

GOOD FAITH IN CONTRACT LAW: THE MALAYSIAN PERSPECTIVE

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Abstract

The recognition of a general duty of good faith in contracts varies by country. In Malaysia, it has become the subject matter of recent cases but without much academic writing. This article seeks to complement the existing legal literature and to generate discussion on this area of law. This article uses a doctrinal approach with comparative law analysis to examine the duty of good faith in contract law. Like England and Singapore, Malaysia does not recognise a general duty of good faith in contracts. However, it has developed the law on a piecemeal basis through contractual implied terms. This approach is pragmatic for two reasons: first, it acknowledges that good faith is already inherent in Malaysian contract law; second, context is crucial- a duty of good faith will only be implied by law and/or in fact into contracts when the tests of implied terms are satisfied. This approach is more likely to respect the intention of the parties than having a general overriding duty of good faith since it affirms the freedom of contract. This article further highlights the potential challenges arising from the introduction of ‘relational’ contracts as to whether a general duty of good faith can be implied in such contracts. It is argued that if the parties intend to impose a duty of good faith, they should expressly stipulate it in the contract for the avoidance of doubt.

Keywords: Good faith, contract law, Malaysia

I INTRODUCTION

It is not uncommon that some legal concepts are like an elephant. ‘It is difficult to describe, but you know it when you see it’.¹ The notion of good faith is one example. Although it does not have a definite legal meaning, it is no stranger to the courts. The more contentious question is whether a general duty of good faith exists in all contracts.

In this article, Part II deals with three preliminary matters, namely the objective and the scope of discussion of this article, as well as the definition of the phrase ‘good faith’

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¹ *Cadogan v Morris* [1998] EWCA Civ 1671, [17] (Court of Appeal). It is known as the elephant test. There, Stuart-Smith LJ refused to set out precise guidelines to determine the validity of a tenant’s statutory notice for the new lease of a flat. His Lordship suggested that most cases will answer the legal question(s) on their own facts.

in existing literature. Part III provides a comparative overview of the approaches taken in civil law jurisdictions and select common law countries. Part IV sets out the research analysis in fourfold. First, it reviews the law of implied terms in Malaysian contract law. It also studies the relevant local cases relating to the implied duty of good faith (if any). Second, it considers the possible implications arising from the recognition of a general duty of good faith in Malaysian contract law. Third, it evaluates whether the approach taken by the Malaysian courts is satisfactory and pragmatic. Fourth, it explores the potential challenges and recommendations in the context of the doctrine of good faith in contract law. Part V concludes that as a matter of general rule, Malaysia does not recognise a general duty of good faith in contracts. However, the Malaysian courts have developed the law on a piecemeal basis by implying a duty of good faith by law and/or in fact into certain contracts based on circumstances of the case. For two reasons discussed therein, this article argues that this approach is satisfactory and pragmatic. It respects the cornerstone of the common law of contract, namely the freedom of contract and contractual certainty. This article goes further to acknowledge the potential challenges arising from the introduction of ‘relational’ contracts as to whether a general duty of good faith is to be implied into such contract. In any event, if it is the parties’ contractual intention to impose a duty of good faith, the parties should expressly stipulate so in the contract.

II PRELIMINARY MATTERS

Three preliminary matters are dealt with here. First, the duty of good faith has noticeably been considered and discussed in several recent cases in Malaysia. As there appears to be lack of academic writing on the doctrine of good faith in contract law taking into account the recent local cases, this article seeks to complement the existing legal literature in Malaysia² and to generate discussion on this area of law.

Second, it is acknowledged that good faith also exists in other areas of law in Malaysia, among others, administrative law,³ company law,⁴ land law⁵ and equity.⁶ This article limits the scope of its discussion to the duty of good faith in contract law.

² Cheong May Fong, ‘Good Faith in Contract Law: A Comparative Survey’ (Universiti Malaya – Universitas Indonesia Law Seminar, Kuala Lumpur, 16 December 2006) 7-9; Visu Sinnadurai and Low Weng Tchung, *Sinnadurai: Law of Contract* (Lexis Nexis, 5th ed, 2023) [4.47]-[4.49]; Nurhidayah Abdullah, ‘Good Faith in Contractual Performance: Chasing a Mirage?’ [2022] (Jan) *Journal of the Malaysian Judiciary* 200-260; Nurhidayah Abdullah and Zuhairah Ariff Abd Ghadas, ‘The Application of Good Faith in Contracts during a Force Majeure Event and Beyond with Special Reference to the COVID-19 Act 2020’ (2023) 14(1) *UUM Journal of Legal Studies* 141-160.

³ A decision of the public authority exercised in bad faith may be subject to judicial review in public law. See, *Mohamad Ezam bin Mohd Noor v Ketua Polis Negara* [2002] 4 MLJ 449, 470 (Federal Court).

⁴ A company director owes a statutory duty to exercise his powers ‘for a proper purpose and in good faith in the best interest of the company’. See, *Companies Act 2016* (Malaysia) s 213(1). See also, *Tengku Dato’ Ibrahim Petra bin Tengku Indra Petra v Petra Perdana Bhd* [2018] 2 MLJ 177, [155]-[192] (Federal Court).

⁵ If a subsequent purchaser is a purchaser in good faith and for valuable consideration, her/his title and interest in the land would be indefeasible notwithstanding any vitiating factors. See, *National Land Code* (Malaysia) proviso to s 340(3). See also, *See Leong Chye v United Overseas Bank (M) Bhd* [2021] 5 MLJ 759, [68] (Federal Court).

⁶ The Malaysian courts have invoked equity to grant relief against unconscionable and/or unfair transactions between the parties to ensure the observance of good conscience and practical justice. See, *PECD Bhd v*

Third, the phrase ‘good faith’ has been defined by dictionaries as ‘faithfulness, loyalty, truthfulness’⁷ and/or ‘done in an honest and sincere way’.⁸ The existing literature has suggested that good faith revolves around, among others, honesty, fair dealing, fidelity to the contractual purpose and cooperation between the parties.⁹ However, these definitions do not translate into a universal content which applies across all contracts. This may cause uncertainty, as ‘good faith presupposes a set of moral standards against which [contracting party is] to be judged, but it is not clear whose (or which) morality this is’.¹⁰ In this regard, Lady Arden extra-judicially clarified that good faith has ‘both a subjective and an objective meaning’.¹¹ One must act in a manner which s/he reasonably believes is honest and fair, and that it must be considered so by the court according to the understanding of a reasonable third party.¹² Ultimately, it is for the court to determine the requirements of good faith applicable to a particular contract based on the context and the circumstances of the case.¹³ It is not uncommon that the court is entrusted to ascertain the scope of open-ended legal concepts based on the factual matrix of the case. One instance is the concept of reasonableness¹⁴ in the law of contract. The doctrine of good faith is arguably another example.

AmTrustee Bhd [2014] 1 MLJ 91, [63]-[68] (Federal Court); *RHB Bank Bhd v Travelsight (M) Sdn Bhd* [2016] 1 MLJ 175, [32] (Federal Court).

⁷ *Oxford English Dictionary* (online, 24 February 2024) ‘good faith’.

⁸ *Cambridge Dictionary* (online, 24 February 2024) ‘good faith’.

⁹ AF Mason, ‘Contract, Good Faith and Equitable Standards in Fair Dealing’ (2000) 116 *Law Quarterly Review* 66, 75-76; Jeannie Marie Paterson, ‘Good Faith Duties in Contract Performance’ (2014) 14 *Oxford University Commonwealth Law Journal* 283, 292-298; Yong Qiang Han, ‘When West Meets East: Thinking Big in Singapore over Good Faith in Commercial Contract Law’ (2019) 1 *Journal of Commonwealth Law* 317, 350-360; Mindy Chen-Wishart and Victoria Dixon, ‘Good Faith in English Contract Law: A Humble “3 by 4” Approach’ in Paul B. Miller and John Oberdiek (eds), *Oxford Studies in Private Law Theory: Volume 1* (Oxford University Press 2020) 204-206; Mindy Chen-Wishart, *Contract Law* (Oxford University Press, 7th ed, 2022) 619-621; Nurhidayah Abdullah (n 2) [7]-[13].

¹⁰ Roger Brownsword, ‘Positive, Negative, Neutral: The Reception of Good Faith in English Contract Law’ in Roger Brownsword, Norma J Hird and Geraint Howells (eds), *Good Faith in Contract: Concept and Context* (Ashgate, 1999) 16.

¹¹ Lady Arden, ‘Coming to Terms with Good Faith’ (2013) 30 *Journal of Contract Law* 199, 200.

¹² David Campbell, ‘Good Faith and the Ubiquity of the “Relational” Contract’ (2014) 77 *Modern Law Review* 475, 485.

¹³ Martin Hogg, ‘The Implication of Terms-In-Fact: Good Faith, Contextualism, and Interpretation’ (2017) 85 *George Washington Law Review* 1660, 1691; Paula Giliker, ‘Contract Negotiations and the Common Law: A Move to Good Faith in Commercial Contracting?’ (2022) 43 *Liverpool Law Review* 175, 198.

¹⁴ The courts are empowered to determine the sum of liquidated damages which is reasonable for a breach of contract. See, *Contracts Act 1950* (Malaysia) s 75. See also, *Cubic Electronics Sdn Bhd v Mars Telecommunications Sdn Bhd* [2019] 6 MLJ 15, [66] (Federal Court). See further, Ng Seng Yi, ‘Cubic Electronics: A Fresh Look or A Daze on Section 75 of the Contracts Act 1950’ (2021) 3 *Malayan Law Journal* lxxxviii, cxiv-cxvii; May Fong Cheong and Pei Meng Tan, ‘The New Law on Penalties in Malaysia: The Impact of Cubic Electronics after Cavendish Square’ (2023) 38 *Journal of Contract Law* 132, 142-147.

III COMPARATIVE OVERVIEW OF GOOD FAITH

A *Civil law*

The notion of good faith finds its origins in Roman law.¹⁵ In Germany¹⁶ and Italy,¹⁷ the Civil Codes impose a general obligation to act in good faith on the contracting parties. The French Civil Code provides that ‘[c]ontracts must be negotiated, made and performed in good faith’.¹⁸ It extends the duty of good faith not only to the performance of the contract, but also the negotiation and formation of the contract. Noticeably, the Civil Codes do not generally define good faith. One may argue that it is immaterial to define good faith.¹⁹ It is because the requirements and contents of good faith are largely determined based on the facts of the case.²⁰ As a result, civil law judges ‘have a greater power to evaluate the fairness of the contract and intervene to reinstate the balance of interests between the parties’.²¹

B *United States*

Despite being a common law country, the United States has codified its commercial law in the form of the Uniform Commercial Code. It provides that ‘[e]very contract... imposes an obligation of good faith in its performance or enforcement’.²² Similarly, the American Restatement (Second) of Contracts states that ‘[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement’.²³ Two observations are relevant here. First, unlike the Civilian version, the American version of good faith only applies to the performance and enforcement of contracts but not at the pre-contractual stage. Second, although the Uniform Commercial Code defines good faith as ‘honesty in fact in the conduct or transaction concerned’²⁴ and ‘honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade’,²⁵ its scope remains vague. It is ‘difficult to determine what a trade is, and a given trade may not have any standards [of good faith] at all’.²⁶ For completeness, in some lender liability

¹⁵ Martin Josef Schermaier, ‘*Bona Fides* in Roman Contract Law’ in Reinhard Zimmermann and Simon Whittaker (eds), *Good Faith in European Contract Law* (Cambridge University Press, 2000) 63-92.

¹⁶ German Civil Code, para 242.

¹⁷ Italian Civil Code, art 1337.

¹⁸ French Civil Code, art 1104.

¹⁹ Woo Pei Yee, ‘Protecting Parties’ Reasonable Expectations: A General Principle of Good Faith’ (2001) 1 *Oxford University Commonwealth Law Journal* 195, 220-221.

²⁰ Martijn Hasselink, ‘Good Faith’ in Arthur Hartkamp and others (eds), *Towards A European Civil Code* (Kluwer Law International, 1998) 289.

²¹ Giuditta Cordero Moss, ‘Commercial Contracts and European Private Law’ in Christian Twigg-Flesner (ed) *The Cambridge Companion to European Union Private Law* (Cambridge University Press, 2015) 153.

²² Uniform Commercial Code, s 1.203.

²³ Restatement, s 205.

²⁴ Uniform Commercial Code, s 1.201(19).

²⁵ Uniform Commercial Code, s 2.103(1)(b).

²⁶ Robert S Summers, ‘The Conceptualisation of Good Faith in American Contract Law: A General Account’ in Reinhard Zimmermann and Simon Whittaker (eds), *Good Faith in European Contract Law* (Cambridge University Press, 2000) 122.

cases, the American courts appear to have extended the contractual liability to tortious liability for breach of an implied duty of good faith and fair dealing.²⁷

C Canada

In Canada, a duty of good faith has been demonstrated in three circumstances before 2014.²⁸ They include rules which (i) require the cooperation of the parties to achieve the contractual purposes,²⁹ (ii) relate to the exercise of contractual discretion which must not be made arbitrarily,³⁰ and (iii) preclude a party from conduct which seeks to evade contractual obligations.³¹

In the 2014 case of *Bhasin*,³² the Supreme Court of Canada introduced a general duty of honesty in contractual performance. There, a vendor was alleged to have terminated a dealership agreement for an improper purpose. The vendor allegedly forced a merger of its dealer with another competing dealer and appointed the competing dealer to audit the dealer's business records. The dealer argued that the vendor's termination was not made in good faith. In the judgment, the Canadian apex court recognised 'good faith contractual performance [as] a general organising principle of the common law of contract'.³³ It went on to acknowledge a specific duty to 'act honestly in the performance of contractual obligations'.³⁴ As the parties may reasonably expect 'a basic level of honesty and good faith in contractual dealings', they 'must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract'.³⁵ There, it was decided that the vendor was in breach of this specific duty of honesty in contractual performance for its termination of the dealership agreement. Noticeably, this duty does not operate as an implied term but rather a general doctrine of contract law.³⁶ Since then, *Bhasin* has been considered and/or applied by the same court in two recent occasions.³⁷

²⁷ *First National Bank v Twombly* 689 P.2d 1226, 1230 (1984). However, tortious breach of duty of good faith remains contentious and is arguably not of general application: see Anon, 'Lender Liability: Breach of Good Faith Lending and Related Theories' (1988) 64 *North Dakota Law Review* 273, 296-298.

²⁸ John McCamus, 'Abuse of Discretion, Failure to Cooperate and Evasion of Duty: Unpacking the Common Law Duty of Good Faith Contractual Performance' (2004) 29 *Advocate Quarterly* 72, 77-90.

²⁹ *Dynamic Transport Ltd v OK Detailing Ltd* [1978] 2 SCR 1072 (Supreme Court).

³⁰ *Mitsui & Co (Canada) Ltd v Royal Bank of Canada* [1995] 2 SCR 187 (Supreme Court).

³¹ *Mason v Freedman* [1958] SCR 483 (Supreme Court).

³² *Bhasin v Hrynew* [2014] 3 SCR 494 (Supreme Court). See also, John Enman-Beech, 'The Good Faith Challenge' (2019) 1 *Journal of Commonwealth Law* 35, 63-64.

³³ *Ibid* [33].

³⁴ *Ibid*.

³⁵ *Ibid* [60] and [73].

³⁶ *Ibid* [74]. See also, John D McCamus, 'The New General "Principle" of Good Faith Performance and the New "Rule" of Honesty in Performance in Canadian Contract Law' (2015) 32 *Journal of Contract Law* 103, 113.

³⁷ *CM Callow Inc v Zollinger* [2020] SCJ No.45 (Supreme Court); *Wastech Services Ltd v Greater Vancouver Sewerage and Drainage District* [2021] SCJ No.7 (Supreme Court). See also, John D McCamus, 'The Canadian Doctrine of Good Faith Contractual Performance: Further Clarification' (2022) 38 *Journal of Contract Law* 1.

D England

In *Carter*, Lord Mansfield once sought to broaden the application of good faith duty in insurance contracts to a ‘governing principle... applicable to all contracts and dealings’.³⁸ However, as commercial law prefers ‘the benefits of simplicity and certainty which flow from requiring those engaging in commerce to look after their own interests’, this proposition ‘did not survive’.³⁹ Indeed, the House of Lords in *Walford* authoritatively held that the requirement to negotiate in good faith at pre-contractual stage was unenforceable due to the lack of certainty. It would be inherently ‘repugnant to the adversarial position’ of the negotiating parties where each party are entitled to pursue their own interest.⁴⁰ Bingham LJ in *Interfoto* observed that there is no overriding principle of good faith. However, his Lordship acknowledged that English law has instead developed ‘piecemeal solutions in response to demonstrated problems of unfairness’.⁴¹ Three instances are relevant here.

First, a duty of good faith has been implied by law in certain contracts, such as employment contracts,⁴² partnership contracts⁴³ and insurance contracts.⁴⁴ In these instances, it upholds the contractual relationship of trust and confidence between the parties. What remains uncertain is whether a general duty of good faith can be implied in other contracts. In *Yam Seng*,⁴⁵ Leggatt J found on the facts that a long-term distribution agreement constituted a relational contract. An implied duty of good faith was imposed on the vendor to not knowingly supply misleading market information to the distributor.⁴⁶ Although *Yam Seng* is a judgment of the court of first instance with limited precedential value,⁴⁷ it has nevertheless reignited the debate on the recognition of a general duty of good faith in all (relational) contracts.⁴⁸ In fact, *Yam Seng*’s proposition has met with a

³⁸ *Carter v Boehm* (1766) 3 Burr 1905, 1909-1911.

³⁹ *Manifest Shipping Co Ltd v Uni-Polaris Ins Co Ltd (The Star Sea)* [2001] UKHL 1, [45] (House of Lords).

⁴⁰ *Walford v Miles* [1992] AC 128, 138 (House of Lords).

⁴¹ *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] QB 433, 439 (Court of Appeal).

⁴² *Malik v BCCI* [1998] AC 20, 45-49 (House of Lords). See also, Lord Bingham, ‘From Servant to Employee: A Study of the Common Law in Action’ in Sir Jeffrey Jowell (eds), *Lives of the Law: Selected Essays and Speeches 2000-2010* (Oxford University Press, 2011) 255-268.

⁴³ Roderick I’Anson Banks, *Lindley & Banks on Partnership* (Sweet & Maxwell, 21st ed, 2022) ch 16; Laura Macgregor, ‘The Partner’s Fiduciary and Good Faith Duties: More than Just an Agent?’ in Paul S Davies and Tan Cheng-Han (eds), *Intermediaries in Commercial Law* (Hart Publishing, 2022) 267-270.

⁴⁴ *Insurance Act 2015*, ss 2-8 (new statutory duty of fair presentation as an example of good faith). See also, John Birds and others, *MacGillivray on Insurance Law* (Sweet & Maxwell, 15th ed, 2022) ch 16.

⁴⁵ *Yam Seng Pte Ltd v International Trade Corp Ltd* [2013] EWHC 111 (High Court). See case commentaries, Edward Granger, ‘Sweating Over an Implied Duty of Good Faith’ [2013] *Lloyd’s Maritime and Commercial Law Quarterly* 418, 421-426; Ewan McKendrick, ‘Good Faith in the Performance of a Contract in English Law’ in Larry DiMatteo and Martin Hogg (eds), *Comparative Contract Law: British and American Perspectives* (Oxford University Press, 2015) 196-209; JW Carter and Wayne Courtney, ‘Good Faith in Contracts: Is There an Implied Promise to Act Honestly?’ (2016) 75 *Cambridge Law Journal* 608, 609-619; Ewan McKendrick, ‘Doctrine and Discretion in the Law of Contract Revisited’ (2019) 7 *Chinese Journal of Comparative Law* 1, 13-15.

⁴⁶ *Ibid* [141]-[144].

⁴⁷ Ewan McKendrick, ‘Good Faith in the Performance of a Contract in English Law’ (n 48) 204-205; Yong Qiang Han (n 9) 331.

⁴⁸ Zhong Xing Tan, ‘Keeping Faith with Good Faith? The Evolving Trajectory Post-Yam Seng and Bhasin’ [2016] *Journal of Business Law* 420, 429-437.

mixed reaction⁴⁹ by the court of first instance⁵⁰ and the Court of Appeal,⁵¹ but without an authoritative judicial guidance by the Supreme Court⁵² to date.

Second, in determining whether a contractual discretion should be exercised in good faith, a growing number of cases have applied administrative law principles. If a contract empowers *A* with a discretionary right, *A* must not exercise her/his contractual discretion arbitrarily. Contractual discretion is not ‘unfettered’.⁵³ In *Paragon*,⁵⁴ a lender was authorised to vary the interest rate on loans payable by the borrower at its discretion. The Court of Appeal held that there was an implied term where the lender must not exercise its discretion ‘dishonestly, for an improper purpose, capriciously or arbitrarily’.⁵⁵ Similarly, although the discretion to value investment securities could be subjective considering the fluctuating interest rate of the market, it is necessary to restrain one from abusing its contractual discretion.⁵⁶ In *Socimer*, Rix LJ suggested that contractual discretion should ‘be limited, as a matter of necessary implication, by concepts of honesty, good faith, and genuineness, and the need for the absence of arbitrariness, capriciousness, perversity and irrationality’.⁵⁷ To that end, contractual discretion ‘must be exercised consistently with its contractual purpose’.⁵⁸ The parties should adopt a decision-making process similar to the *Wednesbury* public law concept.⁵⁹ It examines the mechanism, and not the quality, of the discretion where it should not be made irrationally or arbitrarily.⁶⁰

Third, if the contract expressly requires the parties to act in good faith in contractual performance, the court will generally give effect to it. For instance, a term which expressly requires the parties to ‘resolve the dispute or claim by friendly discussion’ before the commencement of the intended arbitration has been ruled as an enforceable condition

⁴⁹ Gerard McMeel, ‘Foucault’s Pendulum: Text, Context and Good Faith in Contract Law’ (2017) 70 *Current Legal Problems* 365, 395-396.

⁵⁰ *Bates v Post Office Ltd* [2019] EWHC 606, [702]-[742] (High Court). cf *TSG Building Services plc v South Anglia Housing Ltd* [2013] EWHC 1151, [44]-[46] (High Court).

⁵¹ *Candey Ltd v Boshah* [2022] EWCA Civ 1103, [29]-[43] (Court of Appeal). cf *Re Compound Photonics Group Ltd v Vollin Holdings Ltd* [2022] EWCA Civ 1371, [228]-[234] (Court of Appeal). See also, *Globe Motors Inc v TRW Lucas Varsity Electrical Steering Ltd* [2016] EWCA Civ 396, [67]-[71] (Court of Appeal).

⁵² In *Pakistan International Airlines Corp v Times Travel (UK) Ltd* [2021] UKSC 40, [26]-[27] (Supreme Court). Lord Hodge observed in obiter in the context of lawful act economic duress that English law has never recognised a general principle of good faith in contracting nor a doctrine of inequality of bargaining power.

⁵³ Jack Beatson, ‘Public Law Influences in Contract Law’ in Jack Beatson and Daniel Friedmann (eds), *Good Faith and Fault in Contract Law* (Oxford University Press, 1995) 269.

⁵⁴ *Paragon Finance plc v Nash* [2001] EWCA Civ 1466 (Court of Appeal).

⁵⁵ *Ibid* [32].

⁵⁶ David Foxton, ‘A Good Faith Goodbye? Good Faith Obligations and Contractual Termination Rights’ [2017] *Lloyd’s Maritime and Commercial Law Quarterly* 360, 363-364.

⁵⁷ *Socimer International Bank Ltd v Standard Bank London Ltd* [2008] EWCA Civ 116, [66] (Court of Appeal). cf *Compass Group UK and Ireland Ltd v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200, [91]-[92] (Court of Appeal). See also, Jonathan Morgan, ‘Against Judicial Review of Discretionary Contractual Powers’ [2008] *Lloyd’s Maritime and Commercial Law Quarterly* 230, 239-240.

⁵⁸ *British Telecommunications plc v Telefonica O2 UK Ltd* [2014] UKSC 42, [37] (Supreme Court).

⁵⁹ *Braganza v BP Shipping Ltd* [2015] UKSC 17, [28]-[31] (Supreme Court). The *Wednesbury* principle was derived from *Associated Provincial Picture House Ltd v Wednesbury Corp* [1948] 1 KB 223 (Court of Appeal). A decision of the public authority can be quashed by a court order of certiorari if it is wholly unreasonable.

⁶⁰ Michael Bridge, ‘Limits on Contractual Freedom’ (2019) 7 *Chinese Journal of Comparative Law* 387, 407

precedent to invoke the arbitration clause.⁶¹ Also, if a development agreement stipulates that ‘[i]n all matters relating to this agreement the parties will act with the utmost good faith towards one another’, the court in *Berkeley* held that the landowners who intended to sell the land to a third party but not the developer were in breach of the said clause.⁶² They were enjoined from selling the land before the developer became entitled to be paid a fee for its work done in developing the land. For completeness, in *Compass*, the Court of Appeal in turn cautioned that if the contract contains more specific provisions, ‘care must be taken not to construe a general and potentially open-ended obligation such as the obligation to co-operate or “to act in good faith”’, which may override the effectiveness of the specific clauses.⁶³

E Singapore

In Singapore, the duty of good faith in contracts has been developed on a piecemeal basis. In *Ng Giap Hon*,⁶⁴ a stockbroker authorised its agent to trade in securities in return for a commission under an agency agreement. The agent sued the stockbroker for commissions which were allegedly due to him by two clients but which the stockbroker had intercepted. He argued that in doing so, the stockbroker had breached its implied duty to act in good faith for the business interception. The Court of Appeal refused to imply a term of good faith where the stockbroker would not do anything to prevent the agent from earning his commissions. However, the apex court did not outrightly reject the doctrine of good faith.⁶⁵ It was observed that much clarifications would be required and until ‘the theoretical foundations [and] structure of this doctrine are settled’, it would be inadvisable to apply it in practice.⁶⁶

To this end, the law has recognised certain categories of contract such as insurance contracts as contracts of utmost good faith.⁶⁷ Second, the courts will not intervene in the exercise of a contractual discretion so long as it is exercised honestly and in good faith, and in the manner which is not capricious or arbitrary.⁶⁸ Third, an express duty to negotiate in good faith within an existing contractual framework is legally enforceable.

⁶¹ *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd* [2014] EWHC 2104, [3] and [26] (High Court).

⁶² *Berkeley Community Villages Ltd v Pullen* [2007] EWHC 1330, [33], [109] and [142] (High Court).

⁶³ *Compass* (n 57) [154]. There, the Court of Appeal found on the facts that there was no breach of the express term to ‘co-operate with each other in good faith’.

⁶⁴ *Ng Giap Hon v Westcomb Securities Pte Ltd* [2009] SGCA 19 (Court of Appeal).

⁶⁵ Colin Liew, ‘A Leap of Good Faith in Singapore Contract Law’ [2012] *Singapore Journal of Legal Studies* 416, 439.

⁶⁶ *Ng Giap Hon* (n 64) [60]. See also, *KS Energy Services Ltd v BR Energy (M) Sdn Bhd* [2014] SGCA 16, [3] (Court of Appeal).

⁶⁷ *Tay Eng Chuan v Ace Insurance Ltd* [2008] SGCA 26, [30] and [32] (Court of Appeal). Cf *Dong Wei v Shell Eastern Trading (Pte) Ltd* [2022] SGHC(A) 8, [82] (High Court) (employment contract); *AL Shams Global Ltd v BNP Paribas* [2018] SGHC 143, [49] (High Court) (banking contract).

⁶⁸ *ABN AMRO Clearing Bank NV v 1050 Capital Pte Ltd* [2015] SGHC 271, [83]-[85] (High Court); *Edwards Jason Glenn v Australia and New Zealand Banking Group Ltd* [2012] SGHC 61, [99]-[102] (High Court); *MGA International Pte Ltd v Wajilam Exports (Singapore) Pte Ltd* [2010] SGHC 319, [103]-[107] (High Court); See also, Ong Ken Wei, ‘The Limits to Contractual Discretion’ (2021) 33 *Singapore Academy of Law Journal* 919.

In a lease agreement which contained an express clause to negotiate the new rental term in good faith, the Court of Appeal of Singapore in *HSBC* held that the parties could not ‘simply walk away from the negotiating table for no rhyme or reason’ and must duly comply with express rent review mechanism.⁶⁹

In short, a general duty of good faith exists in civil law jurisdictions. However, it remains unsettled but evolving in common law countries. The United States imposes a statutory requirement of good faith via the Uniform Commercial Code. Canada has introduced a specific duty of honesty in contractual performance. On the other hand, England and Singapore have developed the law on a piecemeal basis without recognising an overriding duty of good faith in contracts.⁷⁰

IV ANALYSIS OF MALAYSIAN POSITION

A Implied terms and good faith

Before examining the Malaysian cases, it is relevant to recap three types of implied terms in Malaysian contract law. First, a custom or usage of any market or trade which has been well-accepted can be implied into contracts.⁷¹ Second, a term can be implied by law into certain contracts based on previous decided cases of identical factual matrix. Once a term is implied by law, it will be implied into all contracts of a similar class. Many of these implied terms have been incorporated into statutes.⁷² They seek to address the broader concerns of policy consideration and contractual unfairness. Third, the court can imply a term in fact if it is (i) in the interest of giving business efficacy to the contract, and (ii) so obvious to an officious bystander that it goes without saying the parties must have intended to incorporate the term as part of their contract.⁷³ Unlike the English law position where the law is applied as an alternative test to each other,⁷⁴ the objective ‘business efficacy’ and the subjective ‘officious bystander’ tests must both be satisfied before a term can be implied into the contract in Malaysian contract law.⁷⁵ An implied term ‘must be capable of clear expression’ and ‘must not contradict any express term of the contract’.⁷⁶

⁶⁹ *HSBC Institutional Trust Services (Singapore) Ltd v Toshin Development Singapore Pte Ltd* [2012] SGCA 48, [37] (Court of Appeal).

⁷⁰ See the similar approach in Singapore: *Ng Giap Hon* (n 64) [60]; *KS Energy Services Ltd v BR Energy (M) Sdn Bhd* [2014] SGCA 16, [3] (Court of Appeal). See also, *The One Suites Pte Ltd v Pacific Motor Credit (Pte) Ltd* [2015] SGCA 21, [44] (Court of Appeal); *PH Hydraulics & Engineering Pte Ltd v AirTrust (Hong Kong) Ltd* [2017] SGCA 26, [133] (Court of Appeal).

⁷¹ *Sinnadurai: Law of Contract* (n 2) [4.20]-[4.22].

⁷² *Sale of Goods Act 1957* (Malaysia) ss 14 (implied undertaking as to title) and 16 (implied condition as to quality or fitness); *Hire-Purchase Act 1967* (Malaysia) s 7 (conditions and warranties to be implied in every hire-purchase agreement); *Consumer Protection Act 1999* (Malaysia), ss 30-38 (implied guarantees for supply of goods) and 53-56 (implied guarantees for supply of services).

⁷³ *Sababumi (Sandakan) Sdn Bhd v Datuk Yap Pak Leong* [1998] 3 MLJ 151, 168-172 (Federal Court).

⁷⁴ *Mark and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72, [16]-[31] (Supreme Court); *Barton v Morris* [2023] UKSC 3, [21]-[23] (Supreme Court). cf *AG of Belize v Belize Telecom Ltd* [2009] UKPC 10, [21] (Privy Council), where Lord Hoffmann suggested that the process of implying terms into a contract is part of the exercise of contractual interpretation. The central question is ‘what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?’.

⁷⁵ See *Leong Chye v United Overseas Bank Bhd* [2019] 1 MLJ 25, [76] (Federal Court).

⁷⁶ See *Leong Chye v United Overseas Bank (M) Bhd* [2021] 5 MLJ 759, [85] (Federal Court).

In a series of recent cases, the Malaysian appellate court is seemingly reluctant to imply a general duty of good faith into contracts. In *Seven Seas*,⁷⁷ a principal invoked the termination clause and served on its contractor a six-months' notice of its intention to terminate the sub-contractor agreement. The contractor argued that considering the close commercial relationship between the parties, there shall be an implied duty of good faith and honesty to not terminate the contract by a notice simpliciter.⁷⁸ The Malaysian Court of Appeal rejected the contractor's argument. It opined that the existence of the implied duty of good faith depends on the 'expressed intention of the parties which is to be ascertained from the terms of the contract, and on the nature of the relationship between the parties'.⁷⁹ There, the termination of the contract was held to be valid because it was made in accordance with the express termination clause. More recently, in *Hewlett-Packard*,⁸⁰ a product supplier terminated the appointment of its reseller due to a change of its regional company policy. Although the parties had a long-standing business relationship, the Malaysian Court of Appeal held that the product reseller agreement in question did not impose an implied duty of good faith on the supplier to ensure the continuation of the reseller's status.⁸¹ The appellate court noted that 'there is no general implied duty of good faith in commercial contracts and the court should be slow to imply such a duty'.⁸² Again, in *Aseambankers*,⁸³ the Malaysian Court of Appeal held in the context of a banker and customer contractual relationship that 'there is no general duty of good faith in common law'.⁸⁴ Even if there was such a duty, it was found that the bank had not breached its duty of good faith as it had acted within its express contractual rights at all material times.⁸⁵ In the supporting judgment, Mohamad Ariff JCA however acknowledged that 'it will be unwise to simply dismiss in totality the existence of a duty of good faith and fair dealing in contractual relationships'.⁸⁶ If a duty of good faith is to be taken simply as an implied contractual duty to act in good faith after considering the 'construction of the particular contract against its contractual background and context, it can be applied in a practical sense'.⁸⁷ The observations made by Mohamad Ariff JCA are evident in three circumstances.

First, a duty of good faith has been implied by law into certain classes of contract.⁸⁸ It is an implied term of every employment contract that an employee must serve her/his

⁷⁷ *Seven Seas Industries Sdn Bhd v Philips Electronic Supplies (M) Sdn Bhd* [2008] 4 CLJ 217 (Court of Appeal).

⁷⁸ Ibid [28].

⁷⁹ Ibid [30].

⁸⁰ *Hewlett-Packard (M) Sdn Bhd v Agih Tinta Sdn Bhd* [2022] 6 MLJ 853 (Court of Appeal).

⁸¹ Ibid [66]-[83].

⁸² Ibid [79].

⁸³ *Aseambankers Malaysia Bhd v Shencourt Sdn Bhd* [2014] 4 MLJ 619 (Court of Appeal). See also, Lee Hock Beng, 'Good Faith and the Aseambankers Case' (2017) 6 MLJ xxxvii.

⁸⁴ Ibid [126] and [325]. See also, *Bank Pembangunan Malaysia Bhd v Ketheeswaran a/l M Kanagaratnam* [2022] 5 MLJ 393, [41] (Court of Appeal). cf *Tan Ah Sam v Chartered Bank* [1971] 1 MLJ 28, 29 (Federal Court). There, the Malaysian Federal Court held that banks must act in good faith and without negligence in dealing with a crossed cheque under the then Malaysian Bills of Exchange Ordinance, ss 80 and 82C.

⁸⁵ Ibid [126].

⁸⁶ Ibid [322].

⁸⁷ Ibid [322].

⁸⁸ *Simadurai: Law of Contract* (n 2) [4.48].

employer with good faith and fidelity.⁸⁹ Also, a partner owes her/his co-partners a duty to act in good faith in all dealings arising from their partnership agreement.⁹⁰ Besides, the parties to a joint venture agreement must act in good faith towards each other in achieving the objective(s) of the joint venture.⁹¹ A contract of insurance is a contract of utmost good faith. Both the insured and insurer have a continuing duty of good faith towards each other.⁹² The law is well-established in these contexts for policy consideration. In these instances, a fiduciary relationship of trust and confidence exists between the parties. Where contracting parties are of significant unequal bargaining power, the law does not simply imply a duty of good faith to protect the weaker party from unfairness. Rather, Parliament has intervened to redress the balance. Under the Malaysian Consumer Protection Act 1999, an unfair term of a consumer contract may be declared as unenforceable or void.⁹³ In determining whether a term is procedurally or substantively unfair, the court may consider, among others, the bargaining strength of the parties⁹⁴ and/or whether the term is substantially contrary to reasonable standards of fair dealing.⁹⁵

Second, the position is less clear in the contracts apart from the recognised classes of contract above. In cases where the ‘business efficacy’ and the ‘officious bystander’ tests are satisfied, the court is willing to imply a duty of good faith in fact into contracts. The early case of *Pasuma*⁹⁶ is illustrative. It concerned a dispute arising from an exclusive distribution agreement. The Federal Court observed that ‘it is difficult to resist the conclusion that there was an implied condition that... [contracting] parties should be reasonably honest and truthful with each other’.⁹⁷ It will be recalled that in the English case of *Yam Seng*, Leggatt J found on the facts that the vendor was in breach of its duty of good faith towards its exclusive distributor for knowingly providing misleading market information. However, his Lordship added that it was fact-sensitive based on the presumed intention of the parties. His Lordship doubted that English law was ready to recognise its implication as a ‘default rule... into all commercial contracts’.⁹⁸ Arguably, *Pasuma* should similarly be construed within its factual matrix. It did not introduce a general duty of good faith in contracts. Indeed, in holding that there was an implied duty of good faith between the parties, the Malaysian apex court examined the facts and the nature of the parties’ contractual relationship. There, *A* and *B* entered into an exclusive

⁸⁹ *Zaharen bin Hj Zakaria v Redmax Sdn Bhd* [2016] 5 MLJ 91, [44] (Court of Appeal).

⁹⁰ *Vasu Devan v Nair* [1985] 1 MLJ 137, 141-142 (Federal Court); *Soo Boon Siong v Saw Fatt Seong* [2008] 1 MLJ 27, [21]-[26] (Court of Appeal); *Takako Sakao v Ng Pek Yuen* [2009] 6 MLJ 751, [12] (Federal Court).

⁹¹ *Genisys Integrated Engineers Pte Ltd v UEM Genisys Sdn Bhd* [2008] 6 MLJ 237, [8] (Court of Appeal); *Ezzen Heights Sdn Bhd v Ikhlas Abadi Sdn Bhd* [2011] 4 MLJ 173, [26] (Court of Appeal).

⁹² *Leong Kum Whay v QBE Insurance (M) Sdn Bhd* [2006] 1 MLJ 710, [15] (Court of Appeal); *ALW Car Workshop Sdn Bhd v AXA Affin General Insurance Bhd* [2019] 4 MLJ 561, [26]-[35] (Federal Court); *AmGeneral Insurance Bhd v Sa' Amran a/l Atan* [2022] 5 MLJ 825, [163] (Federal Court).

⁹³ *Consumer Protection Act 1999* (Malaysia) s 24G.

⁹⁴ *Consumer Protection Act 1999* (Malaysia) s 24C(2)(b) (procedural unfairness).

⁹⁵ *Consumer Protection Act 1999* (Malaysia), ss 24C(2)(c) (procedural unfairness) and 24D(2)(d) (substantive unfairness).

⁹⁶ *Pasuma Pharmacal Corp v McAlister & Co Ltd* [1965] 1 MLJ 221 (Federal Court). See also, *Gentali (M) Sdn Bhd v Kawasaki Sunrock Sdn Bhd (No.3)* [1998] 5 MLJ 409, 424 (High Court).

⁹⁷ *Ibid* 226.

⁹⁸ *Yam Seng* (n 45) [131].

agreement for the distribution of *B*'s chicken essence in certain countries. Despite *B*'s undertaking to replace defective chicken essence supplied by it to *A*, *B* found out that stocks of poor quality nevertheless remained in the market. *A* had fraudulently inflated the amount of chicken essence to be replaced by *B*. The court applied the twofold tests of an implied term. First, suppose an officious bystander raises a question as to what would happen if a party were to deceive the other on the defective stock. A reasonable man will simply conclude that it 'would be the end of the relationship between [them]'.⁹⁹ Second, the distribution agreement was to 'continue for a very long time and throughout that time there was always the possibility that the question of replacement of defective stock would arise'.¹⁰⁰ It would be difficult for the parties to continue with their business dealings after discovering that *A* had been defrauding *B* for its own benefits. The business efficacy of the contract had regrettably been undermined.

Third, the court has followed the English law position in applying public law principle of *Wednesbury* reasonableness¹⁰¹ in the exercise of contractual discretion in good faith. In *KAB Corp*,¹⁰² a contractual discretion was conferred on *A* to determine the amount of the administrative fee for the procurement of its consent for *B*'s third-party assignment of a property. The Court of Appeal observed that such discretion must not subject *B* to *A*'s 'uninhibited whim and fancy'.¹⁰³ It was necessary to imply a term that the discretion must be exercised honestly and in good faith, having regard to the contractual provisions and the context of the case.¹⁰⁴ It was a presumed reasonable expectation and common intention of the parties that 'there should be a genuine and rational, as opposed to an empty or rational, exercise of discretion'.¹⁰⁵ Also, if a main contractor 'reserve[s] the right to omit wholly or in part of the works' from its subcontractor and that '[n]o claim whatsoever will be entertained for such omissions' under a subcontract, the discretionary right could 'not be exercised unreasonably in the absence of good faith'.¹⁰⁶ If the subcontractor was/is at all material times ready to perform and complete the contract as agreed, the main contractor could not prevent it from doing so without proper reasons.¹⁰⁷

In summary, three propositions can be made here. First, as a matter of general rule, the Malaysian contract law does not recognise a general duty of good faith. Second, the general rule is not absolute and is subject to exceptions. A contractual duty of good faith can be implied by law and/or in fact if the construction of the contract against its background renders it necessary and without it the contract will not work. Third, the implied duty of good faith must not contradict the express terms of the contract. These

⁹⁹ *Pasuma* (n 96) 220-221.

¹⁰⁰ *Pasuma* (n 96) 221.

¹⁰¹ In Malaysian public law, the general rule is that a discretion should be exercised reasonably and for a proper purpose. It cannot be free from legal restraint. Where it is wrongly exercised, it becomes the duty of the courts to intervene. See, *Pengarah Tanah dan Galian v Sri Lempah Enterprise Sdn Bhd* [1979] 1 MLJ 135, 148 (Federal Court).

¹⁰² *KAB Corp Sdn Bhd v Master Platform Sdn Bhd* [2019] 6 MLJ 752 (Court of Appeal).

¹⁰³ *Ibid* [29].

¹⁰⁴ *Ibid* [29]-[30].

¹⁰⁵ *Ibid* [29].

¹⁰⁶ *Pembinaan Perwira Harta Sdn Bhd v Letrikon Jaya Bina Sdn Bhd* [2013] 2 MLJ 620, [2e] and [11] (Federal Court).

¹⁰⁷ *Ibid* [15].

propositions share striking similarities with the piecemeal development of the doctrine of good faith in the law of contract in England and Singapore. In the following sections, this article examines the possible implications of a general duty of good faith in contracts. It also evaluates whether this piecemeal approach is satisfactory and pragmatic.

B Implications of a general duty of good faith

A general duty of good faith means that a duty of good faith is implied into all contracts regardless of the contractual background and context.¹⁰⁸ Like express term, the breach of an implied term creates a cause of action in contract. If the breach of an implied term of good faith duty is so fundamental and/or goes to the root of the contract, the innocent party is entitled to either terminate or affirm the contract and claim damages.¹⁰⁹ The Malaysian High Court's decision of *Aseambankers*¹¹⁰ was a case of a lender-borrower/banker-customer relationship. Upon relying on the American authorities, the High Court held that a breach of the implied duty of good faith can be extended to incur a separate tortious liability on the defaulting party. However, it was overruled by the Court of Appeal for the very reason that Malaysian court is bound by the confines of the Malaysian Civil Law Act 1956¹¹¹ to apply English law in commercial matters in the absence of local written law.¹¹²

Also, a general duty of good faith is inconsistent with freedom of contract and contractual certainty. Such a duty not only will be imposed on the parties regardless of the contractual background and context, but can also in effect disregard the express terms of the contract which have been freely agreed upon by the parties. In *Aseambankers*, the borrower contended that the bank had threatened it with legal action if it did not repay and service the interest on the loan under the facility agreement.¹¹³ The borrower further alleged that its default was due to a breach of the bank's duty to act in good faith to allow drawdown of the loan facility for the borrower's benefit to complete a construction project.¹¹⁴ Suppose the bank owes a general duty of good faith towards the borrower, the bank would in effect be faulted for enforcing its contractual rights to recover loan under the express terms of the facility agreement. A banking transaction of significant value is commonly noted for detailed terms being incorporated in the contract at arm's length and on the advice of legal counsel. To subject it to a general duty of good faith will clearly undermine the commercial needs of certainty in the banking industry.¹¹⁵ Similarly in *Seven Seas*, the principal should not be prevented from terminating the contract in accordance with the express termination clause. To invalidate the termination of the contract on grounds of a general duty of good faith will compromise the express

¹⁰⁸ See, the Civil codes discussed at Part III above. See also, the Canadian position in *Bhasin* (n 32) [74] in the context of a specific duty to act honestly in contractual performance.

¹⁰⁹ *Contracts Act 1950* (Malaysia) s 40. See generally, *Sinnadurai: Law of Contract* (n 2) ch 12.

¹¹⁰ *Shencourt Sdn Bhd v Aseambankers Malaysia Bhd* [2011] 6 MLJ 236, [300]-[310] (High Court).

¹¹¹ *Civil Law Act 1956* (Malaysia) s 5(1).

¹¹² *Aseambankers* (n 83) [117]-[126] (Abdul Malik Ishak JCA) and [314]-[315], [327] (Mohamad Ariff JCA).

¹¹³ *Ibid* [249].

¹¹⁴ *Ibid*.

¹¹⁵ *Ibid* [329].

termination mechanism agreed between the parties. It will subordinate one's commercial interests to another in the name of good faith. It is against the contractual certainty and freedom of contract (and conversely, to exit contract). It is especially so where parties have in fact formalised their relationship into a written contract to set out their respective contractual rights and obligations.

C *Malaysian approach is satisfactory and pragmatic*

There is no need to recognise a general duty of good faith in contracts. Arguably, the current Malaysian approach in developing the law on duty of good faith on a piecemeal basis is satisfactory and pragmatic. Two reasons are offered here.

First, good faith is already inherent in Malaysian contract law as an underlying contractual attitude. Parties are expected to act honestly in performing the contract. The implication of a good faith duty '[does] no more than express the normal expectation of contracting parties'.¹¹⁶ However, it does not necessarily equate to an actionable implied term of good faith duty. In many instances, the existing contract law principles are self-sufficient. The very recent case of the Malaysian Federal Court in *Lai Fee*¹¹⁷ is of relevance. In affirming the common law position¹¹⁸ that the contracting parties are not expected to arrange their affairs on the basis that other people may commit fraud applies in Malaysia, Vernon Ong FCJ associated it to the application of the Malaysian Contracts Act.¹¹⁹ His Lordship observed that the Malaysian Contracts Act 'starts on the assumption that all contracts are valid' and that contracts must be made by the free consent of the parties.¹²⁰ A contract becomes voidable if the innocent party's consent to the contract was procured by coercion, fraud, misrepresentation or undue influence.¹²¹ It is in the context of these vitiating factors that Vernon Ong FCJ suggested the duty to act in good faith constitutes 'a *sine qua non* in every contract'.¹²² Parties must 'conduct themselves on the expectation of honesty, good faith and fair dealing' and are 'not expected to arrange their affairs on the basis that other people may commit fraud'.¹²³ In the absence of this expectation, there shall be no free consent and there will not be an agreement.¹²⁴ A contract becomes void due to the vitiating factors.¹²⁵ The duty of good faith merely constitutes an underlying

¹¹⁶ Leggatt J, 'Contractual Duties of Good Faith' (Commercial Bar Association Lecture, London, 18 October 2016) [23]. See also, Daniel Markovits, 'Good Faith as Contract's Core Value' in Gregory Klass and others (eds), *Philosophical Foundations of Contract Law* (Oxford University Press, 2014) 293.

¹¹⁷ *Lai Fee v Wong Yu Vee* [2023] 3 MLJ 503 (Federal Court). There, A relied on the representation of a dormant company incorporated by B that the balance purchase price would be paid in the future and agreed to effect immediate transfer of their partnership business. On default of the payment, it was held that the B was *ipso facto* liable to A for fraudulent trading under the Malaysian Companies Act.

¹¹⁸ *Takhar v Gracefield Developments Ltd* [2019] UKSC 13, [44] (Supreme Court).

¹¹⁹ *Lai Fee* (n 117) [57]-[70].

¹²⁰ *Ibid* [58]-[61].

¹²¹ *Ibid* [61]. These vitiating factors are statutorily provided in the *Contracts Act 1950* (Malaysia) ss 14-18.

¹²² *Ibid* [62].

¹²³ *Ibid* [67].

¹²⁴ *Ibid*.

¹²⁵ *Ibid* [66].

attitude of the parties in contracting.¹²⁶ It should not be regarded as an actionable general term of good faith duty in contracts.

Second, it is only when the circumstances of the case require a standard higher than the implicit contractual attitude of good faith, and as a matter of necessity, the courts will imply a term of good faith duty by law and/or in fact into contracts. One may argue that if good faith is already implicit in contract law principles, to imply a specific term of good faith duty is to imply a redundant term in the contract.¹²⁷ Two arguments are offered here. First, the law does not simply imply a duty of good faith in contracts. It will be recalled that in the recognised classes of contract where a duty of good faith is implied by law, a special relationship (fiduciary or otherwise) exists between the parties. It is necessary to imply a duty of good faith to uphold the trust and confidence of the parties' contractual relationship. Similarly, when implying a term in fact, the courts must investigate two questions. First, if an officious bystander were to suggest a term that the contract should be performed in good faith, would the parties without hesitation reply with a common 'Oh, of course!'¹²⁸ Second, is it commercially necessary to give business efficacy to the contract by implying a duty of good faith, without which the contract will lack commercial coherence to achieve its intended contractual purpose? Both questions must be examined through a strict construction of the contract against its contractual background and context. This appears to be the case of *Pasuma*. The exercise of contractual discretion is yet another example. It is trite law that the courts will not rewrite the parties' bargain.

However, there is a risk that a contractual discretion, if left unfettered, will substantially affect the rights of the other party. This arises especially where there is a significant imbalance of power between the parties. In the absence of statutory protection,¹²⁹ the law may fall short of ensuring that the contractual discretion is not abused. While the party may nevertheless exercise its decision-making power in good faith, it is arguably only an unenforceable moral duty but not a legal duty to do so. In this regard, the Malaysian courts have sought to imply a term to exercise the contractual discretion in good faith. Such discretion 'must not be exercised arbitrarily, capriciously or unreasonably'.¹³⁰ However, context is crucial. As Vernon Ong JCA noted in *KAB Corp*, 'context will shape the content of the implied term and the practice of contractual review'.¹³¹ There, it was found that the parties were of significant imbalance of power. The individual office unit owner was compelled to pay an administrative fee to obtain the developer's written consent for a third-party assignment of the office unit. Having regard to the relevant sale and purchase agreement and the House Rules, Vernon Ong JCA

¹²⁶ See also, *CIMB Bank Bhd v Maybank Trustees Bhd* [2014] 3 MLJ 169, [162]-[165] (Federal Court); *Bellajade Sdn Bhd v CME Group Bhd* [2017] 1 MLJ 92, [91]-[94] (Court of Appeal).

¹²⁷ JW Carter and Elisabeth Peden, 'Good Faith in Australian Contract Law' (2003) 19 *Journal of Contract Law* 155, 162-163; Elisabeth Peden, "'Implicit Good Faith' – or Do We Still Need an Implied Term of Good Faith?' (2009) 25 *Journal of Contract Law* 50, 56-59. cf Hugh Collins, 'Implied Terms: The Foundation in Good Faith and Fair Dealing' (2014) 67 *Current Legal Problems* 297, 330-331.

¹²⁸ *Shirlaw v Southern Foundries Ltd* [1939] 2 KB 206, 227 (Court of Appeal).

¹²⁹ The *Consumer Protection Act 1999* (Malaysia) specifically deals with the protection of individual consumers, but not to commercial contracts in general.

¹³⁰ *KAB Corp* (n 102) [29].

¹³¹ *Ibid* [28].

held that the dominant developer's exercise of absolute discretion to impose excessive administrative fee, despite it simply being 'a matter of administrative expediency', was 'plainly arbitrary, unreasonable, unfair and oppressive'.¹³² Second, and more importantly, the contractual implication of a specific term of good faith duty provides an actionable recourse to sue on a contractual breach of the (implied) term. An implicit good faith attitude does not.

Reading the two reasons together, it balances the general rule that there is no general duty of good faith in contracts, and the need to create space for exceptions on a piecemeal basis to achieve justice and contractual fairness. It must be emphasised that a term is implied not because it is reasonable.¹³³ Rather, it is because the court finds that, as a matter of necessity, the parties must have intended to include it as part of the contract.¹³⁴ In line with the freedom of contract and contractual certainty, it does no more than realising the understanding and reasonable expectations of the parties at the time of making the contract.¹³⁵ Where the circumstances of the case require a standard higher than the underlying attitude of good faith, the breach of a specific term of good faith duty, express or implied, constitutes an actionable cause of action. It allows the innocent party to seek appropriate legal redress. This pragmatic approach respects the freedom of contract and contractual certainty which are essential to commerce. It is satisfactory and pragmatic.

D Potential challenge and recommendations

Without derogating from the above, it must be cautioned that the law continues to develop and is in a 'state of flux' in other Commonwealth countries.¹³⁶ As Lord Bingham extra-judicially highlighted the significance of transnationalisation of commercial law,¹³⁷ one must remain vigilant of the legal development of good faith duty in the form of an implied duty in the common law of contract.

The English landmark case of *Yam Seng* indicates that a duty of good faith is likely implied into contracts if the contract is a 'relational' one. There, Leggatt J observed that the parties' agreement in the form of a distributorship contract 'required the parties to communicate effectively and co-operate with each other in its performance'.¹³⁸ The contract was regarded as 'relational' in nature and that a good faith duty imposed on the parties was necessary.¹³⁹ The question then arose as to what precisely is a relational contract? Broadly, Leggatt J described it as a contract which requires 'a high degree of communication, co-operation and predictable performance based on mutual trust and

¹³² Ibid [32].

¹³³ Pek San Tay, 'Interpretation and Implication of Contractual Terms in Malaysia' in Mindy Chen-Wishart and Stefan Vogenauer (eds), *Contents of Contracts and Unfair Terms* (Oxford University Press, 2020) 254.

¹³⁴ *SPM Membrane Switch Sdn Bhd v Kerajaan Negeri Selangor* [2016] 1 MLJ 464, [55] (Federal Court).

¹³⁵ John Wightman, 'Good Faith and Pluralism in the Law of Contract' in Roger Brownsword and others (eds), *Good Faith in Contract: Concept and Context* (Ashgate, 1999) 137.

¹³⁶ See, eg, *Ng Giap Hon* (n 64) [47]-[60].

¹³⁷ Lord Bingham, 'The Law as the Handmaid of Commerce' in Visu Sinnadurai (ed), *The Sultan Azlan Shah Law Lectures: Judges on the Common Law* (Professional Law Books, 2004) 373-375.

¹³⁸ *Yam Seng* (n 45) [143].

¹³⁹ Ibid [142].

confidence' and which involves 'expectations of loyalty'.¹⁴⁰ Assuming a contract is identified as a relational contract, does a duty of good faith constitute a term implied by law or in fact?¹⁴¹ How is it different from the well-established categories of contract where a duty of good faith has already been implied by law based on similar factual matrix of the case? In concluding that a contract is relational, the courts may well have considered the relevant contractual background and context, potentially leading to implication of a term of good faith duty in fact. It is also unclear whether relational contracts mean contracts which are long-term, or which are lacking in detail but solely premised on the trust and confidence between the parties.¹⁴² It will be 'no easy task' to define a category of relational contracts.¹⁴³ The scope and implications of relational contracts in the application of good faith duty remain to be more extensively clarified by the court.

Nevertheless, it must be remembered that context is crucial. Rather than determining whether a contract is relational and therefore a general duty of good faith is implied by default, the court should always resort to the tests of implied terms and examine the relevant facts of the case. A specific and actionable term of good faith duty can be implied only if it is a matter of necessity. It will be recalled that in *Yam Seng*, the vendor was under a specific implied duty of good faith to not knowingly supply misleading market information to the distributor.¹⁴⁴ Leggatt J only arrived at this specific implied duty of good faith after examining the factual matrix of the case that such duty was necessary to be implied to make the contract works.

Alternatively, if the parties intend to govern their contractual relationship by a duty of good faith without resorting to the implied terms, they should expressly stipulate so in the contract.¹⁴⁵ In *Seven Seas*, although the Malaysian Court of Appeal rejected the existence of a general implied term of good faith duty, it nevertheless suggested that the duty of good faith may exist based on the 'expressed intention of the parties which is to be ascertained from the terms of the contract'.¹⁴⁶ To this end, contracting parties may consider to include an express term of good faith duty as follows:

In all matters relating to this agreement, the parties shall act in good faith towards each other. For the purposes of this agreement, good faith means the parties shall cooperate with each other honestly and fairly to do such acts as may be reasonably required to give full effect to the terms and conditions of this agreement.

¹⁴⁰ Ibid [142]. See also, *Bates* (n 50) [725]-[726] and [738].

¹⁴¹ Edwin Peel, *Treitel: The Law of Contract* (Sweet & Maxwell, 15th ed, 2020) [6.076].

¹⁴² Ewan McKendrick, 'Implied Terms' in Hugh Beale (ed), *Chitty on Contracts: General Principles*, vol 1 (Sweet & Maxwell, 34th ed, 2021) fn 149.

¹⁴³ Ewan McKendrick, 'The Regulation of Long-term Contracts in English Law' in Jack Beatson and Daniel Friedmann (eds), *Good Faith and Fault in Contract Law* (Oxford University Press, 1995) 316.

¹⁴⁴ *Yam Seng* (n 45) [141]-[144].

¹⁴⁵ Lady Arden (n 11) 212-213; Paul S Davies, 'The Basis of Contractual Duties of Good Faith' (2019) 1 *Journal of Commonwealth Law* 1, 28. Ewan McKendrick, *Contract Law: Text, Cases, and Materials* (Oxford University Press, 10th ed, 2022) 499.

¹⁴⁶ *Seven Seas* (n 77) [30].

V CONCLUSION

Pragmatism is important in the common law of contract.¹⁴⁷ The doctrine of good faith is a telling example. As a matter of general rule, Malaysia does not recognise a general duty of good faith in contracts. However, the general rule is not absolute. Like the position in England and Singapore, Malaysia has developed the law on a piecemeal basis through contractual implied terms.

It is opined that the Malaysian approach is satisfactory and pragmatic for two reasons. First, it acknowledges that good faith is already inherent in Malaysian contract law. However, it does not necessarily translate into an actionable general duty of good faith. In many instances, the existing contract law principles are self-sufficient. Second, context is crucial. It is only when the tests of implied terms are satisfied to render a duty of good faith necessary and without it the contract will not work, the court will imply a duty of good faith by law and/or in fact into contracts.

However, the introduction of ‘relational’ contracts in *Yam Seng* may pose challenges as to whether a general duty of good faith can be implied into such contracts. It is hoped that the court will clarify the scope and implications of a relational contract vis-à-vis the application of a general duty of good faith in the near future. If the parties intend to impose a duty of good faith, they should expressly stipulate so in the contract. This pragmatic approach does not derogate from the established rules of contract law. It is more likely to respect the intention of the parties than a general overriding duty of good faith. It affirms the importance of the freedom of contract and contractual certainty. At this juncture, one will certainly remember the words of Lord Steyn delivered in a lecture, where his Lordship said:¹⁴⁸

I have no heroic suggestion for the introduction of a general duty of good faith in our contract law. It is not necessary. As long as our courts always respect the reasonable expectations of parties, our contract law can satisfactorily be left to develop in accordance with its own pragmatic traditions. And where in specific contexts duties of good faith are imposed on parties, our legal system can readily accommodate such a well-tried notion.

¹⁴⁷ Lady Hale, ‘Principle and Pragmatism in Developing Private Law’ (Cambridge Freshfields Lecture 2019, Cambridge, 7 March 2019) 13.

¹⁴⁸ Lord Steyn, ‘Contract Law: Fulfilling the Reasonable Expectations of Honest Men’ in Visu Sinnadurai (ed) *The Sultan Azlan Shah Law Lectures: Judges on the Common Law* (Professional Law Books, 2004) 273-274. See also, Justice Steyn, ‘The Role of Good faith and Fair Dealing in Contract Law: A Hair-Shirt Philosophy’ (1991) 6 *Denning Law Journal* 131, 141; Vasanti Selvaratnam, ‘Good Faith: Is English Law Swimming against the International Tide?’ [2020] *Lloyd’s Maritime and Commercial Law Quarterly* 232, 249.