to be said for more general statements.

First and foremost, the good faith principle acknowledges an essential truth about contract law – that significant parts of it *are* infused by good faith values, albeit at what might be described as a subterranean level in Scotland. A very large example relates to the implication of contractual terms and the exercise of contractual discretions. Second, the good

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<sup>173</sup> *Bhasin* SCC at para 70.

<sup>174</sup> Robertson (n 103) at 816, n 39.

<sup>175</sup> Paterson (n 14).

<sup>176</sup> See above, text accompanying nn 137-143.

faith principle offers a viable alternative to unsystematic judicial reasoning on multiple fronts. Most significantly, it can set the tone for lower courts in relation to the legitimacy of those aspects of the common law founded on good faith.<sup>177</sup> It can also explain and make more coherent existing authorities. In Scotland, for example, a good faith principle might help better align the currently incoherent and uncertain approaches to equitable control of specific implement, anticipated breach and mutuality retention.

Third, the good faith principle helps put certain judicial lines of authority on more solid ground, thereby contributing to legal certainty. Thus, the SCC's endorsement of the new duty of honesty makes the duty to negotiate in good faith (derived from an existing contract) much more accepted and uncontroversial. Such an effect might be attractive and indeed desirable in Scotland, given increasing use of "good faith" clauses in commercial contracts despite the judicial doubts expressed thereon. It might even assist in validating the controversial group of cases establishing non-contractual liability in certain circumstances for unjustifiable or unreasonable breaking off negotiations for a contract, rather than leaving them in an uncertain and doubtful limbo.<sup>178</sup> Again, a focus on the specific context in such cases would help identify those circumstances (probably exceptional) in which such liability could arise, while its subjection to contrary contract terms could avoid any uncertainty for parties engaging in negotiations likely to take some time to complete and bearing a clear risk of possible failure.

Finally, the good faith principle grounds judicial innovation. For example, from *Bhasin* itself emerges the new duty of honesty, identified because "[c]ommercial parties reasonably expect a basic level of honesty and good faith in contractual dealings"<sup>179</sup>; a proposition established empirically as much as by any theory or "judicial moralism". In this way, the SCC established a new avenue of liability in relation to how parties communicate with each other during the performance of the contract, making lies and equivocations therein actionable with a contractual measure of damages.

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<sup>177</sup> D Percy, "The Emergence of Good Faith as a Principle of Contract Performance", in S Degeling, J Edelman, J Goudkamp (eds) *Contract in Commercial Law* (2016) 231 at 232, citing G H L Fridman challenging the SCC to develop the common law.

<sup>178</sup> See above, note 125.

<sup>179</sup> *Bhasin* SCC at para 60.

*Bhasin*'s versatility derives, in part, from its decision to eschew the familiar judicial technique both in Canada and Scotland of "inductive analogy from the existing body of precedent."<sup>180</sup> It consciously took a deductive or universalist approach<sup>181</sup> whereby a general principle is posited and the case at bar is measured in relation to it.<sup>182</sup> In short, *Bhasin* followed a top-down, not bottom-up technique.<sup>183</sup> This approach provides the judiciary with a formalised marker which contextualises and moors the judge's task in relation to good faith arguments. Under the universalist approach, as Percy observes, future courts are left with "the task of working out the detailed implications of broadly stated doctrine,"<sup>184</sup> and the good faith principle provides the overall, guiding framework.<sup>185</sup> It is an approach that is consistent with Scots law's image of itself as a system of principle as much as if not more than one of precedent.

Setting aside whether the courts in Scotland might consider adopting a good faith principle, *Bhasin* seems to us nonetheless immediately helpful in advancing the discussion of good faith within the UK generally. Its emphasis on the continuing primacy of the contract and the variability of the standard of good faith and the duty of honesty according to context is more useful than consideration of the extent to which a contract is or is not "relational", given the debate around that concept. The "relationality" of a contract will undoubtedly be important context in finding that the parties' relationship is one justifying implicit requirements of open-ness, co-operation, and concern for each other's position.<sup>186</sup> But, as Hugh Collins points out, in first proposing relational contract theory Ian Macneil did not intend to make a conceptual distinction with legal effects: rather, "he argued that the context of an exchange matters for an understanding of all contracts, because they are normally embedded in prior social relations".<sup>187</sup> Similarly, the position between parties negotiating a

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<sup>180</sup> Percy (n 177) at 231.

<sup>181</sup> *Ibid* at 233.

<sup>182</sup> *Ibid* at 233.

<sup>183</sup> *Ibid* at 233.

<sup>184</sup> *Ibid* at 232.

<sup>185</sup> *Ibid* at 233.

<sup>186</sup> *Bhasin* SCC acknowledges that the general organising principle of good faith "would likely have different implications in the context of a long-term contract of mutual cooperation than it would in a more transactional exchange" (para 69).

<sup>187</sup> Collins (n 13), 45.

contract, whether or not under an agreement to do so in good faith, cannot really be described as “relational” in the Leggatt sense, but it too may surely be nonetheless susceptible to requirements of open-ness, co-operation and concern for the other party’s position for the reasons that Macneil provides. The socio-economic setting of *Smith v Bank of Scotland* is an excellent illustration of the point.

For the moment, it seems unlikely that the Scottish courts will offer a judicial restatement of the various strands of law imposing standards of reasonableness and honesty to draw them together under an over-arching rubric of good faith. The only circumstance in which that might conceivably happen is if the English appellate courts, and in particular the UKSC, are persuaded (as so far they have not been) to take up and endorse or develop Sir George Leggatt’s arguments about good faith. *Bhasin* and the Canadian experience since the SCC’s judgment ought to encourage those in England prepared to contemplate the limited development of a good faith principle in the performance of a contract.<sup>188</sup> By itself, unfortunately, it is thought that *Bhasin* is unlikely to have any immediate impact upon the Scottish position.

But all that said, the good faith principle can be emboldening and even ignite the judicial imagination such that advance word from the UKSC may not be required. The growing need to interpret the good faith clauses that commercial practitioners continue to insist on putting into the contracts they draft may have its own, independent effect. Perhaps like the bird that it was thought would never fly, the Scottish courts under the stimulus of *Bhasin* and commercial usage will yet come to life and recognise the potential of the good faith principle as a way to doing their work better.

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<sup>188</sup> As it may yet: see Z X Tan, "Keeping the Faith with Good Faith? The Evolving Trajectory Post *Yam Seng* and *Bhasin*" [2016] JBL 420.