Final author version of chapter contributed to L.A.DiMatteo and Chen Lei (eds.), *Chinese Contract Law: Civil and Common Law Perspectives* (Cambridge University Press, 2017)

The General Principles of the Chinese Contract Law from the Perspective of an (English) Common Lawyer

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Introduction

This chapter will contrast the statement of general principles found in Arts.1-7 of the Chinese Contract Law ("CCL") with the approach to general principles of contract law in the (English) common law. The particular purpose of this paper will be on how these two contract law regimes regard contractual freedom and the extent to which there are limitations to this. It will begin with a short summary account of the CCL's general principles. The bulk of this paper will then set out the English common law's approach to general principles, the notion of "freedom of contract", and the extent to which restrictions to this notion are imposed by the common law. It must be stressed from the outset that this paper is concerned with English variant of the common law[1] and how this contrasts with the CCL. There are, of course, different versions of the common law, and whilst these have common origins, significant variations have developed over time. Secondly, as will be explained, this paper is only concerned with the common law of contracts, and will not consider the way English law now regulates specific types of contracts, such as consumer contracts.[2]

General Principles in the Chinese Contract Law (CCL)

Before turning to the common law position with regard to freedom of contract and its limitations, it will be helpful to summarise the main general principles in the CCL. The CCL is a codification of the law of contract, and its opening sections sets out a number of general objectives and key principles. The CCL has three key objective set out in Article 1 CCL: (i) to protect the lawful rights and interest of the contracting parties; (ii) to maintain social and economic order; and (iii) to promote socialist modernisation. The principles set out in subsequent articles would appear to have two functions: (i) to guide the interpretation of specific substantive provisions of the CCL, and (ii) to be used as a basis on

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[1] For a good introduction to the English law of contract, see John Cartwright, *Contract Law – An introduction to the English law of contract for the civil lawyer*, 3rd edition (Bloomsbury, 2016), chs.1-3.
A very useful and concise overview of the current shape of English contract law, including relevant statutory rules, can be found in Andrew Burrows, *A Restatement of the English Law of Contract* (Oxford University Press, 2016) (hereiafter "Burrows, *Restatement*").

[2] See, in particular, the provisions of the Consumer Rights Act 2015 and the Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013 S.I. 2013/3134

which gaps in the CCL could be bridged when adjudicating on a particular matter.[3] However, it seems that where a specific rule is available to dispose of a particular matter, it is not permissible to rely on any of the general principles instead.

The first general principle underpinning any kind of contractual agreement is that of "equality", i.e., the parties are equal (Art.2 CCL), combined with the added obligation that no party may impose its will upon the other party (Art.3 CCL). This suggests that no coercion in the process of contract formation or contract performance is permissible. However, this general assumption leaves unclear as to what should happen if there are clear instances of an inequality in the position of the parties.

The second principle is that of "voluntariness", or party autonomy,[4] found in Art.4 CCL, according to which parties have "the right to voluntarily conclude contracts". Added to this is that "no unit or individually may illegally intervene therein", which of course leaves open the possibility for restrictions imposed by law on the exercise of the right to conclude a contract. It seems that the principle of "voluntariness" should not be equated too readily with the notion of freedom *of* contract which is the hallmark of the common law of contract (and, indeed, of all Western legal systems);[5] rather, it might better be understood as freedom *to* contract. This is more than just semantics – as the discussion of the common law approach will show, freedom of contract is about much more than just enabling parties to enter into legally binding agreements.

The behaviour of the parties to a contract is then regulated by the third and fourth general principles: first, in determining their respective rights and duties, the parties must observe the "principle of fairness" (Art.5 CCL); secondly, in exercising their rights and performing their duties, parties must observe the principle of "good faith" (Art.6 CCL). For neither principle, factors relevant to their application have been fleshed-out in the text of the CCL itself, leaving it for the courts to specify the factors which will be relevant in establishing whether both parties have complied with these key principles. There are further provisions in the CCL particularly on good faith: Art.42 CCL holds a party liable for (i) negotiating in bad faith; (ii) intentionally concealing a fact or providing wrong information; and (iii) any other instance which violates the principle of good faith. This suggests that two of the key aspects of "good faith" are honesty and transparency. Moreover, Art.60 requires that the parties must observe the principle of good faith in performing their obligations.

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[3] Cf. the discussion by Shiyuan Han, "General Principles under the CCL: System Structure, Norm Functions and Developments in Practice", in this volume.

[4] Zhang Yuqing and Huang Danhan, "The New Contract Law in the People's Republic of China and the UNIDROIT Principles of International Commercial Contracts: A Brief Comparison" [2000] *Uniform Law Review* 429-440, p.431.

[5] See Junwei Fu, *Modern European and Chinese Contract Law: A Comparative Study of Party Autonomy* (Alphen aan de Rhijn: Kluwer Law International, 2011); also Junwei Fu, "Towards a Social Value Convergence: a Comparative Study of Fundamental Principles of Contract Law in the EU and China" (2009) Oxford U Comparative L Forum 5.

The fifth general principle could be summarised as the "compliance with public interest". Thus, Art.7 specifies that parties must act in accordance with relevant laws when concluding and performing a contract, respect public morals, and not disturb the social and economic order nor harm the public interest. What seems like a reasonable obligation imposed on the parties could potentially form the basis for far-reaching control over the contracting process from negotiation to content to performance.

The task for this paper is now to contrast this position with the common law approach. There will first be a consideration of how the common law deals with general principles, before examining the scope of "freedom of contract" and its limitations. It will become apparent that the common law takes a generous attitude towards the freedom of the parties to enter into contracts and to determine the scope of their bargain, with limited intervention by the law to set boundaries to what the parties can and cannot do.

General Principles in the English Common Law of Contract

The approach of the English common law of contract to general principles, particularly freedom of contract, will be analysed in this part, starting with an overview of the general principles which are said to underpin the law, before focusing on freedom of contract and its limitations in particular. This discussion will, where appropriate, contrast the common law approach with that in the CCL. Inevitably, in a paper of this length, it will only be possible to provide a sketch of the common law's approach, highlighting its main features. This brings with it the obvious risk of skimming over the richness of the case-law.[6]

When it comes to the common law of contract, several key features spring to mind as its particular hallmarks: first, as already mentioned, freedom of contract, i.e., the right of the parties to enter into contracts with whomever, for whatever and one whichever terms they wish, is regarded as paramount. As will be discussed more fully later, this means that there will be few instances when the law will interfere in the bargain reached between the parties. Secondly, alongside freedom of contract, certainty and the sanctity of the contract are regarded as equally important – *pacta sunt servanda*. This means that parties to a contract can be confident that their bargain will be upheld, but also that the law will hold the parties to their bargain – even where this might produce unexpected outcomes for them.

The hands-off (*laissez-faire*) attitude of the common law is further reflected in emphasising the adversarial position of the parties, which allows parties to act in a primarily self-interested fashion without being under any legal obligation to act co-operatively, transparently nor fairly.

[6] Many of the case discussed in this paper are relatively recent decisions by the English Supreme Court, not least because they offer a helpful and current statement of the present position.

Before continuing, one important *caveat* must be made: this characterisation of the common law provides only a partial view of the modern English law of contract. The high value attached to contractual freedom and certainty continues to be evident in the case-law, not least in several recent rulings by the Supreme Court, but at same time, there is a recognition by the courts that a more tempered approach is occasionally appropriate, especially in circumstances where one party might be in a less-strong bargaining position than the other. However, instances where this happens are offset by other cases where the courts have adhered to the orthodox approach of the common law and have not interfered in bargains which have turned out to produce bad outcomes.[7] Moreover, the common law has been affected by legislation aimed at protecting the interest of parties generally regarded as significantly weaker, particularly in the context of contracts of employment and perhaps even more so with regard to consumer contracts.[8] In those contexts, the degree of legislative intervention is now such that the freedom of the parties to determine the content of their contract is significantly restricted. So whilst the common law of contract continues to provide the background law for those heavily regulated types of contract, legislation has largely superseded many common law doctrines. It is therefore perhaps more accurate to say that the common law of contract primarily focuses on contracts concluded between commercial parties (although some of the doctrines, such as undue influence, which permit the courts to interfere in a contract are of greater assistance to private individuals). Thus, Hugh Beale has observed that "[t]o put it simply, English contract law is not for everyone: not for all courts, not for all parties. It is in effect designed for big business".[9] For such contracts, the non-interventionist approach with its focus on freedom of contract and certainty will be most appropriate. However, it also means that taking a common law perspective on the CCL will mean that this perspective will be shaped by this focus on business contracts, which tends to be less concerned with circumstances where there is a degree of inequality between the parties because this is usually dealt with through legislative intervention. Indeed, one of the few instances where there is some control over the substance of the bargain concluded between *commercial* parties is based on legislation: the Unfair Contract Terms Act 1977. Interestingly, its subsequent application by the courts suggests that it will rarely be deployed by the courts to interfere in a contract made between parties of comparable bargaining strength. Thus, whilst provides a basis for challenging terms which exclude or limit liability for breach of contract where this would fail to meet

[7] See e.g, *Arnold v Brittan* [2015] UKSC 15, discussed below.

[8] In the United Kingdom, the Consumer Rights Act 2015 and related legislation such as the Consumer Protection from Unfair Trading Regulations 2008, as amended, now regulate many aspects of contracts concluded between a trader/business and consumers. The degree of legislative intervention has reached a stage where some scholars have argued that consumer contract law should be regarded as a form of regulation and not be treated as a branch of contract law at all because of its very different rationales: see Roger Brownsword, "Regulating Transactions: Good Faith and Fair Dealing" in G.Howells and R.Schulze (eds.), *Modernising and Harmonizing Consumer Contract Law* (Munich: Sellier, 2009); and, by the same author, "Contract, Consent and Civil Society: Private Governance and Public Imposition" in P.Odell and C.Willett, *Global Governance and the Quest for Justice – Civil Society* (Oxford: Hart, 2008).

[9] Cf. Hugh Beale, "The Impact of the Decisions of the European Courts on English Contract Law: The Limits of Voluntary Harmonization" (2010) 18 *European Review of Private Law* 501- 526 at 526.

the requirement that the term was a "fair and reasonable one to have been included in the contract",[10] the courts generally tend to regard such terms as reasonable when a commercial contract has been concluded between parties of equal bargaining power able to determine how to allocate risks between each other and to seek insurance protection in case such risks materialise.[11] In *The Salvage Association v CAP Financial Services Ltd*.,[12] Forbes J noted that "[g]enerally speaking, where a party well able to look after itself enters into a commercial contract and, with full knowledge of all relevant circumstances, willingly accepts the terms of the contract which provides for apportionment of the financial risks of that transaction, I think that it is very likely that those terms will be held to be fair and reasonable".[13]

(i) General attitude to general principles

Although freedom of contract and certainty are the key guiding principles for the English common law of contract, an attempt to find other, more substantive principles, will only have limited success. Most obviously, English contract law has rejected any legal duty on the parties to a contract to act in good faith, although very recent cases suggest a subtle shift in that regard (discussed below). Beyond this, English courts have resisted the recognition that there are any other general principles operating within the law of contract which could be used to develop the law and fashion new rules to fill perceived gaps in the law. At best, one might be able to trace themes which offer additional guidance to judges in applying the law to difficult circumstances. Thus, Steyn LJ (as he then was) once famously observed the following:

> "A theme that runs through our law of contract is that the reasonable expectations of honest men must be protected. It is not a rule or a principle of law. It is the objective which has been and still is the principal moulding force of our law of contract. It affords no licence to a judge to depart from binding precedent. On the other hand, if the *prima facie* solution to a problem runs counter to the reasonable expectations of honest men, this criterion sometimes requires a rigorous re-examination of the problem to ascertain whether the law does indeed compel demonstrable unfairness."[14]

Steyn LJ emphasises that the protection of the "reasonable expectations" of honest men is no more than a theme or an objective pursued by the law of contract, but not a principle which would permit a judge

[10] Section 11(1) UCTA.
[11] See e.g., the view expressed by Lords Diplock and Wilberforce in *Photo Production Ltd v Securicor Ltd* [1980] AC 827
[12] [1995] FSR 654.
[13] See also e.g., *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361, where a clause excluding liability for loss of business, profits, anticipated savings, data, third-party claims or consequential loss was found to be reasonable *int. al.* because both parties were experience businessmen and were of equal bargaining strength.
[14] *First Energy (UK) Ltd v Hungarian International Bank Ltd* [1993] BCLC 1409 at 1410.

to depart from the rules of contract law established through the doctrine of precedent.[15] Writing extra-judicially,[16] Lord Steyn stressed that this notion is not a rule of law, and whilst it might be arguable that it is a general principle, he preferred to treat is as a "central objective of the law of contract".[17] He also conceded that there will be instances where countervailing principles and policies might prevail over the parties' reasonable expectations, which means that these would not act as an over-riding criterion in deciding the outcome of a specific case.[18] In subsequent rulings, courts have referred to this notion but have not treated it as a general principle. For example, in *Reveille Independent LLC v Anotech International (UK) Ltd*,[19] Cranston J treated it as a policy:

> "These rules [on contract formation] take effect against the background of legal policies recognised in the case law. One such policy is the need for certainty in commercial contracts, a policy which since Lord Mansfield's time has run as a thread through the jurisprudence… A second policy is that in commercial dealings the reasonable expectations of honest, sensible business persons must be protected…."[20]

This means that "protecting the reasonable expectations of honest business persons" cannot be deployed as a freestanding argument in the context of a legal dispute, but it becomes a guiding principle, or policy, which courts utilise when applying inherently flexible rules of law. Thus, as the Supreme Court's ruling in *RTS Flexible Systems Ltd v Molkerei Alois Müller GmbH & Co KG (UK Production)*[21] confirmed, it is relevant in applying the objective determination of whether a binding contract had come into existence (e.g., in the absence of a written contract when a court has to consider whether the communications between the parties and their conduct has resulted in a binding agreement with the intention to create legal relations). There are good reasons for such an objective: the rules of contract law are at risk of being out-of-step with commercial practice, but if courts are mindful of the fact that they should aim insofar as possible to uphold the parties' reasonable expectations, then this minimises the number of instances where the law seriously collides with commercial practice.[22]

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[15] For an excellent discussion, see Catherine Mitchell, "Leading a Life of its Own? The Roles of Reasonable Expectation in Contract Law" (2003) 23 *Oxford Journal of Legal Studies* 639-665.
[16] Johan Steyn, "Contract Law: Fulfilling the Reasonable Expectations of Honest Men" (1997) 113 *Law Quarterly Review* 433 – 442.
[17] *Ibid*, at 434.
[18] For a well-known example of this, see *Baird Textile Holdings Ltd v Marks and Spencer plc* [2001] EWCA 274.
[19] [2016] EWCA Civ 443.
[20] Ibid, para [42].
[21] [2010] UKSC 14, confirming Steyn LJ's approach in *Trentham (G Percy) Ltd v Archital Luxfer Ltd* [1993] 1 Lloyd's Rep 25 at p.27: "The first is the fact that English law generally adopts an objective theory of contract formation. That means that in practice our law generally ignores the subjective expectations and the unexpressed reservations of the parties. Instead the governing criterion is the reasonable expectations of honest men. And in the present case that means that the yardstick is the reasonable expectations of sensible businessmen."
[22] Cf. Robert Bradgate, "Contracts, Contract Law and Reasonable Expectations" in Sarah Worthington (ed.), *Commercial Law & Commercial Practice* (Hart Publishing, 2003).

Aside from freedom of contract, certainty, and perhaps the desire to facilitate commercial dealings,[23] the common law therefore does not draw on general principles – neither as a normative basis on which detailed legal rules are based nor as background principles to fill gaps in the legal rules which have been recognised by the common law. Instead, contracting parties are guided through the process of negotiating, concluding and performing a contract through discrete and quite narrowly defined doctrines which can be deployed to deal with particular circumstances when it is regarded as necessary that the law should step in and provide relief to one, or both, of the parties, irrespective of what they objectively agreed. Although it is arguable that these doctrines rely on a common basis,[24] the English courts have declined to use this as a reason for recognising broader general principles. The effect of this is that where doctrines exist to, they will only provide relief within their particular narrow confines. For example, the doctrine of proprietary estoppel is available in some circumstances to recognise a proprietary interest in land or chattels even though a contract to transfer a legal interest has not been concluded. In *Yeoman's Row Management Ltd v Cobbe*,[25] the House of Lords considered the elements that needed to be satisfied for a proprietary estoppel to operate and repeatedly emphasised that estoppel would only arise on these defined criteria: "it is not a sort of joker or wildcard to be used whenever the Court disapproves of the conduct of a litigant who seems to have the law on his side".[26] Crucially, it is not a broad weapon against unconscionable behaviour by a defendant. So even where the law does step in, it will do so reluctantly and on narrow grounds.

(ii) The scope of "freedom of contract"

The English common law of contract is often portrayed as being primarily concerned with facilitating the bargains made by the parties without too much interference in the process of concluding and performing a contract.

In a recent Privy Council decision,[27] Lord Toulson summarised the position of the English Common law as follows:

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[23] See e.g., Goff: "Commercial Contracts and the Commercial Court" [1984] *LMCLQ* 382 and Irvine of Lairg, "The Law: An Engine for Trade" (2001) 64 *Modern Law Review* 333; also Lord Hoffmann's observations in *Re BCCI (No.8)* [1997] 4 All ER 568 at 578 that "in a case in which there is no threat to the consistency of the law or objection of public policy, the courts should be very slow to declare a practice of the commercial community to be conceptually impossible. ... Rules of law must obviously be consistent and not self-contradictory ... But the law is fashioned to suit the practicalities of life…"

[24] Cf. Lord Denning in *Lloyd's Bank Ltd v Bundy* [1975] Q.B. 326.

[25] *Yeoman's Row Management Ltd* v *Cobbe* [2008] UKHL 55, [2008] 1 WLR 1752.

[26] Ibid. para [46].

[27] *Prime Sight Limited (A company Registered in Gibraltar) (Appellant) v Edgar Charles Lavarello (Official Trustee of Benjamin Marrache a Bankrupt) (Respondent)* [2013] UKPC 22.

> "Parties are ordinarily free to contract on whatever terms they choose and the court's role is to enforce them. There are exceptions and qualifications, but these too are part of the general law of contract. In *Greer v Kettle* Lord Maugham referred to fraud, illegality, mistake and misrepresentation. Similarly, […] a court may refuse in some circumstances to enforce a contract on grounds of public policy (a topic closely related to illegality) […]"[28]

This reflects the importance attached by the law to the idea of "freedom of contract", and to the freedom to contract on "whatever terms", one might also add the general freedom to contract with, or not to contract with, whomever one chooses. It needs to be emphasised that this is the general view, and, as will be explained below, there are a number of instances (some of which alluded to in the extract above) when this generous freedom is curtailed in some way. But these are small in number and applied very restrictively and predominantly in circumstances where the freedom of one party to enter into a contract had been impeded in some way.

A corollary of this generous attitude towards freedom of contract is that the parties to a contract generally also have to accept the consequences of the bargain they have made, and that the law will not step in to alleviate the consequences of a harsh bargain. For example, in *Arnold v Britton*, a recent Supreme Court ruling,[29] a clause provided for annual increases to the service charge payable in long-term leases of static caravans. The basic charge was £90, with an annual increase of 10%. The contracts had been concluded in the 1970s and were for a 99-year period. The effect of this term was that, after several decades, the annual service charge would increase to tens and hundreds of thousands of pounds. The tenants argued that a literal interpretation of this clause would produce an absurdly unfair outcome, and contended for a modified interpretation of the clause, but the Supreme Court rejected this and upheld the clause in its literal meaning. The Supreme Court stressed that, when interpreting a provision in a contract, the language used in the contract is more important that notions of "commercial common sense". Thus, Lord Neuberger noted that

> "…the mere fact that a contractual arrangement, if interpreted according to its natural language, has worked out badly, or even disastrously, for one of the parties is not a reason for departing from the natural language"[30]

and further

[28] *Ibid*, para [47].
[29] [2015] UKSC 15.
[30] *Ibid*., para 19.

> "while commercial common sense is a very important factor to take into account when interpreting a contract, a court should be very slow to reject the natural meaning of a provision as correct simply because it appears to be a very imprudent term for one of the parties to have agreed, even ignoring the benefit of wisdom of hindsight…Experience shows that it is by no means unknown for people to enter into agreements which are ill-advised…and it is not the function of a court when interpreting an agreement to relieve a party from the consequences of his imprudence or poor advice."[31]

These observations, made in the context of interpreting the written contract between the parties, emphasise the paramountcy accorded to the agreement reached freely between the parties. It is clear that, absent any vitiating factor (see below), the parties will have to accept the consequences of the contract they have concluded, no matter how disadvantageous that might be for one of the parties. So in the context of the English common law of contract, freedom of contract also comes with an obligation to pay close attention to what is being agreed, as relief is unlikely to be granted by a court if the outcome of the contract turns out to be "disastrous".[32]

(iii) Limitations to "freedom of contract"

Although freedom of contract has a very broad scope in the English common law of contract, there are a number of instances when this very broad freedom is restricted. These include:[33]

1. The so-called "vitiating factors" of fraud, misrepresentation, undue influence or duress (where one party's ability to exercise their freedom is impaired in some way by the actions of the other party), as well as mistake.
2. Controls over the substance of the contract through the implications of some terms as a matter of *law*, the rules on penalties and forfeiture
3. Instances of conduct which is illegal or contrary to public policy
4. Various statutory controls, including those over certain exclusion and limitation clauses (and unfair terms in a consumer contract) as well as legislation which precludes the parties from derogating from the rules in such legislation
5. Refusal to concluded a contract for reasons which are prohibited under the Equality Act 2010

[31] *Ibid*., para [20].
[32] Lord Carnwath dissented, arguing that the clause itself had not been drafted clearly ("It is clear to my mind that something has gone wrong with the drafting…" [para 125]). He concluded that "I regard the consequences…as so commercially improbable that only the clearest words would justify the court in adopting it".
[33] Burrows, *Restatement*, s.5.

(iii)(a) Vitiating Factors

The first category of limitations to the broad notion of freedom of contract are the so-called vitiating factors, which are a number of doctrines developed to deal with specific instances where the ability of one party freely to conclude a contract was in some way impaired by the actions of the other party.

Misrepresentation

As already noted, one aspect of the generous freedom of contract approach of the English common law is that there is no duty to provide information, and each party needs to make their own necessary enquiries as to any information they regard as relevant – in essence, *caveat emptor* applies.[34] However, insofar as one party does provide information to the other party, English law requires that any such information is correct, otherwise it will be regarded as a misrepresentation. If a contract was concluded after a misrepresentation had been made by one party, the contract is voidable and may be rescinded, and damages may be claimed.[35] There are several requirements for a party seeking to establish that there was a misrepresentation: first, one party must have provided some information to the other party, and this must have been a statement of *fact* rather than simply an opinion.[36] Also, the statement must relate to *present* facts, although this can include a stating the intention to do something in the future without actually having that intention when making the statement.[37]

Secondly, the information given must be untrue. This includes making a statement which is deliberately ambiguous, if the intention is that the recipient of the information would assume a meaning which is not correct.[38] Although silence does not of itself constitute a misrepresentation, the conduct of the parties can be regarded as a misrepresentation: in *Spice Girls Ltd v Aprilia World Service BV*,[39] it was held that there had been a representation that all five members of a music-group would be available for an advertising campaign when the group already knew that one of them had decided to leave the group. Although nothing had been said, the statement of fact was inferred from the conduct of one of the parties. Similarly, a deliberate attempt to conceal information can be a misrepresentation,[40] as can partial non-disclosure.[41] Also, a statement which is literally true but still misleading because not all the relevant

[34] *Keates v Cadogan* (1851) 10 CB 591, CCP; *Bradford Third Equitable Benefit Building Society v Borders* [1941] 2 All ER 205, HL.
[35] The latter are largely governed by the Misrepresentation Act 1967.
[36] eg *Esso Petroleum Co Ltd v Mardon* [1976] QB 801, CA. The dividing line between a statement of fact and one of opinion is not always easy to make out, as sometimes an opinion could imply an underlying state of fact.
[37] *Edgington v Fitzmaurice* [1885] 29 ChD 459, CA.
[38] Cf. *Sykes v Taylor-Rose* [2004] EWCA Civ 299, [2004] All ER (D) 468. A standard questionnaire sent to the vendor of a house asked, *int. al.*, whether there was any other information which, in the vendor's view, the purchaser might have a right to know. This was answered honestly with a "no", despite the fact that the vendor was aware that a murder had been committed in the house and body-parts might still be hidden there.
[39] *Spice Girls Ltd v Aprilia World Service BV* [2002] EMLR 27, CA.
[40] *Schneider v Heath* (1813) 3 Camp 506, CCP.
[41] *Peek v Gurney* [1871–73] All ER Rep 116, HL.

information has been given can be a misrepresentation, [42] as can a statement which was true when given but becomes untrue before a contract is concluded.[43]

A third requirement is that the misrepresentation must be *material*, i.e, it must have an effect on the decision to conclude the contract on the particular terms offered.[44] Finally, the recipient of the statement must have relied on it in deciding to enter into the contract. Actual reliance needs to be proven,[45] although reliance is presumed if a reasonable person would have relied on the incorrect information.[46] Materiality and reliance are separate requirements and both need to be shown by the claimant.[47] It is apparent that misrepresentation will therefore only assist a party under strict conditions, and the general position that each party is responsible for protecting its interests is not significantly altered by this doctrine.

Duress

The principle of freedom of contract entails that both parties are able to exercise that freedom without constraint, i.e., a contract should not be the result of one party effectively having pressured the other into concluding a contract. The common law had long accepted that making physical threats would constitute duress and the innocent party would be entitled to have a contract set aside.[48] However, the common law has gone further and developed a distinct doctrine of economic duress.[49] As Lord Goff states, "economic pressure may be sufficient to amount to duress...provided at least that the economic pressure may be characterised as illegitimate and has constituted a significant cause inducing the [claimant] to enter into the relevant contract."[50] Generally speaking, a contract can be avoided by the innocent party by showing that there was illegitimate pressure (e.g., to break a contract), exercised in bad faith, which left the victim with no realistic practical alternative but to submit to the pressure.[51] If this can be established, the contract is voidable, i.e., the innocent party can set the contract aside. This requires an active step and must be done swiftly; otherwise, the innocent party will be deemed to have affirmed the contract through having waived its right to avoid the contract.

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[42] *Notts Patent Brick and Tile Co v Butler* (1866) 16 QBD 778, QBD.
[43] *With v O'Flanagan* [1936] Ch 575, CA. See R Bigwood, 'Pre-contractual misrepresentation and the limits of the principle in *With v O'Flanagan*' (2005) 64 Cambridge Law Journal 94.
[44] For a recent exploration of this requirement in the context of fraudulent misrepresentation (the tort of deceit), see *Hayward v Zurich Insurance Company plc* [2016] UKSC 48, where the Supreme Court held that an insurance company which had doubts about the extent of a claimant's injuries was not precluded from applying to have a settlement agreement set aside once sufficient evidence about the untruth of the claimant's statement was available.
[45] *Museprime Properties Ltd v Adhill Properties Ltd* [1990] 2 EGLR 196, Ch.
[46] *Smith v Chadwick* (1884) 9 App Cas 187, HL.
[47] *Pan Atlantic Insurance Ltd v Pine Top Insurance Ltd* [1995] 2 AC 501, HL.
[48] Cf, *Barton v Armstrong* [1976] A.C. 104 (PC).
[49] *North Ocean Shipping Company v Hyundai Construction, The Atlantic Baron* [1979] Q.B. 705.
[50] Lord Goff in *The Evia Luck (No.2)* [1992] 2 A.C. 152.
[51] Cf Dyson J in *DSND Subsea Ltd v Petroleum Geo-Services ASA* [2000] B.L.R. 530.

In comparison, Art.52 (1) CCL states that a contract is void where "a party uses fraud or duress to conclude the contract, thereby harming the interests of the state". If a contract is void, it has no binding force *ab initio* (Art.56 CCL). However, Art.54 CCL also provides that where contracts are concluded as a result of duress, the innocent party can apply to a court or arbitral institution to have the contract rescinded or modified. The relationship between these two provisions is not clear – in particular, whether Art.54 operates as an alternative to the effect of Art.52 where a contract was the result of duress.

Undue Influence

In order to supplement the strictness of the doctrine of duress developed at common law, the courts of equity developed the supplementary doctrine of undue influence. As with duress, it is concerned with the way a person was persuaded to enter into a contract by the other party in circumstances when it can be said that that person no longer exercised his or her free will.[52] As Lord Nicholls explained in the leading English authority on this:

> "[It] arises out of a relationship between two persons where one has acquired over another a measure of influence, or ascendancy, of which the ascendant person then takes unfair advantage. … In cases of this latter nature the influence one person has over another provides scope for misuse without any specific overt acts of persuasion. The relationship between two individuals may be such that, without more, one of them is disposed to agree a course of action proposed by the other. Typically this occurs when one person places trust in another to look after his affairs and interests, and the latter betrays this trust by preferring his own interests. He abuses the influence he has acquired."[53]

Although it may be possible to establish undue influence on the facts of a given case, it many instances, it is possible to rely on the so-called rebuttable presumption of undue influence. This presumption can be established by showing that there is a relationship of trust and confidence between the parties, with one party having reposed their trust in the other, and that the subsequent transaction is one which is not readily explicable by the relationship between the parties or otherwise calls for an explanation. Certain categories of relationship are irrebuttably presumed to be relationships of trust and confidence,[54] whereas it is necessary for claimant in other relationships to show on the facts that trust and confidence was reposed in the defendant going beyond what is usual in relationships of this kind.[55] Where such a

[52] *Royal Bank of Scotland v Etridge (No.2)* [2001] UKHL 44, para [7].
[53] *Ibid.*, paras [8]-[9].
[54] These are: parent and child; trustee and beneficiary; solicitor and client; doctor and patient; religious adviser and disciple; and guardian and ward.
[55] Cf. *O'Sullivan v Management Agency & Music Ltd* [1985] Q.B. 428; *Credit Lyonnais Nederland NV v Burch* [1997] 1 All ER 144; *Macklin v Dowsett* [2004] EWCA Civ 904 and *Crossfield v Jackson* [2014] EWCA Civ 1548.

relationship exists, and "given the circumstances and nature of the transaction, it says to the unbiased observer that absent explanation it must represent the beneficiary taking advantage of his position",[56] then the transaction can be set aside for undue influence unless the defendant can show that the claimant did not enter into the transaction as a result of undue influence. It can be seen that this doctrine, in a similar way as the doctrines of misrepresentation and duress, is primarily concerned with protection the exercise of free will – so if the circumstances of a particular case are such that a transaction clearly disadvantageous to one person was entered into freely and with full awareness of its implications, then that person cannot rely on the doctrine to have the contract set aside.[57]

(iii)(b) Common law controls over substance

Although freedom of contract generally entails that the parties will be held to the terms of their contract without interference by the courts, there are some instances where there are common law controls over the substance of the contract. The two main instances are where terms are implied into a contract as well as the common law controls over so-called "penalty clauses" and terms which grant one contracting party a significant amount of discretion with regard to the performance of the contract.

Implication of Terms

Generally speaking, there are two instances when the contract concluded by the parties can be supplemented through the implication of terms: the first is where terms are implied *in law* due to the nature of the transaction, whereas the second is the implications of terms "*in fact*" when this is necessary to clarify an omission from the terms of the contract.

Terms are implied into a contract in law when the contract is of a particular type. For example, in an arbitration agreement, there will be a term implied in law that the parties are subject to a duty of confidentiality as a result of the nature of this agreement, without there being any need for the parties expressly to include a term to that effect.[58] Sometimes, terms are also implied in law under specific statutes. The Sale of Goods Act 1979 implies a number of terms into any (non-consumer) contract of sale setting out the seller's obligations in respect of the goods provided under the contract (see ss.12-15 of the Act).

Terms are implied "in fact" to reflect what the parties had seemingly agreed but not made explicit in the terms of their contract. As such, it does not necessarily interfere directly with the parties' freedom

[56] *Turkey v Awadh* [2005] EWCA Civ 382, paras. [22]-[23].
[57] *Royal Bank of Scotland v Etridge (No.2)* [2001] UKHL 44; *Turkey v Awadh* [2005] EWCA Civ 382.
[58] *Ali Shipping Corporation v "Shipyard Tiger"* [1998] 1 Lloyds Rep 643; *John Foster Emmot v Michael Wilson & Partners Ltd* [2008] EWCA Civ 184

of contract, although the consequence of implying a term into a contract in this way might mean that the obligations of one or both parties are different from what they assumed when concluding the contract in question. The Supreme Court recently clarified the legal principles which will be applied when considering whether to imply a term into a contract,[59] following a degree of uncertainty created by a Privy Council ruling.[60] The position now is that, when construing a contract, a court may imply a term into that contract only where this is necessary for business efficacy and the term would be so obvious that it goes without saying. Beyond this, courts will not usually supplement the contract as agreed between the parties, which means that the parties will have to accept the consequences of applying the terms of the contract.

Controls over penalty clauses

Commercial contracts often include "liquidate damages clauses" providing for the payment of a fixed sum when there is a breach of the contract, e.g., failure to complete performance by a stipulated deadline. Such a clause brings with it the advantage of certainty, because both parties will know what has to be paid if one party has failed to comply with its obligations under the contract. On the other hand, the sum specified in the contract might be higher than the loss actually suffered. Somewhat unusually, the common law treats as void a term in a contract which it regards as a "penalty clause". For many years, the leading case on this issue was *Dunlop Pneumatic Tyre Co. v New Garage & Motor Co Ltd*.[61] In that case, a distinction was drawn between a liquidated damages clause, which is a genuine attempt to pre-estimate the loss likely to result from the breach (although it need not be the precise amount) and penalty clause, which requires "a payment of money stipulated as in terrorem of the offending party".[62] In order to consider whether a particular term should be considered as a penalty clause, Lord Dunedin set down a number of rules of construction:

> (1) "If the sum stipulated is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach", it is a penalty.
>
> (2) It will also be a penalty if the obligation is to pay a sum of money, and the sum specified in the clause is greater than the sum which ought to have been paid.
>
> (3) A clause may be presumed to be a penalty if the same sum is payable if one or more of several events occur, but the consequences of these differ in terms of their severity.

[59] *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Limited* [2015] UKSC 72.
[60] *A-G of Belize v Belize Telecom Ltd* [2009] UKPC 10; for a summary, see E.McKendrick, Contract Law, 11th ed., Palgrave 2015, pp.168-171.
[61] [1915] AC 79.
[62] *Ibid*, at p.86.

(4) Although the sum should be a genuine pre-estimate of the damage that the consequences of the breach are, it is not an obstacle to this requirement that precise pre-estimation is impossible.

In *McAlpine v Tilebox*,[63] Jackson J emphasised that "[b]ecause the rule about penalties is an anomaly within the law of contract, the courts are predisposed, where possible, to uphold contractual terms which fix the level of damages for breach. This predisposition is even stronger in the case of commercial contracts freely entered into between parties of comparable bargaining power."[64]

The legal principles applicable to penalty clauses were recently reconsidered by the Supreme Court.[65] In their joint speech, Lords Neuberger and Sumption made it clear that

> "The penalty rule is an interference with freedom of contract. It undermines the certainty which parties are entitled to expect of the law. …"[66]

There is therefore a clear recognition that this is one instance where the common law has developed a derogation from the general adherence to the notion of freedom of contract. However, the case-law leading up to this ruling had seemingly allowed the doctrine to operate in a somewhat unpredictable fashion, which made it more difficult for parties to a contract to identify which clauses would be upheld as reflecting the parties' freedom of contract, and which clauses would be struck down for being a penalty. Lords Neuberger and Sumption rephrased the key test thus:

> "The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation."[67]

So whilst the criteria set out by Lord Dunedin in *Dunlop Pneumatic Tyre Co* continue to be relevant in identifying whether a clause should be regarded as a penalty, it is only if the test above is satisfied that the clause will be struck down.

Controls over Contractual Discretion

Although English Law does not impose general standards of conduct on the parties during the performance of a contract, courts have been prepared to require a party who has a degree of discretion under a contract term to exercise that discretion properly. Thus, in *Abu Dhabi National Tanker Co. v Product Star Shipping, The Product Star*,[68] Leggatt LJ stated that :

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[63] [2005] EWHC 281 (TCC).
[64] *Ibid*, para [48].
[65] *Cavendish Square Holding BV (Appellant) v Talal El Makdessi (Respondent); ParkingEye Limited (Respondent) v Beavis (Appellant)* [2015] UKSC 67
[66] Para. [33].
[67] Para .[32].
[68] [1993] 1 Lloyd's Rep 397.

> "Where A and B contract with each other to confer a discretion on A, that does not render B subject to A's uninhibited whim. In my judgment, the authorities show that not only must the discretion be exercised honestly and in good faith, but, having regard to the provisions of the contract by which it is conferred, it must not be exercised arbitrarily, capriciously or unreasonably".[69] (p.404).

In *Gan Insurance v Tai Ping Insurance Co*,[70] in considering the factors which should be considered by a reinsurer when determining whether to grant approval, the Court of Appeal was prepared to imply a term into a contract requiring approval not to be withheld arbitrarily. Mance LJ observed that

> "The right to withhold approval … is a right to be exercised in good faith after consideration of and on the basis of the facts giving rise to the particular claim, and not with reference to considerations wholly extraneous to the subject-matter of the particular reinsurance or arbitrarily."[71]

In *Nash and Staunton v Paragon Finance plc*,[72] the term in issue was an interest variation clause in a mortgage contract. One of the questions that arose was whether there was any restriction on the lender's power to vary interest rates. The Court of Appeal held that such clauses were not completely unfettered, and that the parties are deemed reasonably to expect that the discretion would not be exercised dishonestly, for an improper purpose, capriciously, arbitrarily or in a way which no reasonable lender, acting reasonably, would do.[73] A term to that effect was therefore implied into the contract, because it would go "without saying".[74] On the facts, there was no breach of this implied term, because the decision to raise interest rates had been made purely for commercial considerations. Nevertheless, these cases illustrate that the courts will take a closer look at how terms granting one party a degree of discretion are utilised by the party to ensure that this discretion is exercised in accordance with the "reasonable expectations" of both parties.[75]

More recently, the Supreme Court has refined the approach a court should take in reviewing the way a party exercises the discretionary power given to it under the terms of the contract. In *Braganza v BP Shipping Limited and another*,[76] the justices were agreed on the principles to be applied (although the panel was divided as to how these should be applied to the case before it). Lady Hale gave the leading judgment. In addressing the general question of what is meant when one requires the exercise of contractual discretion to be reasonable, Lady Hale's starting point is that terms giving one party the

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[69] *Ibid*., p.404.
[70] [2001] EWCA Civ 1047.
[71] *Ibid*., para [76]
[72] [2001] EWCA Civ 1466.
[73] *Ibid*., para [41].
[74] *Ibid*., para [36].
[75] *Ibid.*
[76] [2015] UKSC 17

right to exercise discretion are common and freedom of contract requires a court to take a non-interventionist stance:

> "Contractual terms in which one party to a contract is given the power to exercise a discretion…are extremely common. It is not for the courts to re-write the parties' bargain for them, still less to substitute themselves for the contractually agreed decision-maker."[77]

Thus, it is perfectly acceptable and in accordance with freedom of contract for the parties to have such a term in the contract. However, as Lady Hale continues,

> "the party who is charged with making decisions…has a clear conflict of interest…the courts have therefore sought to ensure that such contractual powers are not abused. They have done so by implying a term as to the manner in which such powers may be exercised…"[78]

The scope of this implied term varies according to the contractual context, but the standard of review which a court should apply in considering whether such a discretion has been exercised in an appropriate manner is comparable to that used to review the exercise of discretion by administrative bodies.[79] This involves a two-stage process: first, whether during the decision-making process, the right matters have been taken into account; and secondly, whether the outcome is such that no reasonable decision-maker could have reached it.[80] Overall, therefore, a court will imply "a term into the contract that the decision-making process be lawful and rational in the public law sense, that the decision is made rationally (as well as in good faith) and consistently with its contractual purpose."[81] This is in line with previous cases, which had already begun to align their approach to the review of discretionary powers under a contractual provisions with that used in respect of administrative actions.

(iii)(c) Illegality/Public Policy

In dealing with questions of illegality, there is a tension between the generous conception of freedom of contract in English law and the desire to discourage the entry into illegal contracts.[82] It is a rather complex and somewhat inconsistent aspect of the English law of contract- indeed, one judge has observed that "Illegality and the law of contract is notoriously knotty territory".[83] Generally speaking, illegality can arise if a contract is concluded for an illegal purpose prohibited by law, or during the

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[77] *Ibid*, para [18].
[78] *Ibid*.
[79] See the seminal cases of *Associated Provincial Picture House Ltd v Wednesbury Corporation* p1948] 1 KB 223, and *Council of Civil Service Unions v Minister for the Civil Service* [2015] AC 374.
[80] *Braganza*, para [24].
[81] *Ibid.*, para [30].
[82] McKendrick, *Contract Law*, 11th ed (Palgrave, 2015).
[83] Jacob J in ParkingEye Ltd v Somerfield Stores Ltd. [2012] EWCA Civ 1338, para [28].

performance of an otherwise lawfully concluded contract. In the latter situation, the fact that illegal conduct occurred during the performance of the contract will not usually render the contract itself invalid except when the statutory or common law rule which has been broken envisages that the contract itself should be invalidated.

Alongside illegality, there are also instances where the common law will not enforce contracts which it regards as contrary to Public Policy. However, this does not seem to be a broad principle and the courts have treaded carefully in refusing to uphold contracts on this basis. It has been deployed, *int. al.*, in respect of contracts contrary to good morals, contracts to commit a crime, contracts which are prejudicial to the administration of justice or public relations, and contracts in unreasonable restraint of trade. It is important to note that "public policy" is confined to categories of contracts in respect of which it has been applied in the past, but it seems unlikely that it could be extended to new types of contract. Also, as far as existing categories are concerned, developments are likely to reflect changes to social and moral values, which would restrict further the scope of the common law to intervene in contracts on the grounds of public policy.[84]

In comparison, Art.52(3) and (4) CCL declares that a contract is void where it "conceals an illegal purpose in lawful form" or where it "violates the public interest". This could be a much broader power of intervention in contractual relations than those adopted by the common law under these heads.

(iii)(d) Statutory Controls

The Unfair Contract Terms Act 1977 (UCTA) controls the effectiveness of certain types of exclusion or limitation clauses. In particular, clauses which exclude liability for death or personal injury will always be ineffective.[85] Moreover, clauses excluding or limiting liability for damage caused by negligence[86] or for breach of contract[87] will only be effective if they are shown to be reasonable in the context of the particular contract. In considering whether a term is reasonable, it is necessary to consider whether it is a "fair and reasonable one to have been included in the contract", taking into account the "circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made" (s.11(1) UCTA). Case-law on the application of this test since UCTA was enacted suggests that in commercial contracts, the courts will be slow to interfere with the freedom of the parties to set the extent and limits of their obligations. In

[84] Also, other grounds for intervening in contracts cannot be justified by reference to a general notion of public policy but only on more specific grounds. For example, undue influence is justified on the basis that there is specific victimization of one party by the other: *National Westminster Bank v Morgan* [1985] A.C. 686.
[85] S.2(1) UCTA.
[86] S.2(2) UCTA.
[87] S.3 UCTA.

the early leading case of *Photo Production Ltd v Securicor Ltd*,[88] both Lord Diplock and Lord Wilberforce said that the courts should not intervene where commercial contracts are negotiated between businesspeople of equal bargaining power, able to determine how best to allocate the risks connected with the contract and able to seek insurance protection in case those risks materialise. Clauses subject to the UCTA reasonableness test in contracts concluded between experienced businessmen of comparable bargaining power in a competitive market are likely to pass that test, particularly where insurance is available to a party who would suffer a particular loss.[89] However, courts have been willing to intervene in circumstances where a clause ran counter to a "fundamental assumption" made by all the parties, allowing it to exclude liability for matters which could not be foreseen.[90] Overall, however, exclusion and limitation clauses have generally been upheld where these reflect a freely negotiated allocation of risk between the parties.

The CCL includes comparable restrictions, although these appear to be broader. Article 40 declares void any term which seeks to exclude "the liability of the party supplying the standard term, increases the liability of the other party or deprives the other party of a major right." Article 53 CCL declares void any exemption clause which exempts liability for personal injury to the other party, as well as for property loss caused intentionally or due to gross negligence to the other party. Moreover, Arts.39-43 deal with rules regarding standard terms. In addition, Art.52(5) CCL declares void a contract which violates mandatory provisions of law or administrative regulations.

(iii)(e) Restriction on freedom not to conclude a contract

The Equality Act 2010 provides one further limitation on the principle of freedom of contract by prohibiting the possibility to refuse to contract with someone where this would be discrimination on the grounds of age, gender, disability, sexual orientation, religion, race, nationality, marital status, pregnancy or being a transgender person.

(iv) Good Faith and Fairness

The CCL refers to fairness and good faith as two principles which need to be adhered to during the conclusion and performance of the contract. As already noted, the common law is much more reluctant to deploy such broad principles, preferring instead to utilise specific doctrines to deal with particular instances of unacceptable conduct by one of the parties to a contract.

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[88] [1980] AC 827.
[89] Cf. *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361.
[90] *Britvic Soft Drinks Ltd v Messer UK* [2002] EWCA Civ 548.

A good illustration of how the English common law approach deals with instances of fairness is offered by the on-going reluctance to recognise any obligation on the parties to act in accordance with some sort of "good faith" principle.[91] The general position is that there is no legal duty imposed on the parties to a contract to act in good faith.[92] Indeed, in the context of a duty to negotiate in good faith, a leading House of Lords decision famously rejected such a duty in no uncertain terms. *Walford v Miles*[93] concerned the enforceability of a 'lock-out' agreement, whereby one party was said to have agreed not to negotiate with anybody else with regard to the sale of a business. One of the arguments presented to the court was that such an agreement could be made workable by implying a term into it that negotiations were to continue in good faith. This was firmly rejected by Lord Ackner, who said that

> "The reason why an agreement to negotiate [. . .] is unenforceable is simply because it lacks the necessary certainty. [. . .] The answer suggested depends on whether the negotiations have been determined 'in good faith.' However, the concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations. To advance that interest he must be entitled, if he thinks it appropriate, to threaten to withdraw from further negotiations or to withdraw in fact, in the hope that the opposite party may seek to reopen negotiations by offering him improved terms. [. . .]".[94]

In many ways, this extract reflects the orthodox attitude of the common law: first, parties are in an adversarial position, with each party entitled to pursue its own self-interest. Secondly, that conduct is not subject to a general standard to police the behaviour of each contracting party. The only restriction that exists is that a party must refrain from making misrepresentations, i.e., acting in breach of a specific doctrine dealing with false or inaccurate statements made prior to the conclusion of a contract which induce a party to enter into the contract.

So a principle of good faith is regarded as being incompatible with the autonomy of the contracting parties and, indeed, the principle of freedom of contract. However, if these principles are regarded as

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[91] Although note the rather different attitude in Canada, where the Supreme Court of Canada has now recognised good faith contractual performance as a "general organising principle" which underpin the specific doctrines which effectively constitute good faith performance: *Bhasin v Hryney* [2014] 3 S.C.R. 494. This is a considerably different position from that in English law, which continues to hesitate to recognise any kind of organising principle underpinning the various doctrines which can be said to reflect fairness in contractual performance.

[92] There are some exceptions particularly as a result of the obligation to implement certain EU Directives (Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts [1993] OJ L95/29 and Council Directive 86/653/EEC of 18 December 1986 on the coordination of the laws of the Member States relating to self-employed commercial agents [1986] OJ L382/17).

[93] *Walford v Miles* [1992] 2 AC 128, HL.

[94] *Walford v Miles* [1992] 2 AC 128 at 138.

paramount, the question arises how the courts should treat a term in a contract requiring the parties to act in good faith, including when e.g, negotiating to revise agreed terms such as pricing terms? In *Petromec v Petroleo Brasileiro*,[95] Longmore LJ made *obiter* observations on this question.[96] In this case, the contract included an express term dealing with the re-negotiation of aspects of an existing contract, which was a slightly different situation from that in *Walford v Miles*. Longmore LJ examined three objections to enforcing such a term. First, it was argued that an obligation to negotiate in good faith was effectively an agreement to agree, and therefore too uncertain to be enforceable. However, Longmore LJ noted that this particular term focused on a re-negotiation of costs, and should the parties fail to agree, a court determine what would be reasonable costs. A second objection was that it would be difficult to provide a remedy if there was a breach of the contractual duty to renegotiate in good faith because the losses suffered would be difficult to quantity. Longmore LJ suggested that this could be approach by quantifying any losses on the basis of assessing what would have been reasonable costs. Finally, and perhaps as the strongest objection, it was argued that it would be too difficult to determine whether negotiations had been terminated in good or in bad faith. Longmore LJ conceded that this was a valid concern, but also noted that "the difficulty of a problem should not be an excuse for the court to withhold relevant assistance from the parties by declaring a blanket unenforceability of the obligation."[97] Although these observations do not form part of the *ratio decidendi* of this case, they are indicative of the tension between the reluctance to adopt a legal duty of good faith and upholding the intentions of the parties.

In the more recent decision of *Mid Essex Hospital Services NHS Trust v Compass Group (t/a Medirest)*,[98] a contract for the provision of catering and cleaning services to two hospitals included an express term requiring the parties to "co-operate with each other in good faith". A dispute arose and one of the issues to be considered by the Court of Appeal was the scope of this term. Jackson LJ reaffirmed the position that there was no general duty of good faith in English contract law but the parties could provide for this expressly, as had happened here. However, where such a term was included in a contract expressly, its scope would then depend on how that term was construed. In this instance, the term included also listed a number of matters in respect of which parties had to co-operate in good faith, and so the duty was limited to those matters rather than covering the whole contract.[99]

However, there are signs that the courts may be prepared to go one step further by *implying* a term imposing an obligation on the parties to act in good faith, provided that this would follow from the application of the general test for implying a term into a contract *in fact*, rather than as a matter of law.

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[95] *Petromec v Petroleo Brasileiro* [2005] EWCA Civ 891, [2007] All ER (D) 378.
[96] *Petromec v Petroleo Brasileiro* [115]–[121].
[97] *Petromec v Petroleo Brasileiro* [119].
[98] [2013] EWCA Civ 200
[99] See also TSG Building Services plc v South Anglia Housing Ltd. [2013] EWHC 1151 (TCC).

This was considered in some detail by Leggat J in *Yam Seng v International Trade Corporation*.[100] He first highlighted what are commonly regarded as the main reasons for the "hostility" towards good faith in English law: (1) English law prefers incremental responses to particular problems; (2) English law embodies individualism, leaving parties free to pursue their own self-interest in negotiating and performing a contract (as long as they don't breach a term); (3) a general requirement would create too much uncertainty.[101] He noted that there is " doubt that English law has reached the stage, however, where it is ready to recognise a requirement of good faith as a duty implied by law, even as a default rule, into all commercial contracts. Nevertheless, there seems to me to be no difficulty, following the established methodology of English law for implication of terms in fact, in implying such a duty in any ordinary commercial contract based on the presumed intention of the parties."[102] Provided that the application of established principles on the interpretation of contracts and implication of terms in fact would lead to the conclusion that such a term should be implied, then the courts should do so. Crucially, if such a duty arises in this way, Leggat J says that the basis of this duty would be the presumed intention of parties and as a result, it would not be an illegitimate restriction of party freedom to pursue self-interest. Parties to a contract are free to bind themselves to co-operate for their mutual benefit. Moreover, as it is based on presumed intentions of the parties, they could exclude or modify it expressly.

The approach adopted by Leggat J is a more refined approach towards balancing the orthodox position that parties are free to pursue their self-interest with the corollary that freedom of contract and the pursuit of the self-interest should also permit the recognition of an obligation to act in good faith. Although a good faith duty imposed in law is open to challenge because of its inherent vagueness, a duty based on the presumed intention of the parties and interpreted against the factual background matrix of the specific contract would, in Leggat J's view, be workable.

(v) Equality between the parties

A further general principle in the CCL is the notion of equality between the parties (Arts.2 and 3). As already noted, the English common law of contract is not concerned with ensuring equality between the parties except in some circumstances where a party in a strong position actively takes advantage of this. In particular, the doctrines of duress and undue influence have been developed to police the conduct of a party in a position of strength over the other party. However, attempts to develop these discrete doctrines into a broader general principle have been firmly rejected by the courts.

[100] [2013] EWHC 111 (QB)
[101] At para. [123].
[102] At para. [131].

In *Lloyd's Bank Ltd v Bundy*,[103] Lord Denning suggested that there was a general principle of English contract law for relief to be granted on the basis of "inequality of bargaining power". He had derived this general principle by generalising the common features of doctrines such as duress and undue influence:

> "English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for an consideration which is grossly inadequate, where is bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influence or pressures brought to bear on him by or for the benefit of the other."

However, his observations met with no support from his fellow judges in that case. In subsequent cases, both the Privy Council and the House of Lords firmly closed the door on this idea: In *Pao On v Lau Yiu Long*,[104] a case on duress, the Privy Council rejected a claim that the contract in question was invalid because it had resulted from the unfair use of a dominant bargaining position. The Privy Council thought that accepting such a principle as a ground for relief would make the law uncertain. Subsequently, the House of Lords in *National Westminster Bank v Morgan*[105] also doubted the need for such a general principle.

Conclusions

This paper has sought to contrast the English common law's approach to freedom of contract and associated doctrines with the fundamental principles of the CCL. A general conclusion which is evident from the discussion of the main features of English contract law is its non-interventionist attitude and a generous conception of freedom of contract. Although there are some limitations to this freedom, these generally apply in narrowly defined instances, and the English law of contract does not deploy broad principles to guide the behaviour of contracting parties. A corollary of this is that the parties to a contract have to accept the consequences of the choices they make in exercising that freedom, with courts unwilling to come to their aid when a contract turns out to have severe negative economic consequences for one party. The burden on each contracting party to pay close attention to the substance of the obligations and risks assumed under a contract is therefore very high. In contrast, the CCL seems to subject contracting parties to greater control. Although both systems use comparable labels set limits to

[103] [1975] Q.B. 326.
[104] [1980] A.C. 614
[105] [1985] A.C. 686

the operation of freedom of contract, there is a clear difference in how widely or restrictively these are applied. English common law generally has a very restrictive approach, and courts are reluctant to interfere in the bargain reached between the parties. The general reluctance of the common law towards the deployment of broad general principles means that even categories which could be given a broad interpretation (e.g., public policy) are applied cautiously and in a narrow range of circumstances. The overall effect is that the law generally ensures a high degree of certainty and predictability by having defined instances when the freedom of the party to design their contractual relationship is controlled or restricted, but the corollary of this is that the parties need to take sufficient care to ensure that the contract provides for matters which they regard as important, as only limited assistance will be available from the courts.