VALEDICTORY LECTURE

"THE LAW OF CONTRACT IN THE NEW MILLENNIUM"

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INTRODUCTION

The notion of a Valedictory Lecture is something completely new for the ANU – or at least for the Law School. We have not been very strong on Inaugural Lectures for new Professors, and so far as I can recall the only other Inaugural Lecture (apart from that given by John McMillan a fortnight ago) was that given by Patrick Atiyah in 1970. But the idea of an Inaugural Lecture is reasonably common – at least in Faculties apart from this one. Law Reviews regularly contain printed versions of them, and I have always understood an Inaugural Lecture to be an opportunity for the newly appointed Professor to demonstrate his or her expertise in a chosen field – a task which John performed with resounding success a couple of weeks ago. But the very fact that Valedictory Lectures are so rare gives me, I think, a considerable degree of latitude in deciding what I should say.

I have taken the invitation to give this lecture as an opportunity to look back over the 30 years that I have been teaching Contract Law here at the ANU, to reflect on the changes that have occurred, and to put forward at least some views on where the law might go from here.

CONTRACT LAW IN THE EARLY 70s

Although I may not have realised it at the time, Contract Law in the early 70s, when I first started to teach the unit, was scarcely a proper subject of academic study. To talk of an aspect of the law implies that there are rules and principles which guide the behaviour of those who enter into contracts, but really the content of the subject was little more than a series of illustrations of how (fortunately litigious) parties had attempted to organise their affairs – but had failed adequately to do so, leading to their appearance in Court, and subsequently in the Law Reports. And most of the time and effort of Court appearances was concerned with attempting to divine the true intention

of the parties, hampered at times by arcane rules of evidence such as the Parol Evidence Rule.

The only "rules" which might be regarded as having any normative value were such obvious principles as that there must be an exchange between the parties (ie, that consideration was necessary and that a court should be able to spell out of the parties' words and conduct an offer that had been accepted). It would also be fair to characterise the "postal acceptance rule" as another principle, and the doctrine of privity, together with the basic principles for the assessment of damages – such as the remoteness rules, the obligation on the innocent party to mitigate the loss, and the denial of effectiveness of a clause which was regarded as imposing a penalty on breach. But apart from these instances, much of the content of the course was to be found in single instances of judicial attempts to determine the parties' intentions.

This freedom from regulation and control – this *laissez faire* principle that the parties are competent to put whatever they like into a contract – had then, and to some extent continues to have, a variety of consequences.

One result of freedom of contract was that conscience played no part whatever in the formation and enforcement of contracts.

Another effect of the fact that "the law of contract" was no more than a set of default rules which applied on relatively few occasions was that parties to a contract (or other set of promises) in a commercial setting were free essentially to ignore the law and rely on their own (different) sanctions to ensure compliance with the undertakings given.

One example of this approach, dating from the early years of the 20th century, is Bankers Commercial Letters of Credit – the principal way in which international trade used to be financed. It is widely accepted that, at least in the period before the seller acts on the Letter of Credit, the arrangement breaches the Privity Rule, but no banker would consider relying on that supposed "defect", as it would be commercial suicide to do so.

And these days those who have dealings with bankers apparently continue to rely on commercial pressure rather than legal rules to ensure that the banker abides by its

word. A Performance Bond or Guarantee is paid for by a Contractor, but given in favour of the Principal who has engaged the Contractor. So far as the law is concerned, the Bank's Guarantee is a "gift promise", or it breaches the Privity Rule. For either of those reasons, to be enforceable it should be in a deed. However, I understand that such Bonds are regularly given in the form simply of a letter, and, once again, the only thing which prevents a banker from relying on this technical unenforceability is the commercial need to continue to carry on this sort of business.

In the course of conducting two-day courses on Contract Law for those who actually negotiate, draft and administer contracts – but who have no formal legal training – I have discovered that many commercial arrangements these days – for some reason particularly in the construction industry – are carried out with very considerable lack of formality. It is, I gather, a relatively common occurrence for a multi-story building to have reached the fourth or fifth floor before a formal contract for its construction is signed. An extreme example of this attitude was the arrangement for the installation of all the lifts and escalators on a high-rise building in Brisbane. All of the required work had been carried out, and paid for, while a formal contractual document was shuttling between the head offices of the respective companies.

Clearly, in each of these examples, there was a contract between the parties, and if anything had gone wrong it may well have taken the lawyers on both sides quite a long time to sort out the precise nature of the obligations that each side had undertaken. But, because of the trust that each side placed in the other, and because of the commercial necessity of getting a job started once the broad outlines are in place, the respective parties were prepared to dispense with an over-reliance on the law.

And, although I have heard about these practices only over the past eight years or so, I have no doubt that they developed in the yeas when the law of contract was no more than a minimalist collection of default rules.

One may add, parenthetically, that this great freedom from regulation which used to characterise the whole law of contract – and which still applies to much of that body of law – can work to a party's disadvantage. Since the law allows parties to write their contract in any way they please, it requires the parties themselves to foresee any

difficulties that may arise with enforcement, and to make provision for themselves. At least in relation to commercial contracts, the equitable remedies of Specific Performance and Injunction are of no practical use, and the only remedy that the law will grant is damages. And, furthermore, in the absence of a contractual specification, the plaintiff must prove the amount of its loss before it is entitled to any more than nominal damages.

The problems inherent in this lack of regulation – this refusal to intrude – can be seen most clearly in any Government contract for the outsourcing of the provision of services to the public – and this includes any or all services, from the collection of garbage for a local council to finding employment for the long-term unemployed. Even though the contractor is in breach, since the services are to be provided to members of the public, the government body has, prima facie, suffered no loss and so – in the absence of express provision in the contract – can neither sue for damages nor withhold future payments, and even if the breach were serious enough to warrant termination, it is doubtful whether that would be a realistic option in many cases.

CHANGES OVER THE LAST TWENTY YEARS

The law **of contract** has not changed very much, if at all, over the last twenty years. The common law principles described above are still much as they were when I started teaching the subject. But there has been a considerable change in other closely related areas of the law which have impacted considerably on those who enter into contracts. As has been pointed out on many occasions over that period, contracting parties are subject to a wide variety of rules with normative content which determine what each of them may (or may not) do. Let me provide a few examples.

Restitution and Frustrated Contracts

The first example comes from the area of the common law closely related to the law of contract, that of Restitution. In *Codelfa Construction v State Rail Authority* the High Court was faced with a contracting party – the State Rail Authority – which had received all of the benefit which had been promised under the contract – that is, the construction of the tunnels and stations for the Eastern Suburbs Railway in Sydney – but which was seeking to adhere to the strict letter of the contract to deny Codelfa payment for any more than was specified in the contract, despite the fact that Codelfa

had been forced to spend approximately one third longer than the 130 weeks specified, because of an injunction obtained by the residents of Edgecliff to prevent Codelfa carrying out its tunnelling work between 10 pm and 6 am.

One might add as an aside that the reason for the State Rail Authority being so perverse was that it had been instructed by the then Minister for Transport in New South Wales to stick to the precise terms of the contract. The Minister was under a certain amount of political pressure to honour his promise that the Eastern Suburbs Railway would be completed within the budgeted figure. And in those days we were all innocent and did not realise that political promises may be classified as “core” and “non-core”

Although the principal argument before the High Court was that a term should be implied into the contract which would ensure proper remuneration for Codelfa, that argument was rejected. But justice was done to Codelfa by breathing life into the moribund doctrine of frustration – a doctrine which had achieved considerable prominence during the First World War, but which had been gradually slipping into one of those forgotten byways of the law ever since. By declaring the contract to have been frustrated by the issue of the injunction, the Court was able to free Codelfa from the shackles of a very tightly-drawn contract. And, since Codelfa had in fact completed the required work, to the complete satisfaction of the State Rail Authority, the latter was required to pay a reasonable amount for that work, by the operation of principles of Restitution.

One might add, as a further aside, that by the time the High Court handed down that decision, the political imperatives which had been operating on the Minister for Transport at the time of the completion of the tunnelling work had long since evaporated. Indeed, by the time of the High Court decision, the Government may well have changed complexion, and the new Minister for Transport could place all the blame for the increased costs on the former Government.

The Infusion of Equity

It is here, of course, that the greatest changes have taken place. By recognising the role that unconscionability plays in informing doctrines of Equity, and by importing those doctrines, and that guiding theme of unconscionability, into the relations

between contracting parties, there has developed a new wave of interventionism by the courts into a relationship which had previously been completely free of judicial proscription. As Paul Finn remarked some years ago,

The concept of unconscionability captured the legal imagination in Australia. The circumstances where unconscionability now plays a leading role in regulating the conduct of parties, whether in negotiating for a contract or in seeking to enforce its terms, cover a wide area.

(a) Promissory estoppel

After some preliminary discussion of the idea in *Legione v Hateley*, it was, of course, in *Waltons v Maher* that the High Court accepted that promissory estoppel was no longer only a shield, to be used defensively, but could also be a sword to be used aggressively to permit the enforcement of gratuitous promises, and other promises which, for one reason or another, could not have been enforced at common law.

The *Waltons* case itself demonstrates that promissory estoppel can be used to prevent reliance on the Statute of Frauds. Other possible uses of the concept as a means of tempering the strict requirements of the common law include:

- Policing the tender evaluation process in the **private sector**, in the same way that the *Hughes Aircraft* case regulates that process in the public sector

- Allowing for further limitations on the Privity Rule [see the comments of Brennan and Deane in *Trident*, but cf Mason's response thereto]

- Ensuring that modifications to a contract are adhered to, even though the contractual procedure for changes has not been complied with [see *Update Construction*].

- Another way of putting that point is to say that promissory estoppel renders nugatory any contractual provision for variations in the face of the parties' conduct

- Relieving a party of the "normal" consequences of breach, if the other party has made it clear that performance is pointless – see *Foran v Wight*

- Possibly (and at long last) overthrowing the Rule in *Hoyt's v Spencer* – a rule which allows a party to a written to contract to persuade the other party to enter into the transaction on the faith of an oral promise that not all of the terms of the written contract will be enforced, and then, once the written contract has been entered into, to renege on that oral promise.

(b) The process of formation of a contract

The intervention of Equity has played a major role in ensuring that one party, while in the course of negotiating for a contract, is not treated unconscionably by the other. Thus

- If one of the parties is labouring under a mistake, and the other is aware of that fact, the mistaken party may resile from the resulting contract – see *Taylor v Johnson*.

- It is possible that if both parties are mistaken over some matter fundamental to the contract, it will be regarded as unconscionable for one to take improper advantage of any windfall accruing from the discovery of the mistake, permitting the contract to be set aside – see *Lukacs v Woods*

- A doctrine of "catching bargains" which 20 years ago was thought to be confined to spendthrift heirs and at least one drunken Queenslander was transformed by *Amadio* into a general principal of protection for anyone suffering a position of special disadvantage

- In the light of *Garcia*, banks and other financial institutions must now take care to ensure that if a business loan for one member of a family is guaranteed by another member of the family, that guarantor has independent advice about the transaction, and fully understands the nature of the obligations being undertaken

- And, finally, economic duress, though scarcely ever applied in this country, is acknowledged as a ground for the avoidance of a contract based at bottom on principles of unconscionability

(c) Relief against forfeiture

One circumstance, at least, in which principles of unconscionability will prevent a party from enforcing the terms of a validly concluded bargain is that in which that enforcement would lead to a purchaser of an interest in land forfeiting that interest. Equity's jurisdiction to relieve against forfeiture is one which was developed in the latter years of the 19th century, but that development was severely retarded by decisions of the Privy Council in the early years of the 20th century. Fortunately, however, the High Court, in *Legione v Hateley* in 1983 and *Stern v McArthur* in 1988, have revitalised that jurisdiction.

(d) Penalty rules

Closely allied to relief against forfeiture are those principles of construction by which a court may deny enforceability to a contractual provision for the payment or retention of money on breach by one of the parties.

The penalty rules are closely allied to relief against forfeiture for two reasons:

First, they are both concerned with **substantive defects in the contract** – that is a ground for denying enforceability which arises from the terms of the contract itself, and not from any defect in the process of formation.

And, secondly, both are based fairly and squarely on notions of **unconscionability** – on seeking to ensure that each party enforces obligations freely entered into by the other contracting party only in accordance with good faith and good conscience.

Although for some considerable time the penalty rules were regarded as no more than rules of construction, and as requiring no more than a comparison between the greatest loss likely to be suffered by one party on the other's default and the amount stipulated in the impugned clause, considerable development occurred to this area of the law in the 1980s.

First, in *O'Dea v Allstates Leasing* the High Court extended the applicability of the relevant rules to encompass clauses which seek to enforce obligations, the character of which has been altered by the fact of the defaulting party's breach. And, secondly, in

Esanda Finance v Plessnig the same court made it clear that the basis for the denial of enforcement was solely unconscionability.

After the *Plessnig* case, it is possible that a clause may be enforced, even though it requires the payment of a sum which is greater than a reasonable estimate of the loss likely to be suffered as a result of the particular default, so long as that sum is not so great as to be regarded, in all the circumstances, as unconscionable.

Negligence and the doctrine of privity

Although the High Court, in the *Trident* case, refused to abolish the doctrine of privity, and the majority made only one limited exception to that doctrine, an exception which in any case had been legislated for, in the *Insurance Contracts Act* in relation to contracts entered into after the passing of that legislation, subsequent decisions of the High Court have made further inroads into the privity doctrine by use of the tort of negligence. I refer, of course, to *Bryan v Maloney* and *Hill v Van Erp*.

In *Bryan v Maloney*, a negligent builder in Launceston was held liable to the third owner of the house he had built, as she happened to be the owner at the time that Bryan's negligence came to light in the subsidence of the house. But in coming to that conclusion the High Court, in effect, imposed a transmissible warranty of quality on all those who engage in building work – a result foreshadowed by Brennan J in his dissenting judgment. Whereas Mr Bryan's contract with the original owner might have made whatever provision the parties agreed to as to the extent and duration of his liability, once the High Court established that he also owed a duty of care to any subsequent owner, his ability to control the extent and duration of his liability was severely curtailed. Indeed, it is difficult to see how Mr Bryan – or anyone engaged in building work – may limit their liability, vis-a-vis any owner other than the first.

Hill v Van Erp is similar, in imposing obligations – in this case on a solicitor, in the drafting and execution of testamentary dispositions for a client – which enure for the benefit of the intended beneficiaries of those testamentary dispositions.

In both of these cases, because of the apparent inability of the respective defendants to limit a liability which springs, initially, from a contract, it might be said that the High Court has taken the law one stage beyond an abrogation of the privity doctrine. If, in

the parlance of United States law, the respective plaintiffs in each of the above cases were regarded as an intended beneficiary of the terms of the contract entered into between the defendant and another party, the plaintiff's rights would be based fairly and squarely on the terms of that contract. By basing the defendant's liability in negligence rather than contract, it has quite possibly been enlarged.

Changes wrought by statute

One further means by which the law applicable to contracting parties has been radically reformulated is by statute. While there has been a steady stream of legislation which corrects perceived difficulties and seeks to enhance the law, the most fundamental change has come from the *Trade Practices Act* and equivalent provisions in the *Fair Trading Acts* of the States, the Territories and New Zealand.

Section 52 and its equivalents, with its prohibition on misleading conduct, has revolutionised the whole process of negotiation, since anything said in the course of negotiation – and that includes negotiation for a change to an existing contract as well as negotiation for a new contract – may be the basis for at least a claim by the recipient of that information if it turns out to be false.

Furthermore, section 52 imposes **strict liability**, and renders irrelevant any plea by the defendant that the mistake in the information provided was wholly inadvertent, or that the information had originally been provided by a third party in whom the defendant had placed complete trust.

And, at least as the law stands at present, in the light of *Henville v Walker*, in a claim for damages under section 82, there is no concept of proportionality of blame. However naive, foolish or overly optimistic the plaintiff might have been, and however great might have been the effect of that naivety, folly or optimism on the plaintiff's resulting loss, if that loss can be shown to have been caused, at least in part, by the defendant's misleading conduct, the latter is liable for all the loss flowing therefrom. We await the decision of the Full Bench, in the *I & L Securities* case, to see if there is any room for a possible reduction of damages to take account of the effect of the plaintiff's own conduct on the loss that has been suffered.

And, while section 52 has undoubtedly raised the standard of commercial behaviour in this country (and in New Zealand) one must not forget the wide range of **remedies** available under **section 87**. Although the section is not relied on to any great extent, it may be used to allow a court to amend a contract in any way which seems just in order to remedy the effect of the defendant's misleading conduct.

There are surely echoes, in the flexibility of the remedies available under section 87, of the flexibility developed by the courts in providing a remedy for a plaintiff who successfully relies on estoppel.

Section 51AC

One other provision which deserves mention in this context is section 51AC – the section which is intended to prevent "big business" from acting unconscionably in relation to "small business" – at least so long as the transaction in question is for less than $3 million.

It had been recognised for some time that the unconscionable dealings principle revitalised by *Amadio* was not entirely adequate for contemporary commercial conditions in Australia, since the *Amadio* doctrine is limited to *individuals* who are in a "position of special disadvantage". But a small business – which has incorporated solely for the purpose of protecting some of the owner's assets – can be just as much in the same position of "special disadvantage" and may well need the same sort of protection. Hence section 51AC, under which *any* entity (other than a publicly listed company) can claim that it is the victim of unconscionable conduct engaged in by "a corporation".

The archetypal victim for which the section is primarily designed is either a tenant (other than the anchor tenant, obviously) in a shopping mall, or a franchisee.

The section came into force as recently as 1 July 1998, so that, in normal circumstances one would have to wait some few years for any body of case law to develop to flesh out the bare words of the section. However, although very few (if any) victims have themselves commenced proceedings under this section, the ACCC is very actively pursuing that role on behalf of the victims. There are already some

few decisions, from which emerges at least a shadowy image of what constitutes unconscionability in these circumstances.

THE PROCESS OF LAW REFORM

Reviewing all of these changes that have occurred in the law relating to those engaged in contracting led me to contemplate the differing processes of law reform which some of the above examples bring to light. While I have no firm views on the benefits of judicial decision-making over legislative change, the difference in process is profound. One may take, as examples from each type of change, the decision in *Waltons v Maher* on the one hand and the enactment of section 51AC on the other.

The decision in *Waltons v Maher*

As I have already mentioned, the decision is of immense importance to commercial life in this country. And, to read the judgments, especially those of the High Court, there is a sense that the conclusion is pre-destined. From the time of *Crabb v Arun District Council* in 1976, the law, especially in England, had been heading in the direction of acknowledging promissory estoppel as a sword as well as a shield. But even by 1988 English law had not moved that far, although the distance that the High Court had to travel from accepted principle to arrive at its conclusion was not far.

But, while the result in *Maher's* case might appear pre-destined, it was surely a random concatenation of facts that led to that conclusion. Certainly, one needed the fact of a promise, seriously made, which was relied on by Maher to his detriment in such circumstances that it would have been unconscionable to allow the promisor to resile from that promise. But, equally importantly, one needed, as the recipient of that promise, a person with very considerable determination and a well-developed fighting spirit.

The essentially random nature of the decision in *Maher's* case is attested to by the fact that, for all the developments in the law in England before it was decided, the courts in that country have still not taken promissory estoppel to the same position that it enjoys here.

And, although my information is only second-hand, I understand that Mr Maher was, indeed, a person of very considerable determination and spirit.

As most of you are no doubt aware, Waltons Stores was, at the time of the events in Nowra that led to the case, owned by Alan Bond. Now, Mr Bond may not have been a very *good* businessman – one need recall only his purchase of Channel Nine from Mr Packer for $1 billion and his subsequent sale of the station back to Mr Packer for a few million, or the fact that he was able to go bankrupt, in Australia, while owning a brewery to realise that his business acumen was not necessarily of the highest order. But I understand that Mr Bond was astute to use the apparently applicable legal principles – such as that a contract for the lease of an interest in land could only be enforced if it were in writing – to their fullest extent in his dispute with Mr Maher. Consequently, I gather that Mr Maher had to fight every inch of the way to obtain what he saw as justice. And, who knows whether, by the time the High Court handed down judgment in his case, ordering Waltons to pay damages in lieu of specific performance, Waltons had not gone into liquidation, leaving Mr Maher covered in honour for having helped to develop the law, but with very little monetary compensation for the detriment he had suffered.

As an aside, I might mention – for the benefit of those of you who are interested in the law of negligence – that I have already put in train a proposal to erect a plaque on Ballast Point in Sydney Harbour. The area has recently been purchased by the N S W Government, and the plaque would commemorate the fact that it was there that the good ship "Wagon Mound" berthed in November 1951 to refuel, and from which the fuel-oil overflowed, and spread down the bay to the Sheerlegs Wharf before catching on fire. Once that project has been successfully prosecuted, I plan to lobby for the erection of a similar plaque in Nowra, to be placed on the building which Mr Maher constructed, initially to Waltons' specifications.

The enactment of section 51AC of the *Trade Practices Act*

The process of law reform which gave us promissory estoppel was relatively brief – less than five years elapsed between Mr Maher's making a start on the building and the High Court handing down its judgment. But, for all the relative brevity, it was extremely expensive for Mr Maher, and, in economic terms, all of those who can now

recover for having relied, to their detriment, on a promise which is not supported by consideration, are "free loaders".

That process may be compared with the enactment of section 51AC of the *Trade Practices Act*. That reform was accomplished at no personal cost to any individual – but rather at considerable collective cost of Committees and Commissions of Inquiry, not to mention the Parliamentary time involved. But the tardiness of the process is staggering. The first move for inclusion of provisions in the *Trade Practices Act* which would prohibit unconscionable conduct, and which would protect small business, was made in 1976, by the Swanson Committee and in the next twenty-two years there were no fewer than seventeen major reports or draft legislation seeking to achieve the same result. There is no need to refer in detail to this lengthy cavalcade of the reform process. It is, however, perhaps worth bearing in mind that the whole process was close to being scuttled in the first half of 1997.

The bi-partisan Reid Committee had, in May 1997, presented a report which proposed reforms of the *Trade Practices Act* very much along the lines of what is now section 51AC. However, the Government's response was, in the first instance, the responsibility of the then Minister for Small Business, Geoff Prosser. It was, perhaps, ironic that reforms aimed at protecting small businesses which were tenants in major shopping malls should be the responsibility of a person who was himself a major landlord of retail business premises. Fortunately, Mr Prosser's business interests came to light not long thereafter, and he was forced to resign his portfolio, leaving carriage of the reforms with the new Minister for Small Business, Peter Reith.

IMPLIED OBLIGATIONS OF GOOD FAITH IN PERFORMANCE

Despite the considerable changes that have taken place in commercial relationships over the past 25 years, there is one area about which contention still rages. There is a movement in some quarters to imply into all contracts an obligation that both sides will observe good faith in the performance of the contract.

The movement started with Paul Finn inviting Horst Lücke to present a paper on "Good Faith and Contractual Performance" at a seminar here at the ANU in 1987. That paper was published in the resulting "Essays in Contract", and the ideas in it were seized upon by Priestley JA in *Renard Construction v Minister of Public Works*

when he first gave a judicial blessing to the notion of good faith in performance of contracts. The views of Priestley JA were, in turn, relied on by Finn J in the *Hughes Aircraft* case in finding the same implied obligation, and both of those judgments were the basis of the unanimous conclusion of the NSW Court of Appeal in the *Alcatel* case that the implied obligation of god faith applied to the performance of a lease.

This view has been expressed most recently by the NSW Court of Appeal in *Burger King Corp v Hungry Jack's Pty Ltd* [2001] NSWCA 187. As their Honours said, at para [159]

> Courts in various Australian jurisdictions have, for the most part, proceeded upon an assumption that there may be implied, as a legal incident of a commercial contract, terms of good faith and reasonableness.

It must, however, be acknowledged that there are some voices raised against the whole idea of a general implication of an obligation of good faith. The objections generally take either of two possible views: first, that the concept of "good faith" is so inherently uncertain as to be incapable of providing a basis for the implication of contractual obligations, and secondly that the concept is quite foreign to the notion of contract as understood in Australian law.

(a) Uncertainty

The objection of uncertainty is easily dismissed, on four grounds, if not more.

First, my colleague Jane Stapleton, basing her arguments primarily on English law when presenting a paper for the *Current Legal Problems* series of lectures, was able to show convincingly that there are, at the very least, well-settled "core principles" of the notion of good faith.

Secondly, my colleague Joachim Dietrich, in a paper presented last year to a Conference of the Faculty's Centre for Commercial Law, and basing himself to a considerable degree on cases from the United States, also had little difficulty in establishing that the concept of good faith has achieved a sufficient degree of certainty in that country for us in Australia to have no qualms about adopting the notion.

Thirdly, a majority of the New South Wales Court of Appeal (Kirby P and Waddell A-JA, Handley J dissenting) in *Coal Cliff Collieries v Sijehama* (1991) 24 NSWLR 1, recognised, at least in principle, the validity of an express agreement to negotiate in good faith. Their Honours were prepared to give sufficient content to that notion to accept that it could be the basis of a binding contract.

And, fourthly, Einstein J, in *Aiton Australia v Transfield* [1999] NSWSC 996 at paras 154-155, in upholding, at least in principle, an agreement to conciliate disputes under a contract in good faith, pointed out that

> the courts have always avoided hampering themselves by defining or laying down as a general proposition what shall be held to constitute fraud. Yet, however difficult it may be to define what fraud is, it is relatively easy to identify some of the elements which must necessarily exist.
>
> In the same way, the Court ought to be wary in the extreme of hampering itself by defining in any exhaustive way or by laying down as a general proposition the ambit of what will constitute a compliance with or failure to comply with an obligation to [carry out a contractual obligation of] good faith

(b) Good faith is foreign to common law precepts

At least three members of the current High Court Bench have suggested, in passing comments, that they regard the concept of good faith in performance of contracts as being foreign to the notion of contract law in Australia.

In *Service Station Association Ltd v Berg Bennett & Associates* (1993) 45 FCR 84 at 96, Gummow J, then of the Federal Court, after acknowledging the intervention of Equity in commercial relationships, considered that

> It requires a leap of faith to translate those well established doctrines and remedies into a new term as to the quality of contractual performance, implied by law.

And, much more recently, in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5 (14 February 2002) the High Court was pressed with an argument that a term of good faith should be implied into the contract between the parties. The majority found it unnecessary to consider the matter, and made no comment on the arguments which had been presented. However, Kirby J, at

least, while pointing out that, in the circumstances of the case it was unnecessary to explore the question, let fall the comment, at para [87], that

> In Australia, [any implied term of good faith] appears to conflict with fundamental notions of *caveat emptor* that are inherent (statute and equitable intervention apart) in common law conceptions of economic freedom.

Callinan J appears also to be of a similar view. He concluded his judgment (at para [155]) by saying

> In view of the conclusion I have reached, it is unnecessary to answer the questions raised by the rather far-reaching contentions of the appellant … whether both in performing obligations and exercising rights under a contract, all parties owe one another a duty of good faith; and the extent to which, if such were to be the law, a duty of good faith might deny a party an opportunistic or commercial exercise of an otherwise lawful commercial right.

(c) But good faith *is* implied in particular contexts

While not necessarily answering any of those objections, it must be observed that the concept of good faith is already a part of the common law of contract, as an implied term in particular contexts. All that is required – albeit, in the words of Gummow J, a "leap of faith" – is an acknowledgment that the particular instances are species of a wider genus.

"Subject to finance"

Since at least the decision of the High Court in *Meehan v Jones* in 1982, it has been accepted that a contract for the sale, for instance, of land, which contains no more than a bare "subject to finance" clause, imposes on the purchaser an implied obligation to exercise good faith in the attempt to obtain finance for the purchase.

Tender Evaluation Contracts

Once Finn J, in *Hughes Aircraft Systems v AirServices Australia* in 1997, implied into the process for tender evaluation for Government procurements a contract between the Government body and each respective tenderer, his Honour had to give that contract

some content beyond the bare words of the Request for Tender. As a result of that decision, any Government body which engages in procurement by calling for tenders – unless it has expressly excluded its liability – is under an implied obligation to treat each of the tenderers fairly and equally, and in good faith. And, although that decision is "merely" that of a single Judge of the Federal Court, it is unthinkable that the concept of a pre-award contract, with its concomitant implied obligation of good faith – a concept which has been accepted in the United States, by the Supreme Court of Canada, the New Zealand Court of Appeal and the English Court of Appeal – would be rejected if the issue were ever to come before a higher court.

Show cause procedures

It is, I suggest, now well accepted that, in the exercise of a show cause procedure, the Principal, who has called on the Contractor to show cause why the contract should not be terminated, must exercise those powers in good faith. Even though the relevant contractual tem is silent as to the need to act in good faith, that obligation will be implied. That, after all, is the principle to be derived from the decision of the NSW Court of Appeal in *Renard Constructions v Minister of Public Works* in 1992, a principle which at least a majority of that Court felt bound to follow in the subsequent case of *Hughes Bros v Roman Catholic Archbishop of Sydney*. And, although that principle may not have been expressly approved by the High Court, views along the same lines were expressed by Davies and Sheppard JJ – admittedly in the context of assessing damages – in *Amann Aviation v Commonwealth* (1990) 22 FCR 527, which found support (at least by Mason CJ and Dawson J) in the subsequent appeal to the High Court (1991) 174 CLR 64.

Franchise agreements

My final example of the judicial implication of an obligation to perform a contract in good faith comes from franchising agreements. Although section 51AC of the *Trade Practices Act* will go a long way to providing a statutory basis for imposing such an obligation on a franchisor, the position appears to have been reached, at least among Judges of the Supreme Court of Victoria, that

> a term that each party to a franchise agreement should exercise the powers conferred upon it in good faith and reasonably is one that is to be implied as a legal incident of a franchise agreement.

See *Bamco Villa P/L v Montedeen P/L* [2000] VSC 192 at para [166-9] per Mandie J, citing (inter alia) *Far Horizons P/L v McDonald's Australia* [2000] VSC 310 at para [42] and *Garry Rogers Motors v Subaru Aust* (1999) ATPR ¶41-703 at [37] per Finkelstein J (Fed Ct).

Good faith and the parties expectations

I further suggest that not only are courts prepared to imply obligations of good faith into at least some types of contracts, but that the parties to at least some kinds of contract are themselves prepared to operate on the basis of there being an underlying notion of good faith informing their obligations.

(a) ANU Standard terms of employment

In the inaugural lecture in this Series, that by John McMillan a fortnight ago, he referred in passing to the terms of his appointment to his current position. Although he did not quote from them verbatim, I have since obtained a copy. Clause 3.1 reads, in part:

> You are eligible to retire at age 55. The University will initiate discussions with you around the time of your fifty-fifth birthday with a view to establishing a mutually agreed retirement date.

I am not aware that this clause has been considered by any court yet. It is a relatively recent addition to the standard terms of appointment, and the evident purpose is to put some temporal limit on an employee's tenure, without contravening the terms of the age discrimination legislation. If the clause were challenged, it may turn out to nothing more than an "agreement to agree", and consequently unenforceable – a result which could cause havoc to the University's Budget in years to come, as more and more septuagenarians and octogenarians continue to draw their full University salary.

However, I have little doubt that the intention of the University – and, for those staff members who bother to read it, the intention of the staff member – is that, at or around

the staff member's 55th birthday, the parties will negotiate, with a view to fixing a retirement date. And, since the clause is (I think) no more than an agreement to negotiate, I have no doubt that the expectation of both parties is that those negotiations will be conducted in good faith.

(b) Informal contracting in the construction industry

I referred earlier to the fact that many contracts in the construction industry are entered into, and carried out, with a very considerable lack of formality. I earlier used that as an example of the virtual irrelevance of contract law, and as demonstrating that many contracting parties feel free to ignore "the law", and use their own (possibly different) sanctions to ensure satisfaction.

There may be another explanation for this lack of formality. No doubt at least some of the people involved in the construction industry are aware of the law of contract. But it is more than likely that their view of those few default rules which make up the common law's contribution to commercial regulation is that, if anything goes wrong in carrying out a particular job, a result will be arrived at based on good faith and fair dealing. In other words, a group of people whose commercial dealings are based very largely on trust must necessarily expect that they will deal with others, and will be dealt with by others, on a footing of good faith.

Globalisation

My final comment on the implication of obligations of good faith into commercial contracts relates to Australia's place in the wider world.

There is general acceptance, in that wider world, of a concept of good faith in the performance of contracts.

- The German Civil Code incorporated such a principle, in Art 242, in 1900
- A number of other countries in Continental Europe also incorporate notions of good faith in performance into their civil codes

- The United States Uniform Commercial Code, Art 1-201, requires the parties to contracts covered by that Code to exercise good faith in the performance of their obligations

- The *Restatement (Second) Contracts* §205 provides that "Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement"

- The United Nations Convention on Contracts for the International Sale of Goods (the Vienna Convention) – given the force of law in Australia by the Sale of Goods legislation in each State and Territory – in Art 7(1), provides that "In the interpretation of this Convention, regard is to be had to the need to promote … the observance of good faith in international trade."

- The UNIDROIT Principles of International Commercial Contracts, in Art 1.7, states "Each party must act in accordance with good faith and fair dealing in international trade"

- The growing convergence between English law and that of Continental Europe is putting pressure on that country to accept a notion of good faith in performance.

Despite our physical isolation – captured in a colourful phrase by a former Prime Minister – we are, in terms of trade and commerce, part of that wider world. To what extent, I ask in conclusion, can we here in Australia afford to remain immune from this movement towards the imposition of standards of good faith in the performance of our commercial contracts?