



# Contract Negotiations and the Common Law: A Move to Good Faith in Commercial Contracting?

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## Abstract

Classically a duty to negotiate commercial contracts in good faith has been seen as part of the civil, not the common, law world. Common law commercial lawyers have long resisted the lure of “good faith” as a contractual concept, despite engagement with civil law principles in harmonisation projects, by virtue of membership of the European Union and their use in international conventions such as the United Nations Convention on Contracts for the International Sale of Goods (CISG). This paper will examine whether this situation is changing, focusing on two common law jurisdictions—England and Wales and Canada. In England and Wales and the common law of Canada, case-law in the last 10 years has indicated a movement towards acceptance of express and implied duties of good faith in relation to contractual performance, see e.g. *Yam Seng Pte Limited v International Trade Corporation Limited* [2013] EWHC 111 (QB) and, most recently, *Essex CC v UBB Waste (Essex) Ltd (No. 2)* [2020] EWHC 1581 (TCC) in England and Wales; *Bhasin v Hrynew* 2014 SCC 71 and *Callow v Zollinger* 2020 SCC 45 in Canada. This paper will examine the extent to which these cases may open the way more generally for a duty to *negotiate* commercial contracts in good faith. It will examine the reception of these cases and whether they indicate (i) greater acceptance of “good faith” as part of contract law thinking and (ii) a possible extension of good faith into the pre-contractual period.

**Keywords** Good faith · Contract law · Negotiations · Comparative contract law · Common law legal culture

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## Introduction: Common Law and the Problem of Good Faith

Traditionally, the common law has opposed duties to negotiate and perform contracts in good faith in commercial law.<sup>1</sup> This is despite the fact that, in civil law, such duties are commonplace. Art. 1104 of the French Civil Code provides that “Contracts must be negotiated, formed and performed in good faith. This provision is a matter of public policy.”<sup>2</sup> The German Civil Code equally states that a party to a contract has a duty to perform according to the requirements of good faith,<sup>3</sup> with *culpa in contrahendo* (fault in contracting) developed first by case-law and academic commentary<sup>4</sup> before finally appearing in the 2001 revision of the BGB at §§311(2) and (3).<sup>5</sup> In transnational law, Art. 7(1), CISG<sup>6</sup> requires that the contract be interpreted having, amongst other things, due regard to the observance of good faith in international trade, although extending this provision to the pre-contractual period has proven contentious.<sup>7</sup> A rare common law example may be found in the US, where both the Restatement (Second) of Contracts and the Uniform Commercial Code provide that every contract “imposes an obligation of good faith in its performance or enforcement”.<sup>8</sup>

The disparity between common and civil law can be attributed to a number of factors. Concern has been expressed about the notion of “good faith” as a generic concept. Bridge (2017, pp. 100–101), for example, has argued that common lawyers are uncomfortable with abstract concepts such as good faith on the basis that they jeopardise legal certainty and place too much power in the hands of judges, rather than the contracting parties themselves. McKendrick (1999, p. 43) has questioned why English law would abandon clearly focused doctrines dealing with impropriety in contracting in favour of the amorphous, multi-purpose notion of good faith. Further, imposing a duty of good faith on negotiating parties has traditionally been

<sup>1</sup> The focus of this article is on general commercial contract law. It should be noted that the common law treats specific contracts dealing with fiduciary relations, partnership, employment and insurance differently.

<sup>2</sup> Amendments to the Code by Ordonnance no 2016-131 of 10 February 2016 made explicit case-law developments extending the duty to perform in good faith to the pre-contractual period. For translation, see [https://www.trans-lex.org/601101/\\_/french-civil-code-2016/](https://www.trans-lex.org/601101/_/french-civil-code-2016/).

<sup>3</sup> §242, BGB. For translation, see [https://www.gesetze-im-internet.de/englisch\\_bgb/](https://www.gesetze-im-internet.de/englisch_bgb/).

<sup>4</sup> See Kessler and Fine (1963–4), classically traced back to Rudolf von Jhering (1861). Von Jhering’s work was also influential in the development of French law, translated into French in 1893: von Jhering (1893).

<sup>5</sup> §311(2) reads that “An obligation with duties under §241(2) also comes into existence by 1. The commencement of contractual negotiations”. §241(2) provides that duties may arise obliging each party to take account of the rights, legal interests and other interests of the other party to the contract.

<sup>6</sup> United Nations Convention on Contracts for the International Sale of Goods.

<sup>7</sup> An express stipulation to this effect was blocked by certain common law jurisdictions in 1980. See Bridge (2017: 108); but contrast art 2:301 of the Principles of European Contract Law, and art 2.1.15 of the UNIDROIT Principles of International Commercial Contracts.

<sup>8</sup> UCC § 1–304; see also, Restatement (Second) of Contracts, § 205. In Sect. 1–201 UCC, good faith is defined generally as “honesty in fact and the observance of reasonable commercial standards of fair dealing.” Again the question of pre-contractual duties of good faith has proven more difficult to resolve.

dismissed as impractical and in conflict with the principle of freedom of contract: in the words of Lord Ackner, “as unworkable in practice as it is inherently inconsistent with the position of a negotiating party”.<sup>9</sup> Such a duty is therefore seen as undermining commercial freedom and failing to recognise the adversarial nature of the negotiating process in which it is economically desirable for each party to be entitled to pursue their own interests. This is sometimes entitled “freedom *from* contract”. Such reasoning argues that intervention prior to contract formation should be resisted except in the presence of overtly wrongful behaviour such as fraud, duress or other misconduct. As Trakman and Sharma (2014, p. 603) indicate, the common law liberal rationale seems to rest on the assumption that negotiating parties are more likely to arrive at a genuine understanding if they are not “shackled” by contractual duties, or by courts holding the legal Sword of Damocles over their heads.

In the commercial context, therefore, a duty to negotiate in good faith is seen by common lawyers as uncertain in content, inefficient, and giving too much power to judges. It is further argued that judges are often insufficiently commercially aware to be able to distinguish between aggressive (but legitimate) negotiation tactics and actual misconduct: Bridge (1999, p. 143). Further objections include difficulties in estimating damages,<sup>10</sup> that it would encourage a plethora of minor claims, and that parties might be forced into contractual obligations they neither desire and which are not in their best economic interests. As leading common law practitioners’ text, *Chitty on Contracts* (2020: para. 1–047) opines:

“Given the remarkably open-textured nature of good faith, this would lead to a very considerable degree of legal uncertainty and could be seen as trespassing too far into the legislative domain.”

However, law is neither static nor untroubled by change. In England and Wales, case-law in the last 10 years has indicated a movement towards acceptance of express and implied duties of good faith in relation to contractual performance. Similar developments have been seen in other common law jurisdictions, such as Canada. It seems likely that post-Brexit, as the United Kingdom law moves away from the EU and seeks global trading partners, the force of comparisons across the common law world will strengthen. Canada represents a key common law example where duties of good faith in contractual performance have received particular attention by the Supreme Court of Canada, with three key decisions since 2014. Such developments show the influence of both proximity to the United States as a major trading partner, and also to Quebec as part of the bicultural culture of Canada.

This article will explore such developments and examine whether acceptance of “good faith” arguments in terms of performance is likely to encourage common

<sup>9</sup> *Walford v Miles* [1992] 2 A.C. 128, 138. For the argument that Lord Ackner has been misinterpreted as advocating solipsistic self-interest, see Campbell (2017).

<sup>10</sup> It has been argued that since it can never be known whether good faith negotiations would have produced an agreement and on what terms, it is impossible to assess any loss caused by breach of the obligation: *Petromec Inc v Petroleo Brasileiro SA Petrobras (No 3)* [2005] EWCA Civ 891, [116] per Longmore L.J.

lawyers to review their opposition to contracts to negotiate in “good faith”. It will start by examining the extent to which the courts in England and Wales and Canada have overcome traditional objections to good faith by recognising duties to *perform* commercial contracts in good faith. It will then, with reference to the underlying reasoning of the courts, consider to what extent such developments can be relied upon to overcome objections to contractual duties to *negotiate* in good faith? Is the common law moving to a gradual acceptance that even commercial negotiations must be subject to some *de minimis* good faith obligation or is resistance likely to continue?

## Good Faith and Contractual Performance in England and Wales

### A General Duty of Good Faith?

The idea of a duty to *perform* in good faith in commercial transactions has traditionally faced a number of objections. It is too abstract and uncertain, too difficult to enforce, it requires the court, rather than the parties, to set commercial standards and is contrary to the “spirit” of freedom of contract in which each contracting party is encouraged to safeguard his or her own economic interests. However, such arguments have always had to be balanced against the piecemeal solutions provided by the common law to deal with misconduct by the parties. In *Interfoto v Stiletto*, Bingham L.J. famously commented that:

“English law has, characteristically, committed itself to no such overriding principle [of good faith] but has developed piecemeal solutions in response to demonstrated problems of unfairness. Many examples could be given. Thus equity has intervened to strike down unconscionable bargains. Parliament has stepped in to regulate the imposition of exemption clauses and the form of certain hire-purchase agreements. The common law also has made its contribution, by holding that certain classes of contract require the utmost good faith, by treating as irrecoverable what purport to be agreed estimates of damage but are in truth a disguised penalty for breach, and in many other ways.”<sup>11</sup>

As this quotation acknowledges, the common law accepts that certain types of contract e.g. involving fiduciaries and contracts classified as *uberrimae fidei* such as insurance contracts may require “good faith”. Equally, EU-sourced legislation provides a further dimension, for example, legislation introduced to implement Directive 93/13/EEC on Unfair Terms in Consumer Contracts,<sup>12</sup> and retained post-Brexit,<sup>13</sup> states that a term is unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations under the

<sup>11</sup> *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] 1 Q.B. 433, 439.

<sup>12</sup> Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts *OJ L 95*, 21.4.1993, p. 29–34.

<sup>13</sup> See Part 2 of the Consumer Rights Act 2015, s 62(4).

contract to the detriment of the consumer.<sup>14</sup> While controversial when introduced,<sup>15</sup> “good faith” has been part of English consumer law, then, since the mid-1990s.<sup>16</sup> At least in consumer law, due to the influence of EU directives and decisions of the European Court of Justice, the divide between common and civil law is not as clear-cut as traditional common lawyers might want to think.<sup>17</sup>

Yet, under commercial law, the piecemeal approach continues. We might nevertheless describe individual causes of action as sharing the common goal of ensuring “commercial fairness” (or excluding unfairness). McKendrick (2021: 12.10) argues that while rejecting “good faith” as a principle, English contract law has nevertheless sought to condemn conduct amounting to “*bad faith*”. Contracts will thus be set aside on proof that one party had been telling lies, using illegitimate pressure, exploiting the weakness of the other or abusing a position of confidence.

The common law courts, however, have had to confront the issue of good faith when faced with commercial contracts where the parties themselves have included a clause that the parties should act in good faith in performing their contracts. In the next two sections, I will examine how the courts have dealt with express duties of good faith and, more radically, arguments that they should imply duties to perform in good faith when they represent the presumed intentions of the contracting parties. In such circumstances, do the courts respect the will of the parties, based on their express or presumed intentions, or are such clauses dismissed as merely aspirational and not legally binding?

### Express Duties of Good Faith in Commercial Contracts

Duties to perform in good faith have long been accepted in specific types of contracts such as partnership, insurance, commercial agency and employment.<sup>18</sup> The question here is to what extent they should be enforceable in general commercial law. In the last 20 years, the English courts have, albeit with some reservations, started to accept that an express obligation to act in good faith in the performance of a contract may, in certain circumstances, be enforced. In the *Mid Essex Hospital Services* case,<sup>19</sup> for example, a 7-year contract for the supply of catering and

<sup>14</sup> This is all but identical to the wording of the test required by the 1993 Directive art.3(1). See, for example, *ParkingEye Ltd v Beavis* [2015] UKSC 67; [2016] A.C. 1172 and, generally, CMA, *Unfair contract terms guidance, Guidance on the unfair terms provisions in the Consumer Rights Act 2015* (CMA37, July 2015).

<sup>15</sup> See Collins (1994); Teubner (1998).

<sup>16</sup> “Good faith” is found in a number of EU directives that have been transposed into UK law e.g. Directive 2005/29/EC concerning unfair business-to-consumer commercial practices in the internal market [2005] O.J. L149/16 arts.5(2) and 2(h) and, in commercial law, Directive 86/653/EEC on the co-ordination of the laws of the Member States relating to self-employed commercial agents [1986] O.J. L382/17: art.3(1).

<sup>17</sup> See Giliker (2017); Whittaker (2017).

<sup>18</sup> See, for example, *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd (The Star Sea)* [2001] UKHL 1; [2003] 1 A.C. 469.

<sup>19</sup> *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200; [2013] B.L.R. 265. However, the court refused to imply a term that the NHS trust

cleaning services contained an express term that the Hospital Trust and the company “will co-operate with each other in good faith”. While accepting its validity, the Court of Appeal held that the term must be construed in the context of the contract as a whole.<sup>20</sup> What it would not accept was a general and potentially open-ended obligation that might clash with other more specific provisions in the contract. However, a clause requiring the parties to honestly endeavour to achieve the purposes stated in the relevant clause would be valid.<sup>21</sup> Beatson L.J. noted the fine line to be achieved: courts should take care “not to construe a general and potentially open-ended obligation such as an obligation to ‘co-operate’ or ‘to act in good faith’ as covering the same ground as other, more specific, provisions, lest it cut across those more specific provisions and any limitations in them.”<sup>22</sup>

Equally in *Berkeley Community Villages Ltd v Pullen*,<sup>23</sup> a property development contract with the express term that “the parties will act with the utmost good faith towards one another” was construed as imposing a contractual obligation to observe reasonable commercial standards of fair dealing in accordance with the agreement, faithful to the agreed common purpose of the parties.<sup>24</sup> In *CPC Group Ltd v Qatari Diar Real Estate Investment Co*,<sup>25</sup> terms of “utmost good faith” in joint venture construction agreements were construed as requiring the parties to “adhere to the spirit of the contract ... and to be faithful to the agreed common purpose, and to act consistently with the justified expectations of the parties.” Such a clause, stated the court, would not require a party to subordinate its own interests so long as the pursuit of these interests did not entail unreasonable interference with the benefits expressly conferred by the contract. It would, however, require parties to eschew bad faith.<sup>26</sup>

In these cases, the English courts are seeking to distinguish vague and open-ended terms from those that can be construed as giving rise to a sufficient degree of objective certainty. This is achieved by adopting a narrow construction that draws on the content of the contract and detailed scrutiny of its provisions. Hoskins (2014, p. 144) comments that:

“... ‘good faith’, as understood here, is not fixed or external to the parties’ intentions; rather, it emphasises co-operation in accordance *with* those intentions and draws its precise requirements from the particular contract and its wider context.” (Emphasis added).

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Footnote 19 (continued)

would not act in an arbitrary, irrational or capricious manner when calculating service failures by the catering company or when making deductions from monthly payments in respect of those failures.

<sup>20</sup> *Ibid.*, at [109] per Jackson L.J.

<sup>21</sup> *Ibid.* at [112].

<sup>22</sup> *Ibid.*, at [154]. See also *BP Gas Marketing v La Société Sonatrach* [2016] EWHC 2461 (Comm) (no “free-standing obligation of good faith” at [403] per Simon Bryan Q.C.).

<sup>23</sup> [2007] EWHC 1330 (Ch); [2007] 3 E.G.L.R. 101.

<sup>24</sup> *Ibid.*, at [97]. The court here was influenced by the US Restatement (Second) of Contracts.

<sup>25</sup> [2010] EWHC 1535 (Ch), [246] per Vos J.

<sup>26</sup> *CPC Group* *ibid.* at [240], relying on *Overlook v Foxtel* [2002] NSWSC 17, [65] and [68].

Reasonable commercial standards, therefore, derive from the contract and the parties themselves, not the views of individual judges.<sup>27</sup>

However, the courts recently have gone further and accepted, to a degree yet to be established, that good faith obligations can be implied into commercial contracts to give them business efficacy. This will be examined in more detail below.

## Implying Duties of Good Faith into Commercial Contracts

Implied terms raise different considerations to express terms. In the words of Lord Bingham.

“...the implication of contract terms involves a different and altogether more ambitious undertaking: the interpolation of terms to deal with matters for which, *ex hypothesi*, the parties themselves have made no provision.”<sup>28</sup>

McKendrick (2021: 12.10) notes, however, that implied terms provide a means by which the courts may encourage fair dealing in transactions and, as such, encourage parties to act in what might be described as “good faith”. These may be implied by custom,<sup>29</sup> by fact (to give business efficacy to a contract)<sup>30</sup> or by law (to particular categories of contract).<sup>31</sup> Nevertheless, in terms of good faith, the courts have made it clear that they do not accept that “there is to be routinely implied some positive obligation upon a contracting party to subordinate its own commercial interests to those of the other contracting party”.<sup>32</sup> English courts further remain reluctant to imply such terms into arm’s length contracts between commercial parties,<sup>33</sup> particularly where the parties could, but did not, use the language of good faith. Equally where it is inconsistent with the other clauses of the contract, no implication will be made.<sup>34</sup> Fears continue to be expressed about the damaging effect of any implication of a broad notion of good faith as a general organising principle.<sup>35</sup>

However, the common law perception of contracting parties as self-interested parties who prioritise their own commercial interests above those of the other contracting party has been challenged. Work by academics, such as Macneil, has sought to distinguish discrete, one-off, transactions from those where the parties are engaged

<sup>27</sup> Soper (2021: 582) describes express (and implied) good faith terms in this sense as chameleonic, varying in content according to context.

<sup>28</sup> *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd* [1995] E.M.L.R. 472, 481.

<sup>29</sup> *Hutton v Warren* (1836) 1 M & W 466.

<sup>30</sup> *The Moorcock* (1889) 14 PD 64. See also *Marks and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72; [2016] A.C. 742.

<sup>31</sup> *Liverpool CC v Irwin* [1977] A.C. 239.

<sup>32</sup> *Hamsard 3147 Ltd v Boots UK Ltd* [2013] EWHC 3251 (Pat), [86] per Norris J.

<sup>33</sup> *Myers v Kestrel Acquisitions Ltd* [2015] EWHC 916 (Ch).

<sup>34</sup> See *Globe Motors Inc v TRW Lucas Varity Electric Steering Ltd* [2016] EWCA Civ 396; [2017] 1 All E.R. (Comm), [68]: “[A]n implication of a duty of good faith will only be possible where the language of the contract, viewed against its context, permits it.”

<sup>35</sup> *MSC Mediterranean Shipping Company SA v Cottonex Anstalt* [2016] EWCA Civ 789, [45] per Moore-Bick L.J.

in a mutually beneficial long-term relationship during which the interests of the parties become intertwined.<sup>36</sup> Examples of the latter—which he calls “relational contracts”—include joint venture, franchise and long-term distributorship agreements. In *Yam Seng Pte Limited v International Trade Corporation Limited*<sup>37</sup> in 2013, Leggatt J noted that many relational contracts will require a high degree of communication, cooperation and predictable performance based on mutual trust and confidence between the parties. These will involve expectations of loyalty which are implicit in the parties’ understanding and necessary to give business efficacy to the contract.<sup>38</sup>

*Yam Seng* itself involved a long-term distributorship contract for a fragrance marketed under the brand name “Manchester United”. In giving judgment, Leggatt J. argued that an implied duty to perform in good faith would arise in relational contracts such as this. The law, he argued, did not draw a simple dichotomy between relationships that give rise to fiduciary duties and other contractual relationships. A duty of honesty, for example, could be implied in fact if it reflected the presumed intentions of the contracting parties on the basis that it was needed to give business efficacy to the parties’ relationship. While honesty would be a core value in such a relationship, Leggatt J. argued that:

“...[i]n addition to honesty, there are other standards of commercial dealing which are so generally accepted that the contracting parties would reasonably be understood to take them as read without explicitly stating them in their contractual document. A key aspect of good faith is the...observance of such standards”.<sup>39</sup>

On this basis, he argued, an implied duty of good faith in the performance of contracts was neither novel nor foreign to English law, but served to protect the reasonable expectations of contracting parties.<sup>40</sup> The essential justification therefore is that the court is simply expressing the presumed intention of the parties.<sup>41</sup>

While strictly obiter, Leggatt J.’s reasoning proved influential in opening up the debate as to the existence of implied duties of good faith in commercial law.<sup>42</sup> In the later 2018 case of *Sheikh Tahnoon v Kent*,<sup>43</sup> Leggatt J. found a breach of an implied duty of good faith owed to the defendant under a joint venture agreement through which the parties had sought to establish a brand of luxury hotels in Greece. Again, pivotal was the finding that this was a relational contract in which each party

<sup>36</sup> Macneil (1978); Macneil (2003) and, generally, Austen-Baker (2004) and Campbell (2001).

<sup>37</sup> [2013] EWHC 111 (QB); [2013] 1 Lloyd’s Rep. 526.

<sup>38</sup> Ibid, [142].

<sup>39</sup> Ibid, [138].

<sup>40</sup> *Yam Seng* (n 37), [145], citing Lord Steyn in *First Energy (UK) Ltd v Hungarian International Bank Ltd* [1993] 2 Lloyd’s Rep 194, 196 and, extra-judicially: Steyn (1997).

<sup>41</sup> Interestingly Leggatt J. also accepted at [150] that it might be advantageous to describe the duty as one of “good faith and fair dealing”. Fair dealing, he argued, would reassure parties that it was the standards of conduct objectively determined to arise from the conduct that shapes the notion of “good faith”.

<sup>42</sup> It was cited in the Canadian case of *Bhasin v Hrynew* 2014 SCC 71, [57], discussed below.

<sup>43</sup> *Sheikh Tahnoon Bin Saeed Bin Shakhboot Al Nehayan v Kent* [2018] EWHC 333 (Comm).



“trust[s] that the other party will act with integrity and in a spirit of cooperation.”<sup>44</sup> He concluded that such “legitimate expectations which the law should protect ... are embodied in the normative standard of good faith.”<sup>45</sup>

Leggatt J. in *Sheikh Tahnoon* went so far as to suggest that such a term could be implied as a matter of law into all relational contracts. He argued that the nature of such a contract implicitly requires, in the absence of a contrary indication, treating it as involving an obligation of good faith.<sup>46</sup> While any move from implication by fact to law remains controversial,<sup>47</sup> a number of first instance judgments have accepted that where the parties are in a contractual relationship which has all the characteristics of a relational contract, it is legitimate to imply as a matter of course a duty to perform in good faith. For example, in *Essex CC v UBB Waste*,<sup>48</sup> the court described a long-term private finance initiative (PFI) contract as a “paradigm example of a relational contract in which the law implies a duty of good faith”. It required a close collaborative working relationship and, in such circumstances, the court found that the parties must have intended that their respective roles be performed with integrity and with fidelity to their bargain and shared environmental objectives.<sup>49</sup>

Can we say, then, in 2022 that English law has accepted a duty, in certain situations, to perform commercial contracts in good faith? The answer is a qualified yes. Courts nevertheless remain reluctant to recognise a duty of good faith in all commercial contracts. Academics, such as Whittaker (2013, p. 468), continue to warn that such a duty will lead to an undesirable degree of uncertainty in that it invites “courts to go well beyond the proper function of judicial law-making. English law’s rejection of a general legal doctrine of good faith should not be undermined by such a general implied term.”<sup>50</sup> In contrast, Saintier (2017) argues that the traditional hostility of English law towards good faith is gradually being replaced by a cautious acceptance that there may be a role for a behavioural norm based on honesty and co-operation. Bell and McCunn (2020, p. 16) note a flurry of recent case-law which indicates growing recognition of implied duties of good faith in English law. They argue (2020, p. 18), however, that there are ongoing uncertainties not only in the content of such duties but whether they should be implied by fact or by law and that the law is in urgent need of the intervention by a higher court.

One further source of uncertainty lies with the definition of “relational contract” itself.<sup>51</sup> As Campbell (2014, p. 482) has argued, all contracts might be said to be

<sup>44</sup> *Ibid.*, at [167].

<sup>45</sup> *Ibid.*

<sup>46</sup> *Ibid.*, at [174]. Contrast, however, his views in *Yam Seng* (n 37) at [131].

<sup>47</sup> Recent case-law has struggled to resolve this point, see e.g. *Bates v Post Office Limited (No 3)* [2019] EWHC 606 (QB) and *Cathay Pacific v Lufthansa* [2020] EWHC 1789 (Ch).

<sup>48</sup> [2020] EWHC 1581 (TCC), [113], Pepperall J.

<sup>49</sup> On the facts, there was, however, no breach of the good faith term.

<sup>50</sup> See also Soper (2021) and Bridge (2017, p. 106), who argues that: “it is far from clear whether [Leggatt J] has more than basic honesty in mind and there are few signs that his call possesses a general appeal outside the ranks of those academic lawyers who are waiting for a sign to lead them into the promised land of ethical contracting.”

<sup>51</sup> See Tan (2016: 428); *UTB v Sheffield United* [2019] EWHC 2322 (Ch) per Fancourt J.

relational in the sense that they anticipate a co-operative exchange relationship with implicit duties of respect for the other party. What Leggatt J. seems to mean in this context are non-discrete contracts, that is, where a long-term business relationship is anticipated in which indeterminate implicit expectations and obligations are essential to its successful performance. Yet we cannot even say that all long-term contracts will be “relational”—the express terms of the contract may indicate to the contrary, for example, by indicating that neither party saw the relationship as exclusive.<sup>52</sup> More subversively, Collins (2016) argues that even if we can identify contracts that seek to articulate obligations of co-operation in support of the long-term pay-offs and obligations of mutual trust and confidence to preserve the necessary trust between the parties, this does not necessarily *require* the implication of a duty of good faith. Given that there is, as yet, no agreed definition of the category of relational contracts, the argument in favour of implication by law becomes problematic to say the least.

Nevertheless, if we examine the cases discussed above, we can identify a number of overlapping elements which judges seem to regard as indicative of the content of the proposed duty to perform in good faith where the parties have a relationship based on mutual trust and confidence:

- To act honestly, with fidelity to the parties’ bargain and reasonably in the spirit of fair dealing, i.e., refrain from conduct which, in the relevant context, would be regarded as commercially unacceptable by reasonable and honest people;
- To be loyal (importantly not to the other party but to the agreement itself);
- To communicate with the other party and perform predictably; and
- To collaborate with the other party in the performance of the contract, acting with integrity and in a spirit of co-operation.

Any such implied term will be subject to the ability of the parties to exclude it by clear and express terms.<sup>53</sup>

It is difficult at present to go any further. Leggatt L.J. himself in the *Sheikh Tahnoon* case conceded that it was perhaps impossible to attempt to spell out an exhaustive description of what an obligation of good faith would involve.<sup>54</sup>

## Good Faith and Contractual Performance in Canada

### A Duty of Honesty in Contractual Performance

While the law of England and Wales is in a state of flux, Canadian law in 2014 took a significant step. Until that date, the common law of Canada had, in general,

<sup>52</sup> *UTB v Sheffield United* [2019] EWHC 2322 (Ch), [202].

<sup>53</sup> Subject to statutory restrictions. See *Bates v Post Office Ltd (No 3)* [2019] EWHC 606 (QB), [726] per Fraser J. In contrast, civil law is more willing to prevent any exclusion of good faith, see Saintier (2017).

<sup>54</sup> *Sheikh Tahnoon* (n 43) at [175].

shared the same reservations as English law about good faith.<sup>55</sup> While this view was not shared by the civil law system of Quebec, Canada is a bijural State in which common and civil law legal traditions co-exist but retain their own cultural identity (Allard 2001, p. 1). In *Yam Seng*, Leggatt J. noted that the Canadian courts had proceeded cautiously in relation to good faith in the performance of commercial contracts, although he noted a willingness to imply duties in some cases.<sup>56</sup> In *Bhasin v Hrynew*,<sup>57</sup> however, the Supreme Court of Canada (SCC) expressly recognised the existence of an “organizing principle of good faith” in commercial contract law. This principle, it argued, underpins and informs the common law piecemeal position. It requires the parties to act reasonably, honestly, and be candid and forthright and not act capriciously or arbitrarily. In carrying out his or her contractual performance, then, the contracting party should have appropriate regard<sup>58</sup> to the legitimate contractual interests of their contracting partner. The standard would be highly context-specific and appropriate consideration should be paid to the legitimate interests of *both* contracting parties. In the words of Cromwell J:

“it is time to take two incremental steps in order to make the common law less unsettled and piecemeal, more coherent and more just. The first step is to acknowledge that good faith contractual performance is a general organizing principle of the common law of contract ... The second is to recognize, as a further manifestation of this organizing principle of good faith, that there is a common law duty which applies to all contracts to act honestly in the performance of contractual obligations.”<sup>59</sup>

On the facts of the case, Bhasin had contracted with Can-Am to sell its education saving plans to investors. The contract provided for automatic renewal at the end of the three-year period unless one of the parties gave six months’ notice to the contrary. Can-Am decided to give notice, exercising its right not to renew the agreement, after tensions arose between Bhasin and a competitor, Hrynew, who also worked for Can-Am. As a result, Bhasin lost business and the majority of his workforce to Hrynew. The court found that Can-Am had been dishonest in its dealings with Bhasin, misleading him as to its intentions and the role of Hrynew in its organisation. Damages for breach of its duty to act honestly in performance of the contract

<sup>55</sup> For traditional opposition, see Bridge (1984); Clark (1993). However, as in England, certain specific categories of contract, such as employment and insurance contracts, have been held to require good faith performance. The concept of “good faith” is also used in hundreds of statutes across Canada, including statutory duties of good faith and fair dealing in franchise legislation and good faith bargaining in labour law.

<sup>56</sup> *Yam Seng* (n 37), [126]. See e.g. *Transamerica Life Inc v ING Canada Inc* (2003) 68 OR (3d) 457, 468. This case opposes, however, a general duty of good faith in all contracts: [53–54].

<sup>57</sup> 2014 SCC 71; [2014] 3 S.C.R. 495, hereafter *Bhasin*.

<sup>58</sup> While “appropriate regard” for the other party’s interests will vary depending on the context of the contractual relationship, it merely requires that a party not seek to undermine those interests in bad faith.

<sup>59</sup> *Bhasin* (n 57), [33] per Cromwell J.

were assessed as the value attached by the trial judge to the loss of Bhasin's agency at the time of non-renewal.<sup>60</sup>

Three key observations may be made on the *Bhasin* decision. First, it is unclear how radical the SCC wanted to be in this case. On its face, the SCC argued that it was not seeking to change the law but to rationalise it to "make the law more certain, more just and more in tune with commercial expectations."<sup>61</sup> It was not, therefore, favouring abstract civil law principle. The SCC was careful to add that any organizing principle of good faith should be applied in a manner consistent with the commitment of the common law of contract to the freedom of contracting parties to pursue their individual self-interest and principles of economic efficiency. However, at the same time, the SCC sought to require that all contracts should be read as subject to a basic level of honest conduct. "It is", the SCC asserted, "to say the least, counterintuitive to think that reasonable commercial parties would accept a contract which contained a provision to the effect that they were not obliged to act honestly in performing their contractual obligations."<sup>62</sup> Honesty, therefore, is a bare minimum, and the SCC envisaged incremental judicial development to ensure the law continues to reflect the reasonable expectations of commercial parties.

Secondly, in taking this position, the Court argued that there was a need to align its commercial law with that of major trading partners. On this basis, it expressed concern that the law was out of step with the civil law of Quebec<sup>63</sup> and most jurisdictions in the United States.<sup>64</sup> It further noted that other common law jurisdictions, such as England and Wales and Australia, were paying increasing attention to the notion of good faith, particularly in the area of contractual performance.<sup>65</sup>

Thirdly, it is important to note that this decision goes further than its English counterpart. Swan (2017) argues that, in the light of *Bhasin*, the Canadian courts are more likely to protect the expectations of contracting parties than the English courts. It is clear that by favouring an "organizing principle" that sets a minimum *standard* of honesty in contractual performance rather than relying on express or implied terms, a broader duty is created which gives the courts a greater ability to extend the law incrementally.<sup>66</sup> The Canadian standard is one that can operate irrespective of

<sup>60</sup> This was notwithstanding the substantial difficulty involved in assessing that value in that Bhasin could not have sold his agency without Can-Am's approval had he known that they intended to terminate their relationship.

<sup>61</sup> *Ibid.*, [1] per Cromwell J. Reference was made to UK judge, Lord Steyn's influential article: Steyn (1997).

<sup>62</sup> *Ibid.*, [61].

<sup>63</sup> The Civil Code of Quebec (*CCQ*) recognizes a broad duty of good faith which extends to the formation, performance and termination of a contract and includes the notion of the abuse of contractual rights: see Arts. 6, 7 and 1375.

<sup>64</sup> The SCC relied on § 1–304 of the U.C.C. and §205 of the *Restatement (Second) of Contracts* (1981) which provides for a general duty of good faith in all contracts, noting that this provision of the *Restatement* has been followed by courts in the vast majority of states. Waddams observes, however, that the duty of good faith has been very narrowly construed by many US courts: (2017a: §449).

<sup>65</sup> See, for example, Paterson (2014) on Australian and Singaporean law.

<sup>66</sup> *Bhasin* (n 57), [74] per Cromwell J. In the case, the implication of a term of good faith would have conflicted with an entire agreement clause. This does not mean that the standard of good faith cannot be used by the courts to imply terms into contracts: *ibid.*, [44].

the intentions of the parties and is to this extent more analogous to equitable doctrines that impose limits on freedom of contract, such as the doctrine of unconscionability. Parties will only be free to relax the requirements of the doctrine so long as they respect its minimum core requirements and do so in express terms.

The *Bhasin* judgment provoked a heated discussion of the scope of this organizing principle of good faith.<sup>67</sup> The Court in *Bhasin* had argued that the law should be developed “incrementally in a way that is consistent with the structure of the common law of contract [giving] due weight to the importance of private ordering and certainty in commercial affairs.”<sup>68</sup> The opportunity to review this advice came in 2020.

### **Post-*Bhasin* Developments: *Callow v Zollinger***

In *C.M. Callow Inc. v Zollinger*,<sup>69</sup> the SCC chose to expand incrementally the *Bhasin* duty of honesty in contractual performance. Dishonesty, it asserted, goes beyond outright lies and can, depending on the context, include half-truths, omissions, and sometimes even silence. In this case, Callow Inc, which had provided maintenance services to a group of condominium corporations (Baycrest) under two contracts (winter and summer), had complained that it had not been informed of Baycrest’s decision to terminate the winter contract until September 2013. This was after Callow had completed its obligations under the summer contract. The winter agreement allowed for termination on notice; there was no dispute that due notice had been given. However, Baycrest had delayed communication of its decision due to concerns that Callow would abandon the less profitable summer contract if informed at an earlier date. It had even entered into discussions with Callow, giving Callow the impression that it was likely to get a two-year renewal of the winter maintenance contract and that Baycrest was satisfied with its services. During the summer of 2013, Callow had performed work above and beyond the summer maintenance contract at no charge in the hope it would act as an incentive for Baycrest to renew the winter maintenance agreement.

The SCC held that, in exercising the termination provision, Baycrest had breached its duty of honest performance in that it had strung Callow along by knowingly misleading it to believe that the winter contract would not be cancelled. Crucially, Baycrest had been aware that Callow had performed the extra work in summer 2013 to encourage renewal of the winter contract and, rather than telling them the truth, had indicated that they were happy with the services and that the winter contract was likely to be renewed. On this basis, the duty to act honestly in the performance of the contract was breached *due to active deception*. By exercising the termination clause dishonestly, Baycrest had breached the duty of honesty on a matter directly linked to the performance of the contract. The majority was willing

<sup>67</sup> The case has attracted considerable commentary, both national and international, see, for example, Swan (2015); Hunt (2015); O’Byrne and Cohen (2015); McCamus (2015).

<sup>68</sup> *Bhasin* (n 57), [66].

<sup>69</sup> 2020 SCC 45; 452 D.L.R. (4th) 44.

to award damages corresponding to the expectation interest measured against the defendant's least onerous means of performance.<sup>70</sup> In this case this would require correction of the misrepresentation once Baycrest knew Callow had drawn a false inference. Had it done so, Callow would have had the opportunity to secure another contract for the upcoming winter.

The *Callow* case is interesting in that it permits intervention in circumstances where Callow were clearly taking a risk in engaging in unpaid work in the *hope* of contract renewal. Baycrest had been careful not to promise that the contract would be renewed, but crucially having already made up its mind to cancel, were found to have actively misled Callow.

### Future Challenges for Canadian Law

Canadian law remains in a state of incremental development as the courts explore how to apply principles of good faith to questions of contractual performance. Bertolini (2021, p. 614) argues that the *Callow* court's incomplete conceptualisation of the scope of the duty of honesty is likely to create further uncertainty as litigants test the outer limits of the duty of honest performance. He notes that, at present, Canadian scholarship seems divided between restrained views of *Bhasin* and expansionist views that argue in favour of the idea of good faith as a general principle of the common law of contract and draw on structural similarities between *Bhasin's* conceptualisation and the civilian approach to good faith.

Reference to the civil law of Quebec, notably by the majority of the SCC in *Callow*, has raised the difficult question of the relationship between the common and civil law of Canada. In his judgment, Kasirer J., a former Justice of the Quebec Court of Appeal and professor at McGill University's Faculty of Law, drew analogies with civil law, notably with the doctrine of *abus du droit* (abuse of rights).<sup>71</sup> Reliance on Quebec law and concepts such as *abus du droit* is worrying for a number of reasons. First, it blurs the line between the common law and civil law concepts of good faith.<sup>72</sup> In so doing it fails to acknowledge the conceptual differences between an abstract principle of good faith and the common law incremental doctrine. It has been rightly criticised by comparative lawyers on this basis.<sup>73</sup> Secondly,

<sup>70</sup> The minority disagreed, arguing that "the justification for awarding expectation damages does not apply to breach of the duty of honest performance. In such cases, the issue is *not* that the defendant has failed to perform the contract, but rather that the defendant *has* performed the contract, but has also caused the plaintiff loss by making dishonest extracontractual misrepresentations concerning that performance, upon which the plaintiff *relied* to its detriment ... [T]he plaintiff's complaint is not lost value of performance, but detrimental reliance on dishonest misrepresentations" *ibid.* at [142] (*per* Brown J.).

<sup>71</sup> The term "abuse of rights" has several uses in Quebec law, but may be explained in this context as imposing liability where an act, although strictly within the bounds of a legal right, is abused through its exercise in a manner which prejudices another and brings no appreciable benefit to its author. Such conduct would be contrary to the duty of good faith in articles 7 and 1375, CCQ.

<sup>72</sup> See e.g. Kasirer J. *ibid.* at [57]: "like in Quebec civil law, no contractual right may be exercised dishonestly and therefore contrary to the requirements of good faith."

<sup>73</sup> See the comments of Professor Stéphane Sérafin in the Obligations Discussion Group, December 18 2020, 'Duty of Honest Performance in the SCC' and Valcke (2019).

one should not lose sight of the fact that, as intellectual and historical traditions, the common law and the civil law represent, in many respects, distinctive ways of knowing the law. Commentators have noted the differing techniques for the genesis of new rules of law according to the common law and civil law methods.<sup>74</sup> Valcke (2019) argues that importing a civilian duty of good faith into Canadian common law will clash with the internal logic of the common law of contracts. Brown J., speaking for the minority, in *Callow* expressed these concerns clearly:

“[T]he majority’s resort to the civil law as a “source of inspiration” ... is inappropriate ... Drawing from civil law in these circumstances departs from this Court’s accepted practice in respect of comparative legal analysis. Rather than permissibly drawing inspiration or comfort from the civil law in filling a gap in the common law or in modifying it, the majority’s approach ... risks subsuming the common law’s already established and distinct conception of good faith into the civil law’s conception. And to the extent it does so, it confuses matters significantly, the majority’s assurances to the contrary notwithstanding.”<sup>75</sup>

Canadian law, therefore, seems to be struggling with its bijural legal tradition (Allard, 2001) and the influence of civilian good faith principles.<sup>76</sup> This has the potential to expand the notion of “good faith” to that of a mixed common law/civilian approach and draw analogies beyond the common law world. Waddams (2017b, pp. 330–331) warned in 2017 that reference to Quebec law in the earlier case of *Bhasin* might be regarded as an “invitation” to consider civil law concepts, including abuse of rights, and his concerns seem to be validated.<sup>77</sup> His view remains that good faith should only be welcomed as a general principle if it is understood in an objective sense as equivalent to reasonableness.<sup>78</sup> MacQueen and O’Byrne (2019, p. 327) equally argue that *Bhasin* should not be read too widely, arguing that 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’”. Such views are difficult to reconcile with that of the majority in *Callow*.

More recently in *Wastech Services Ltd v Greater Vancouver Sewerage and Drainage District*,<sup>79</sup> the SCC considered another aspect of the organizing principle of good faith: its application towards the exercise of contractual discretionary powers in a long-standing commercial relationship. The SCC accepted that a contractual

<sup>74</sup> See, e.g. Daly (2018) who argues that “il serait tout à fait erroné de voir dans *Bhasin* une dérive vers des modes de pensée civils sur les obligations contractuelles.”

<sup>75</sup> *Callow* (n 69) at [154] and [156].

<sup>76</sup> Note also the use of civilian law in cases such as *Canadian National Railway Co v Norsk Pacific Steamship Co.* [1992] 1 S.C.R. 1021, 1143–44; *Deloitte & Touche v Livent Inc. (Receiver of)* [2017] 2 S.C.R. 855, [138]. See also *Kingstreet Investments Ltd. v New Brunswick (Finance)* [2007] 1 S.C.R. 3, [41].

<sup>77</sup> See also Reynolds (2019: 390–397).

<sup>78</sup> Waddams (2017a: §556).

<sup>79</sup> 2021 SCC 7; 454 D.L.R. (4th) 1.

duty to exercise discretionary power in good faith will place limits on how one exercises facially unfettered contractual rights.<sup>80</sup> To exercise it capriciously or arbitrarily, therefore, would be wrongful and constitute breach of contract. The majority chose to interpret the *Bhasin* organizing principle of good faith as a duty “to exercise their discretion reasonably”,<sup>81</sup> that is, in a manner consistent with the purposes for which it was granted in the contract. Tension arose, however, between the majority and the minority as to the extent to which the majority’s interpretation of this test would undermine freedom of contract and distort the parties’ bargain by imposing standards external to the parties in question.<sup>82</sup> The minority further expressed concern that in responding to Counsel’s arguments based on Quebec law, the majority’s “digression” into civil law risked making the law more complicated, uncertain and confused.<sup>83</sup>

While, therefore, recognizing a basic duty to perform honestly, Canadian law continues to struggle to outline its precise content and the degree to which Quebec law should influence its interpretation. In contrast to English law, however, good faith in performance is now, without doubt, part of Canadian commercial law.

## A Contractual Duty to Negotiate in Good Faith?

### Will *Yam Seng* or *Bhasin* Inspire Change?

Given the growing acceptance of duties to perform in good faith in Anglo-Canadian law, in this Part, I will examine to what extent decisions such as *Yam Seng* and *Bhasin* offer support to those advocating a duty to *negotiate* in good faith. The starting point in both systems remains that an agreement to negotiate a contract or contractual terms is treated in law like an “agreement to agree”.<sup>84</sup> Such agreements are regarded as too uncertain to be enforceable.<sup>85</sup> However, post-*Bhasin*, there is growing support in Canada for the idea that, having accepted an underlying organizing principle of good faith in contractual performance, enforcing agreements to negotiate in good faith may be the next incremental step.<sup>86</sup> Reynolds (2017, pp. 118–119) argues that commercial parties have a reasonable expectation at both the negotiation and performance stage that the other contracting party, while vigorously advocating

<sup>80</sup> In the case, GVS had an absolute contractual discretion to allocate waste among disposal facilities at different destinations.

<sup>81</sup> (n 79), [63].

<sup>82</sup> *Ibid.*, [128]–[135].

<sup>83</sup> *Ibid.*, at [115] per Brown and Rowe JJ.

<sup>84</sup> See, classically, *May & Butcher Ltd. v R* (1929), [1934] 2 K.B. 17.

<sup>85</sup> *Courtney & Fairbairn Ltd v Tolaini Brothers (Hotels) Ltd* (1974) [1975] 1 W.L.R. 297, 301; *Martel Building Ltd. v Canada*, 2000 SCC 60; [2000] 2 S.C.R. 860 at [73].

<sup>86</sup> However, such support is not unanimous. Compare *978011 Ontario Ltd. v Cornell Engineering Co.* 53 O.R. (3d) 783 (ONCA), at [34–35] with *Styles v Alberta Investment Management Corp* 2017 ABCA 1, [51]: “the *Bhasin* principle relates to the performance of the contract. It does not relate to the negotiation or terms of the contract.”



for their own interests, will avoid actively dishonest behaviour. Equally, Buckwold (2016) has suggested that recognition of an underlying organizing principle should force the Canadian courts to re-evaluate its opposition to contracts to negotiate in good faith in that such agreements can no longer logically be condemned as too uncertain to have contractual effect. Further, if the law of Quebec is to be regarded as influential, as *Callow* suggests, then it is worth noting that the Civil Code of Quebec recognizes a broad duty of good faith which extends to the *formation*, performance and termination of a contract.<sup>87</sup> The argument is straightforward. If good faith can set an identifiable standard for performance of the contract, including, in *Callow*, terms relating to termination and renewal of the contract, it should logically extend to the negotiation of the contract itself. On this basis, obligations to act honestly and reasonably, and not capriciously or arbitrarily, should be permissible during the negotiation process with a failure to do so leading to contractual damages.

In contrast, given the more tenuous position of good faith in performance in English law, the question of any extension to good faith in negotiating is far more contentious. McKendrick (2021: 12.10) notes ongoing opposition which, he argues, should not be seen as an objection to a “good faith” duty per se, but rather reflecting a concern that a duty to negotiate is, as Lord Ackner stated in *Walford v Miles*, “unworkable in practice”.<sup>88</sup> Nevertheless, there are some signs even in England that opposition is weakening. As seen in Canada pre-*Bhasin*,<sup>89</sup> flexibility has long been shown where the courts have been able to identify with sufficient certainty objective criteria or machinery that can resolve any failure to agree (e.g. market rates for the goods) or where the terms on which the parties failed to agree are not essential to the enforceability of the contract (Peel 2020: 2:102). The Sale of Goods Act 1979, s.8(2), for example, allows the courts to determine the reasonable price that parties should pay for goods. More recently the UK Supreme Court in *RTS Flexible Systems Ltd v Molkerei Alois Müller GmbH*<sup>90</sup> showed itself willing, despite an agreement that negotiations would be subject to contract, to find that the parties had entered into the main contract. Here, the Court was able to refer to the parties’ detailed negotiations and their conduct to ascertain the terms of the main contract and held that the “subject to contract” requirement had been waived by the parties on the facts.<sup>91</sup> Further, as courts become more familiar with ideas such as relational contracts, there is greater acceptance that commercial negotiations will not always be

<sup>87</sup> “The parties shall conduct themselves in good faith both at the time the obligation is created and at the time it is performed or extinguished”: art. 1375, *CCQ*.

<sup>88</sup> Followed by *Barbudev v Eurocom Cable Management Bulgaria EOOD* [2012] EWCA Civ 548; [2012] 2 All E.R. (Comm) 963 especially at [44]–[46].

<sup>89</sup> *Empress Towers Ltd v Bank of Nova Scotia* (1990) 50 B.C.L.R. (2d) 126 (BCCA). [good faith being taken as best efforts]; *Labatt Brewing Co. v NHL Enterprises Canada L.P.* 2011 ONSC 5652 (Ont. S.C.J. [Commercial List]) at [79–80].

<sup>90</sup> [2010] UKSC 14; [2010] 1 W.L.R. 753.

<sup>91</sup> It should be noted, however, that such a finding is not lightly made and the court must find unequivocal agreement in circumstances where it would make commercial common sense to enforce the contract and, importantly, it would not conflict with the general principle that the court should not impose binding contracts on the parties which they have not reached. For arguments that this may raise conflicts with the actual intent of the contracting parties, see Davies (2010: 472).

adversarial (as assumed in cases such as *Walford v Miles*) and parties may willingly undertake duties of co-operation and fair dealing. Where the parties have expressly stated their willingness to do so, then, as Longmore L.J. observed in *Petromec Inc v Petroleo Brasileiro*:

“It would be a strong thing to declare unenforceable a clause into which the parties have deliberately and expressly entered... To decide that it has ‘no legal content’ ... would be for the law deliberately to defeat the reasonable expectations of honest men.”<sup>92</sup>

Even McKendrick (2021: 12.10) concedes that the strongest case for a duty to negotiate in good faith arises where the parties themselves have expressly agreed to such a term, requiring the courts to determine whether they favour the wills of the parties over concerns that such an obligation is too uncertain to enforce.

### Obstacles to Change

While there is greater impetus for change in Canadian, rather than English, law, both systems must overcome a number of obstacles before duties to negotiate in good faith can be recognised in commercial contract law. Buckwold (2016), while arguing in favour of such duties, conceded that the courts would have to overcome the problem of how to quantify damages, given that the courts would have to determine whether, acting in good faith, the parties would have reached agreement and on what terms. In *Petromec*, English judge, Longmore L.J., identified three key objections that must be overcome before a court can contemplate enforcing an obligation to negotiate in good faith. These relate to the *content* of the obligation undertaken (that it would be too uncertain to enforce (1) and difficult, if not impossible, to determine whether the negotiations had been terminated in good or bad faith (2)) and the nature of the *remedy* (3). Longmore L.J., in common with Buckwold, stressed the remedial problem: “since it can never be known whether good faith negotiations would have produced an agreement at all or what the terms of any agreement would have been if it would have been reached, it is impossible to assess any loss caused by breach of the obligation.”<sup>93</sup>

The question is whether the common law can overcome these obstacles. It is important to appreciate that two distinct scenarios arise. In the first, and closest to the performance context, the claimant is trying to enforce a duty to negotiate a term in an existing commercial contract. In the second, and more difficult situation, the claimant is relying on a pre-contractual agreement to negotiate the main contract in good faith. I will examine both scenarios below.

<sup>92</sup> *Petromec Inc v Petroleo Brasileiro SA Petrobas (No 3)* [2005] EWCA Civ 891, [121].

<sup>93</sup> *Petromec* *ibid.*, [116]. See also Lord Denning in *Courtney & Fairbairn Ltd v Tolaini Brothers (Hotels) Ltd* (1974) [1975] 1 W.L.R. 297, 301-302.

## Scenario One: A Duty to Negotiate Elements of an Existing Commercial Contract in Good Faith

In *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd.*,<sup>94</sup> the English High Court was prepared to uphold a dispute resolution clause that had expressly required the parties to seek to resolve a dispute by friendly discussions and within a limited period of time (4 weeks) before the dispute could be referred to arbitration. Here the court interpreted “friendly discussions” as implying good faith but, in this context, it was clear that it meant fair, honest and genuine discussions aimed at resolving a dispute. *Emirates* suggests therefore that where, in a long-term contract, the court is able to find sufficient objective criteria to enable them to enforce such a clause, it should be regarded as binding.<sup>95</sup>

In my view, changes in English and Canadian law have made it at least arguable that an express term to negotiate some element of the contract in good faith might be regarded as certain enough to be enforceable.<sup>96</sup> Indeed, in *Callow*, by identifying a duty to exercise a right to terminate in good faith, the court comes very close to doing exactly that. Much will depend on the context and the degree to which the court is able to determine the content of any duty. As noted above, in English law, a number of characteristics which we might regard as indicative of “good faith” behaviour may be identified from existing case-law. The Canadian courts are engaged in a similar pursuit, albeit one fueled by an underlying organizing principle of good faith. In both cases, reference will be made to the context of the contract and the nature of the parties’ relationship.

The argument would be, therefore, that in this scenario the courts may be able to overcome the *Petromec* objections. In the context of an existing contract, the courts may be able to identify appropriate behavioural standards from the nature of the agreement itself to provide sufficient content to the obligations, reflecting, to paraphrase Lord Steyn, the reasonable expectations of commercial contracting parties. The context of an existing contract may also assist in addressing what would be an appropriate assessment of damages. *Petromec* itself concerned an engineering contract containing a clause that provided that the parties would negotiate in good faith to reach agreement on certain extra costs for the upgrade of an oil production platform. Here the fact that the obligation to negotiate in good faith had been made as part of a complex agreement was regarded as significant, although ultimately any comments were obiter on the facts. What *Petromec* shows is that there is potentially scope for enforcing such obligations, provided that the objections outlined above can be addressed. In a recent decision, May J confirmed that the validity of such a provision would depend upon the court being satisfied that the traditional objections to

<sup>94</sup> [2014] EWHC 2104 (Comm); [2015] 1 W.L.R. 1145. For criticism, see Flannery and Merkin (2015). See also *Knatchbull-Hugessen v SISU Capital Ltd* [2014] EWHC 1194 (QB), [23] per Leggatt J; *United Group Rail Services Ltd. v Rail Corporation of New South Wales* [2009] NSWCA 177; (2009) 74 N.S.W.L.R. 618.

<sup>95</sup> Peel (2020: 2:103), however, argues, that *Emirates* is difficult to reconcile with earlier authorities and is influenced by public interest reasoning.

<sup>96</sup> For arguments against, see Peel (2010).

such clauses, raised by Longmore L.J. in *Petromec*, did not arise.<sup>97</sup> A further example may be found in the *Mid Essex Hospital Services* case discussed above.<sup>98</sup> Here an express obligation to co-operate in good faith was narrowly construed so that it did not impose a general duty of good faith but rather a duty focused on the efficient transmission of information and instructions to enable the Trust to derive the full benefit of the contract. This, stated the Court of Appeal, meant that the parties would work together, honestly endeavouring to achieve those stated purposes.

While there is very limited authority as yet, this does indicate that case-law on performance may encourage the courts to consider enforcing express duties to negotiate in good faith when they arise in a detailed, long-term contractual relationship giving the courts sufficient context to meet the uncertainties highlighted by *Petromec*. One should, however, anticipate English law to be far more conservative than Canadian law and that it will narrowly construe the term in question and verify that it is consistent with the rest of the contract. At this stage, we have only the groundwork for future developments. Whether this groundwork is developed remains to be seen, but it does represent a scenario where developments in relation to contractual performance may assist litigants in their arguments.

In *Emirates* however, the court identified a key distinction between an agreement to negotiate within a concluded contract and a bare agreement to agree. The latter, it argued, lacks the essential terms of a future fully concluded bargain.<sup>99</sup> This will be examined below.

### Scenario Two: A Pre-contractual Agreement to Negotiate in Good Faith

In this scenario, the parties have yet to commit beyond a preliminary agreement to negotiate in good faith, and are, therefore, still well aware of the risks of negotiations failing.<sup>100</sup> The courts do not have a detailed long-term contractual relationship from which to derive objective evidence of the content of any commitments the parties are willing to undertake. The question, therefore, arises: to what extent can the concerns expressed in *Petromec* about uncertainty in relation to the content of the obligation and appropriate remedy for breach be overcome?

Leggatt (2019, p. 111) has argued that the difficulties of overcoming these hurdles should not be overstated. An obligation to negotiate in good faith dictates a

<sup>97</sup> *Rosalina Investments Ltd v New Balance Athletic Shoes (Ul) Ltd* [2018] EWHC 1014 (QB) at [50] per May J.

<sup>98</sup> *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200; [2013] B.L.R. 265. However, the court refused to imply a term that the NHS trust would not act in an arbitrary, irrational or capricious manner when calculating service failures by the catering company or when making deductions from monthly payments in respect of those failures. See also *Hillas v Arcos* (1932) 43 Lloyd's List Rep. 359 (option to purchase in contract was vague but could interpreted with reference to other terms of the contract).

<sup>99</sup> *Emirates* (n 94), [59].

<sup>100</sup> See e.g. *Regalian Properties Plc v London Docklands Development Corp* [1995] 1 W.L.R. 212: "subject to contract" negotiations for a large-scale development held to signify that any costs incurred by either party in preparation for the intended contract would be incurred at their own risk.

*process*, not a result. Fundamentally, it does not require parties to negotiate successfully nor enter into a contract.

“Unlike in some civil law jurisdictions, there is no [general] duty at common law to negotiate contracts in good faith ... But I cannot see why parties should not enter into a binding agreement to negotiate with each other in good faith and limit the grounds in which they are entitled to break off those negotiations, if that is what they choose to do.”<sup>101</sup>

As Leggatt L.J. suggests, at times it may be a straightforward exercise to identify the content of the obligation. The parties may have expressly set this out or it may be regarded as self-evident e.g. not deliberately to lie to each other. It can therefore be argued, drawing on Canadian law, that we can identify a *de minimis* element of a duty to negotiate in good faith, that is, a duty to act honestly. Art. 2:301 of the Principles of European Contract Law (PECL),<sup>102</sup> while advocating more ambitious duties not to negotiate or break off negotiations contrary to good faith and fair dealing (para. 2), would agree—there is a minimum duty not to enter or continue negotiations with no intention of reaching an agreement with the other party (para.3).<sup>103</sup> The question, then, becomes the extent to which one can go beyond basic obligations such as honesty and not actively stringing the other party along without creating undue uncertainty rendering the obligations impossible to enforce.

It is submitted that in this scenario, going beyond the bare minimum will be problematic. Absent the context of a detailed agreement between the parties indicating what will be regarded as “good” contracting behaviour,<sup>104</sup> the courts have no point of reference enabling them to go beyond *de minimis* standards. Consider, for example, *Walford v Miles*, where the parties had very different objectives—here the claimants were seeking to purchase a business for £2million on the basis that it had been badly undervalued (their action was based on the fact it was really worth £3million). Given this background, how does a court ascertain the “reasonable” expectations of contracting parties in the light of such limited evidence of the parties’ intentions? Can we say the parties intended a duty to co-operate and disclose relevant information, when, on the facts, the claimants themselves in *Walford* would have been in breach of such a duty?

In short, it will be difficult for a court to determine what the parameters of any good faith and fair dealing obligations will be when it cannot draw on previous interaction between the parties. While Brownsword (1996, pp. 119–120) suggests that the court, in such circumstances, could rely on the contracting community’s own standards of decency, fairness, and reasonableness, this requires the courts to play a proactive role in determining what these standards actually are. In reality,

<sup>101</sup> (2019, p. 113).

<sup>102</sup> Lando and Beale (1999). See also Book II, Art. 3:301(4) of the Draft Common Frame of Reference (von Bar and Clive 2010).

<sup>103</sup> Commonly known as “stringing along” – an obvious example would be the situation in *Callow*, discussed above.

<sup>104</sup> Query whether industry usages and trade practices would be detailed and consistent enough to fill this gap.

it requires the courts to set the standards that will police the parties' agreement. While such a step would not trouble a civil lawyer who accepts that civil law courts will impose normative obligations on the parties for reasons of public policy, it is difficult to reconcile with the traditional common law position that the role of the courts is to enforce the will of the contracting parties. It should not be forgotten that the civil law approach is premised on a specific view of the role that the State should play in policing the substantive terms of the agreement, with the legislature and the courts acting to ensure compliance with broader social values and objectives (Pargendler 2018, p. 146). As Trakman and Sharma (2014, p. 616) concede, the more the common law courts move beyond the clear evidence of the intentions of the negotiating parties to rely on social norms, the more controversial its ruling will be. This was certainly the view of the UK Supreme Court in its 2021 decision in *Times Travel (UK) Ltd v Pakistan International Airline Corp* ([2021] UKSC 40) which confirmed the English courts' reluctance to engage with the "civilian" idea of a general principle of good faith in contracting; Lord Burrows raising the objection that any such general principle would require the court, not the parties, to determine what would be commercial unacceptable or unreasonable behaviour.

Even if the common law courts are prepared to go so far as to accept a limited duty to negotiate in good faith, this does not answer the remedial question. The court in *Callow* was divided whether expectation and reliance damages should be awarded. Expectation damages—placing the claimant in the position he/she would have been in had the duty been fulfilled<sup>105</sup>—appear to be highly speculative in this context. In essence, they represent the loss of a chance of a hypothetical contract. While loss of chance damages can be awarded in contract law,<sup>106</sup> it is not a straightforward process; the court examining whether there was a “real” or “substantial” (not a speculative) chance and that the loss of chance is not too remote.<sup>107</sup> There is authority that where expectation damages are too speculative, the court may confine the claimant to reliance damages.<sup>108</sup>

The obvious response, and one arguably more consistent with the view of Leggatt J. that the law is regulating a process, not the result, of negotiations, would be to award reliance damages as a matter of course. Art. 2:301, PECL, for example, accepts that the correct remedy for stringing someone along should be reliance damages.<sup>109</sup> The drafters give the example of a person who has been asked to visit a site to discuss future employment, all expenses paid, but who, in reality, had no intention of taking up the position. Here, the remedy would be to require the defendant to refund the money paid to him. Reliance damages will generally, therefore, reflect wasted expenditure and only rarely opportunity costs. Further, the court will not permit claims for expenditure deemed to be at the negotiator's own risk and there is

<sup>105</sup> *Robinson v Harman* (1848) 1 Ex 850.

<sup>106</sup> *Chaplin v Hicks* [1911] 2 K.B. 786; *Emirates* (n 94), [47].

<sup>107</sup> *Allied Maples v Simmons & Simmons* [1995] 1 W.L.R. 1602.

<sup>108</sup> *McRae v Commonwealth Disposals Commission* (1951) 84 C.L.R. 377.

<sup>109</sup> Lando and Beale (1999: 190). At best, the party can try to seek loss of opportunity, but full expectation losses are rejected. See also Von Bar and Clive (2010: 248).

also the question of causation: would these costs have been recouped even if the defendant had negotiated in good faith? Given these factors and that, realistically, reliance damages will be lower than expectation damages, combined with the high cost of litigation in England and Canada, only a very determined litigant would be likely to pursue such claims through the courts.

There is a risk, therefore, that any such duties would in most cases be of symbolic interest only. If this is so, common law legal systems should consider carefully whether, given the uncertainty in terms of the content of, and remedies for, such duties, and the potential for such liability to provide a disruptive precedent, such a development would be desirable.

### From Performance to Pre-Contractual Negotiations: A Step Too Far?

If we reflect on the above analysis, two conclusions stand out. First, in the context of *performance* duties, the courts are assisted in determining the content of the good faith duty by drawing on the details of the contract and the long-term relationship between the parties. The courts seem willing to support express and implied good faith terms where the parties have been working together over a long period of time and their interests are intertwined and informed by prior practice. However, in the absence of this context or any specific mechanisms established by the parties, it becomes difficult to determine the precise content of any duty to negotiate in good faith without falling back on what the courts themselves regard as good practice. This indicates that if the courts are contemplating enforcing duties of good faith in pre-contractual negotiations but wish to adhere to the common law practice of respecting the intentions of the contracting parties, then any such duties must be interpreted narrowly. Such a conclusion is supported by the fact that neither Canadian nor English law have gone further than this.

Secondly, this suggests that the real debate with which we should be engaged is whether the courts should enforce *de minimis* good faith obligations, including, for example, a duty to act honestly and not string along negotiations with no intention of contracting. The common law way is to proceed cautiously and incrementally. Yet even these duties are not clear-cut. While *Bhasin* regards a duty of honesty as easy to apply, posing no risk to commercial certainty,<sup>110</sup> McKendrick (2015, pp. 203–204) warns that a duty of honesty might not be as straightforward as some commentators (or judges) seem to believe. Peel (2010, p. 52), for example, advocates taking a very narrow view and argues that honesty merely requires parties to avoid misrepresentations which is part of the law in any event. *Callow* highlights a further question: how far does such a duty extend beyond not telling lies? Does it extend, for example, to evading questions or to non-disclosure of salient information? We might even regard *Callow* as less than clear-cut. Were the actions of Baycrest in not disclosing it did not intend to renew the winter contract sensible management practice to avoid poor performance (or even breach) of the summer contract, or dishonest and misleading

<sup>110</sup> *Bhasin* (n 57), [80].

behaviour? Is the commercial morality of reasonable men (or women) so unambiguous? While intentionally stringing someone along seems to satisfy this test, proving intention is never a straightforward exercise. There is a narrow dividing line between indecision, over-optimism and intentionally misleading someone as to your intentions. If I say that I intend to contract but do not mention that this is based on a pay rise I fully expect to get (but unexpectedly do not), am I being dishonest or stringing that person along? The answers to such questions are not self-evident.

At best, then, if—and it remains a big “if” at present—the common law accepts a *de minimis* duty to negotiate in good faith, it would have limited content and would likely be confined to reliance damages. Any broader duty would require the common law courts to impose their own views of commercial morality, fundamentally conflicting with the common law perception that it is for the parties to determine the content of any contractual agreement and the court’s role to enforce their intentions.<sup>111</sup> It is not coincidental that in accepting a broader notion of good faith than the English courts, the Canadian courts have been influenced by the civilian ideas of Quebec, leading it to favour a principle, rather than an implied term, of honesty or good faith. It is perhaps ironic that after over 40 years’ membership of the EU, England and Wales continues to represent a purer common law approach which manifests itself in ongoing reluctance to accept duties of good faith, notably during the negotiation period.

## Conclusions

Good faith continues to divide the common law world. While the idea of duties of good faith in performance seems to be gaining ground at least with respect to relational contracts, there is still considerable opposition to its extension to the negotiation period. This article, by reflecting on developments in England and Wales and Canada, has highlighted that moving from express or implied terms requiring good faith (or, as in Canada, a minimum standard of honesty) in the *performance* of long-term contracts to a duty to *negotiate* in good faith is a significant step. The common law approach to construction of contracts and the roles it gives to judge and contracting parties involves the court “revealing” the implicit assumptions of contracting parties. In both systems, “good faith” has been approached by examining the parties’ relationship, as evidenced by their conduct and the contents of the commercial agreement, to gain a contextual understanding of what commercial good faith means in relation to this particular agreement. There is therefore no one definition of “good faith”. It represents what Snowden J. (2021) described in a recent lecture as a portmanteau term. In both systems, it is the context of the parties’ relationship that enables the courts to determine which elements of “good faith” are relevant in each individual case.

It is therefore inevitable that it would be far more difficult to extend *Yam Seng* and *Bhasin* to pre-contractual negotiations. At best, as my study has shown, any duty

<sup>111</sup> *Prime Sight Ltd v Lavarello* [2013] UKPC 22; [2014] A.C. 436, [47] per Lord Toulson.



of “good faith” at this stage would be likely to be confined to the minimum duties that commercial parties could be expected to adhere to in the absence of objective criteria specified by the parties. Yet even focusing on limited duties such as honesty and not intentionally stringing someone along, there are questions of interpretation and how to determine the correct remedial response. Will parties be confined to wasted expenses and, if so, will parties be incentivised to sue? There is a real danger that even if a narrow duty were found to be acceptable, it would have no more than a symbolic value.

At present, for the English courts at least, it seems unlikely that *Yam Seng*-based reasoning will extend to negotiations per se, although a case can be made for considering the enforcement of duties to negotiate within long-term contracts where sufficient information exists, either from the terms of the contract or the parties’ prior practice, to determine the content of the obligation and the appropriate remedial response. However, the law is not static. Lord Leggatt was elevated to the UK Supreme Court in April 2020 and is now in prime position to develop ideas found in *Yam Seng* and *Petromec* in English contract law (although was not present in the *Times Travel* case mentioned above). The Canadian courts continue to review the application of *Bhasin* and inevitably its extension beyond performance will have to be addressed. There is, therefore, only one thing on which we can be certain: the debate whether the common law should embrace an extension of good faith into the negotiation period is far from over.

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