Supreme Court of New South Wales

Alcatel Australia Limited v Scarcella and Ors Matter Nos Ca 40797/97; Ca 40798/97 [1998] NSWSC 483 (16 July 1998)

Last Updated: 9 November 1998

ALCATEL AUSTRALIA LIMITED v SCARCELLA & ORS

CA 40797/97; CA 40798/97; ED 3368/95; ED 2391/97

16 July 1998

Sheller JA, Powell JA, Beazley JA

The Supreme Court of New South Wales Court of Appeal

NATURE OF JURISDICTION: Equity Division - Windeyer J

FILE NO/S: CA 40797/97; CA 40798/97; ED 3368/95; ED 2391/97

DELIVERED: 16 July 1998

HEARING DATE: 24 April 1998

PARTIES: ALCATEL AUSTRALIA LIMITED v SCARCELLA & ORS

JUDGMENT OF: SHELLER, POWELL, BEAZLEY JJA

COUNSEL:

Appellant: S J Motbey

Respondent: V R Gray

SOLICITORS:

Appellant: Quinn & Quinn

Respondent: Henshaws Solicitors

CATCHWORDS: LANDLORD AND TENANT - meaning of "good and substantial repair" in lease CONTRACT LAW - implied duty of good faith

EX TEMPORE/RESERVED: Reserved

ALLOWED/DISMISSED: Dismissed with costs

NO OF PAGES: 41

ALCATEL AUSTRALIA LIMITED v SCARCELLA & ORS

The respondents were the owners of premises known as 276-280 Botany Road, Alexandria (the demised premises) which were leased to the appellant. Two appeals from decisions of the trial Judge concerning provisions of the memorandum of lease of the demised premises were heard together.

The first appeal concerned a referee's report on the true construction of provisions of the lease in which the appellant as lessee covenanted with the respondents as lessors to "well and substantially repair and keep in good and substantial repair" the demised premises. The trial Judge held that good and substantial repair had both a qualitative obligation ("good") and quantitative ("substantial"). The effect of this was that the 28 year old building was not to be made new but in so far as repair could make good or protect against the ravages of time and the elements, it must be undertaken to such a degree as to put the building in the condition it would have been in if good and substantial repair had been undertaken during the period of the lease. On appeal, the appellants submitted that the correct construction of the provision was that it required "substantially good repair".

The second appeal concerned the appellant obligation under the lease to ensure the demised premises complied with any lawful requirements. In particular, its obligations to ensure the demised premises complied with relevant fire safety requirements. The respondents commissioned a report from a fire engineer who reported that the existing internal stairway must be converted into a fire-isolated stairway. The respondents requested that the Council issue a fire safety order to ensure compliance and asked that the fire engineer's report be incorporated into the fire order and required that the appellant carry out the necessary work. The appellant began proceedings against the respondents seeking a declaration that it was entitled to be relieved from its obligation under the lease to ensure the demised premises complied with the fire safety order or, alternatively, that the respondents were bound to indemnify them for any work carried out. The trial Judge dismissed the statement of claim.

On appeal, the appellant claimed that because the respondents had pressured the Council into imposing stricter and unreasonable fire requirements, it was not obliged to comply with the fire order. This flowed from an implied term of good faith or reasonableness in the respondents' performance of their lease obligations which bound them to co-operate in a reasonable way to ensure that the appellant was not subjected to the expense and impact of an unreasonable fire order.

Held:

1. The phrase "good and substantial repair" did not mean "substantially good repair" nor that the building had to be made new. It meant that so far as repair can make good or protect against the ravages of time and the elements, it must be undertaken to such a degree as to put the building in the condition it would have been in if good and substantial repair had been undertaken during the period of the lease. Cases referred to: *Lurcott v Wakely Wheeler* [1911] 1KB 905, *Anstruther-Gough-Calthorpe v McOscar* [1924] 1 KB 716, *Ladbroke Hotels Limited v Sandhu & Singh* (1995) 72 P & CR 498, *Graham v Markets Hotel Pty Limited* [1943] HCA 8; (1943) 67 CLR 567, *Brew Brothers Limited v Snax (Ross) Limited* [1970] 1 QB 612, *Proudfoot v Hart* (1890) 25 QBD 42. *Jeffray v Buckalnd* (1873) 4 AJR 163 distinguished on its facts.

2. In New South Wales a duty of good faith both in performing obligations and exercising rights may by implication be imposed upon parties as part of a contract: *Renard Constructions (ME) Pty Limited v Minister for Public Works* (1992) 26 NSWLR 234, *Hughes Brothers Pty Limited v Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (1993) 31 NSWLR 91. There is no reason why such a duty should not be implied as part of the lease in this case.

3. In a commercial context, it can not be said that a property owner acts unconscionably or in breach of an implied term of good faith in a lease by taking steps to press for more stringent requirements for fire safety if it thinks that the Council requirements were insufficient.

4. It was the duty of the Council to ensure adequate provision of fire safety was made in the demised premises. There was no evidence to suggest that, on the proper application of administrative law, the fire order was so unreasonable that it was bad and therefore unlawful.

5. The appellant was contractually bound to perform the lawful requirements imposed by the Council. Therefore, in the absence of a breach of an implied term of good faith and because the fire order was lawful, the appellant was obliged to comply with the fire order.

Authorities:

Amann Aviation Pty Limited v Commonwealth of Australia [1990] FCA 55; (1990) 22 FCR 527; (1991) 174 CLR 64

Anstruther-Gough-Calthorpe v McOscar [1924] 1 KB 716

Beyfus v Lodge [1925] Ch 350

BP Refinery (Westernport) Pty Limited v Hastings Shire Council (1977) 180 CLR 266

Brew Brothers Limited v Snax (Ross) Limited [1970] 1 QB 612

Byrne v Australian Airlines Limited (1995) 185 CLR 410

Carlish v Salt [1906] 1 Ch 335

Castlemaine Tooheys Limited v Carlton & United Breweries Limited (1987) 10 NSWLR 468

Codelfa Constructions Pty Limited v State Rail Authority of New South Wales [1982] HCA 24; (1982) 149 CLR 337

Commercial Bank of Australia v Amadio [1983] HCA 14; (1983) 151 CLR 447

Distillers Co Biochemicals (Aust) Pty Limited v Ajax Insurance Co Limited [1974] HCA 3; (1974) 130 CLR 1

Dorrough v Bank of Melbourne (1995) (unreported) Federal Court of Australia, Cooper J

Fredrikson v Insurance Corporation of British Columbia (1990) 69 DLR (4^{th}) 431

Gateway Realty v Arton Holdings Limited (No 3) (1991) 106 NSR (2d) 180

Graham v Markets Hotel Pty Limited [1943] HCA 8; (1943) 67 CLR 567

GSA Group Limited v Siebe (unreported) Supreme Court NSW, 24 April 1993 Rogers CJ CommD

Hillas & Co Limited v Acros Limited [1932] UKHL 2; (1932) 38 Com Cas 23

Hospital Products Limited v United States Surgical Corporation & Ors [1984] HCA 64; (1984) 156 CLR 41

Hughes Aircraft Systems International v Airservices Australia [1997] FCA 558; (1997) 146 ALR 1

Hughes Brothers Pty Limited v Trustees of the Roman Catholic Church for the Archdiocese of Sydney (1993) 31 NSWLR 91

In re Scott & Alvarez's Contract [1895] 2 Ch 603

Jeffray v Buckland (1873) 4 AJR 163

Kelly v Cooper [1993] AC 205

Kirke La Schelle Co v Armstrong Co 188 NE 163 (1993)

Ladbroke Hotels Limited v Sandhu & Singh (1995) 72 P & CR 498

Legione v Hately [1983] HCA 11; (1982) 152 CLR 406

Livingstone v Roskilly (1992) 3 NZLR 230

Lurcott v Wakely Wheeler [1911] 1KB 905

Mackay v Dick (1881) 6 App Cas 251

Meehan v Jones [1982] HCA 52; (1982) 149 CLR 571

Minister Trust Limited v Traps Tractors Limited [1954] 1 WLR 963

Perri v Coolangatta Investments Pty Limited [1982] HCA 29; (1982) 149 CLR 537

Peters American Delicacy Co Limited v Heath [1939] HCA 2; (1938) 61 CLR 457

Pierce Bell Sales Pty Limited v Frazer [1973] HCA 13; (1973) 130 CLR 575

Proudfoot v Hart (1890) 25 QBD 42

Renard Constructions (ME) Pty Limited v Minister for Public Works (1992) 26 NSWLR 234

Rogers v Whitaker [1992] HCA 58; (1992) 175 CLR 479

Royal Brunei Airlines Sdn Bhn v Tan [1995] UKPC 4; [1995] 2 AC 378

Secured Income Real Estate (Australia) Limited v St Martins Investments Pty Limited [1979] HCA 51; (1979) 144 CLR 596

Service Station Association Limited v Berg Bennett & Associates Pty Limited [1993] FCA 445; (1993) 45 FCR 84

Sidaway v Governors of Bethlem Royal Hospital [1985] UKHL 1; [1985] AC 871

Stadhard v Lee [1863] EngR 209; [1863] 3 B&S 364; 122 ER 138

Taylor v Johnson [1983] HCA 5; (1983) 151 CLR 422

Walford v Miles [1992] 2 AC 128

Walker v Wimborne [1976] HCA 7; (1976) 137 CLR 1

Wood v Lucy Duff-Gordon 222 NY 88

ORDERS

Both appeals dismissed with costs.

ALCATEL AUSTRALIA LIMITED v SCARCELLA & ORS

JUDGMENT

SHELLER JA:

INTRODUCTION

These are two appeals by Alcatel Australia Limited from decisions of Windeyer J, the first given on 17 September 1997 concerning a referee's report and the second on 12 November 1997 concerning a fire safety order. The respondents are Francesco Scarcella, Helen Scarcella and Rocky Scarcella. Both appeals arise out of the provisions of a memorandum of lease of premises known as 276-280 Botany Road, Alexandria (the demised premises) of which at relevant times the respondents were the owners and lessors and the appellant the lessee. Orders were made that both appeals be heard together.

In 1967 the appellant (then known as Standard Telephone and Cables Pty Limited) became interested in a proposal to build a seven storey administrative building on the demised premises under a sale and lease back arrangement. In accordance with this arrangement, in 1969 Legal and General Assurance Society Limited purchased the demised premises and on 15 December 1969 leased them to the appellant for fifty years. At the time of the lease, the building was newly erected on the demised premises which were within the area of the Sydney City Council, but later of the South Sydney City Council. In July 1989 the respondents purchased Legal and General's interest in the demised premises.

RELEVANT PROVISIONS OF THE LEASE

By the terms of the lease the appellant as the lessee covenanted with the lessor

"2. (c) (i) That the Lessee will during the said term well and substantially repair and keep in good and substantial repair the demised premises and all appurtenances thereto belonging and all additions thereto and the boundary walls and fences thereof and all sewers and drains soil and other pipes and sanitary and water apparatus.

(ii) That the Lessee will paint with two coats of good oil paint in a workmanlike manner all the wood iron and other parts of the demised premises heretofore or usually painted as to the external work in every fifth years and as to the internal work in every seventh years of the said term (the time in each case being computed from the date of the commencement of the said term and in each case the painting to be done in the last year of the term as well) and after every such internal painting to grain varnish distemper wash stop whiten colour or otherwise treat all such parts as have previously been or are usually so dealt with and to repaper the parts usually papered with suitable paper of as good quality as that in use at the commencement of the said term.

.....

(f) To observe and perform all of the lawful requirements of or pursuant to any State Acts, regulations or by-laws and to do and execute or cause to be done and executed such works as under or by virtue of any act or acts of Parliament already or hereafter to be passed now are or shall or may be directed or required by the Government Public Local or any other authority for the district in which the demised premises are situate or any local or public authority to be done or executed upon or in respect of the demised premises or any part thereof whether by the owner, landlord, tenant or occupier thereof and at all times during the term hereby granted to indemnify and keep indemnified the Lessor against all claims and liability in respect thereof.

.....

(o) That the Lessee will not build or permit or suffer to be built or erected any building on the demised premises or make or permit or suffer to be made any additions or alterations of a structural nature to the demised premises except in accordance with plans elevations sections and specifications previously approved by the Lessor's architect or property consultant for the time being PROVIDED FURTHER that such approval shall not be unreasonably withheld."

THE FIRST APPEAL

By summons filed on 28 August 1995 in the Equity Division the appellant claimed declarations, inter alia, as to the true construction of cl 2 (c) (i), cl 2 (c) (ii) and cl 2 (f) of the lease. The summons was later amended but not the claim for these declarations. On 20 August 1996 an order was made pursuant to Pt 72 of the *Supreme Court Rules* referring to:

* the Honourable Denys Needham QC for inquiry and report the matters in the first schedule to the order, namely, the true construction of cl 2 (c) (i) and cl 2 (f) "so far as they impose upon the lessee thereunder any obligation in relation to carry out works in or on or to or connected with the demised premises"; and

* Geoffrey Lumsdaine, an architect, for inquiry and report the matters in the second schedule to the order, namely, having regard to the true construction of cll 2 (c) (i) and 2 (f) which of certain items of work referred to were required to be performed in order to well and substantially repair and keep in good and substantial repair the demised premises and all appurtenances thereto belonging and all additions thereto.

After the death of Mr Needham, The Honourable John Brownie QC was substituted as referee. The schedules were amended to add, inter alia, reference to cl 2 (c) (ii).

MR BROWNIE'S REPORT

On 29 May 1997 Mr Brownie reported and on 9 July 1997 the respondents filed a notice of motion asking the Court to adopt the report subject to certain modifications.

In his report, Mr Brownie referred to the respondents' contention that since at the commencement of the lease the building was new, it was the appellant's obligation to repair every defect as soon as it occurred and upon the termination of the lease to yield up the building in the same condition as it was at the commencement of the lease in an "as new" condition, subject only to the proposition that some parts at least of the building would then be fifty years old, and said:

"However, the lease does not say this. Rather, it obliges the plaintiff to keep the building in `good and substantial repair' and on the expiration or earlier termination of the lease, to deliver it up `in good and substantial repair', and the word `substantial' carries the idea of reasonableness, rather than perfection.

No doubt, at least in respect of some of the items complained about, this raises questions of degree, but it seems clear that the test established by the authorities is whether, in relation to each individual item said to require repair, a reasonably minded owner would carry out that repair work, having full regard to the age of the building, the locality, the class of tenant likely to occupy the building, and the maintenance of the property in such a way that only an average amount of annual work would be necessary in the future: *Anstruther-Gough-Calthorpe* [[1924] 1 KB 716]; and a reasonably minded owner, having regard to these matters, might not consider it appropriate to carry out some of the work demanded by the defendants.

Thus, one of the documents placed before me was a copy of a report by Taylor Lauder Pty Ltd dated 1 November 1995, in which the author said that it was generally accepted that the design life of a building of the type in question was 50 years. Assuming that evidence to this effect is placed before and accepted by Mr Lumsdaine, he might think that this was a relevant consideration, when determining what a reasonably minded owner might consider appropriate, when deciding whether or not to rectify some defect where the continuing existence of that defect constituted a breach of the covenant to repair, and, if so, how to rectify it."

In his judgment on the notice of motion to adopt the report on 17 September 1997, Windeyer J varied the report by deleting the part that I have quoted and substituting the following:

"The lease obliges the plaintiff to keep the building `in good and substantial repair'. What must the plaintiff do to perform this covenant? At the commencement of the lease the building was brand new. What is required to keep a brand new building in good and substantial repair? Time must be taken into account. At 28-year old building is not to be made new. But so far as repair can make good, or protect against the ravages of time and the elements, it must be undertaken. This means that if deterioration of the building is now evident after 28 years but would not have been evident, or evident to such degree, if in earlier years maintenance or repairs which could have been undertaken had been undertaken, then the plaintiff is required to put the building in the condition in which it would have been if the maintenance had been undertaken in the earlier years. This may entail renewing subsidiary parts of the building (though not renewal of the whole building)."

On 15 December 1997 the appellant was granted leave to appeal from this decision. In its notice of appeal the appellant raised a number of grounds, but in substance sought an order that Mr Brownie's report be adopted without amendment.

GROUNDS OF APPEAL

Windeyer J regarded the covenant to keep in good and substantial repair as a double covenant having both a qualitative obligation ("good") and a quantitative ("substantial"). His Honour found support for this conclusion in *Lurcott v Wakely & Wheeler* [1911] 1 KB 905, particularly in the judgment of Fletcher Moulton LJ at 915. The covenant there under consideration was a little different; "well and substantially repair ..... and keep in thorough repair and good condition." Fletcher Moulton LJ at 915-6 said:

"I therefore look upon these as three separate covenants: there is a covenant to repair, there is a covenant to keep in thorough repair, and there is a covenant to keep in good condition."

In *Anstruther-Gough-Calthorpe v McOscar* [1924] 1 KB 716 at 731-2 Atkin LJ referred to Fletcher Moulton LJ's judgment and said that effect should be given, if possible, to every word used by the parties. Windeyer J said that it followed that a covenant to "keep in good and substantial repair" imposed greater obligations upon the covenantor than a covenant to keep in "good tenantable repair" and quoted the following passage from Atkin LJ's judgment in *Anstruther's* case at 734:

"Repair ..... connotes the idea of making good damage so as to leave the subject so far as possible as though it had not been damaged. It involves renewal of subsidiary parts; it does not involve renewal of the whole. Time must be taken into account; an old article is not to be made new; but so far as repair can make good, or protect against the ravages of time and the elements, it must be undertaken."

Windeyer J continued:

"By contrast, a covenant to `keep in good and substantial repair' suggests a higher standard of maintenance is required such that the condition of the premises is both good and substantially sound. I do not, however, accept the contention that such a construction requires the lessee to put the building into `mint condition'. It merely obliges the covenantor to effect such repairs as a reasonably minded owner would effect in accordance with his or her obligations as formulated by Atkin LJ in *Anstruther's* case."

His Honour then referred to a passage in the judgment of Robert Walker J in *Ladbroke Hotels Limited v Sandhu & Singh* (1995) 72 P & CR 498 at 504:

"If a tenant disregards his repairing obligations and, as a result, the premises become rundown and commercially unattractive, it hardly lies in the tenant's mouth to rely on that fact as lowering the standard of repair required under the tenant's repairing covenant."

His Honour also referred to a passage in the judgment of Starke J in *Graham v Markets Hotel Pty Limited* [1943] HCA 8; (1943) 67 CLR 567 at 585. In that case at 579, Latham CJ cited *Lurcott v Wakely & Wheeler* with approval. At 585 Starke J said:

"The state of repair required by a covenant to yield and deliver up premises well and substantially repaired depends primarily upon the words used. It involves, in the present case, an obligation to yield and deliver up the premises in such a state of repair as that in which they would be found if managed by a reasonably minded owner having regard to their age, their character, their ordinary use and the requirements of the tenants likely to take them at the time of the demise or sub-letting (*Lurcott v Wakely & Wheeler; Anstruther-Gough-Calthorpe v McOscar*). Atkin LJ, as he then was, said in the latter case that such a covenant connotes the idea of making good damage so as to leave the subject matter as far as possible as though it had not been damaged. It involves renewal of subsidiary parts: it does not involve renewal of the whole."

In *Brew Bros Limited v Snax (Ross) Limited* [1970] 1 QB 612 at 640 Sachs LJ said:

"It seems to me that the correct approach is to look at the particular building, to look at the state which it is in *at the date of the lease*, to look at the precise terms of the lease, and then come to a conclusion whether, on a fair interpretation of those terms in relation to that state, the requisite work can fairly be termed repair."

Having quoted this passage Windeyer J said that the relation of the obligation to the time of the demise was of real significance:

"Thus I cannot accept the plaintiff's contention that Mr Brownie's statement of the law along the lines of the statement of Lopes LJ in *Proudfoot v Hart* (1890) 25 QBD 42 correctly states the law in the absence of reference back to the date of commencement of the term."

In *Proudfoot v Hart* at 55 Lopes LJ had said:

"What is the meaning of `good tenantable repair'? That expression appears to me to mean such repair as, having regard to the age, character, and locality of the house, would make it reasonably fit for the occupation of a reasonably minded tenant of the class who would be likely to take it. ..... What is the obligation of the tenant under such a contract? First, he must, if the premises are out of repair when he takes them, put them into good tenantable repair."

Windeyer J continued:

"Nor can I accept the contention that the Court in *Anstruther's* case simply applied the principles articulated in *Proudfoot v Hart* without temporal connection. All three members of the English Court of Appeal in *Anstruther's* case specifically distinguished the facts before the Court in *Proudfoot v Hart* from those with which they were concerned. The relevant passage from the judgment of Scrutton LJ appears at 730:

`In *Proudfoot v Hart* the lease was for three years only, and the covenant was to keep in good tenantable repair. There was no suggestion of any change in character of the house or its probable tenants between the beginning and the end of the term. Lopes LJ framed a definition which Lord Esher adopted as follows: `Such repair, as having regard to the age, character, and locality of the house, would make it reasonably fit for occupation of a reasonably-minded tenant of the class who would be likely to take it.' I do not think there was any intention of suggesting that a deterioration in the class of tenants would lower the standard of repairs...Therefore in my view we are bound to look to the character of the house and its ordinary uses at the time of the demise.'

See also Bankes LJ at 726-8 and Atkin LJ at 733. *Anstruther's* case establishes the general proposition that the standard of repair required by a repairing covenant is to be determined by the parties' expectations at the time the lease is granted. Further, good and substantial repair is not necessarily to be equated with good tenantable repair. The former sets a higher standard than the latter."

The appellant's argument was that:

(i) the phrase "good and substantial repair" was a true hendiadys, that is, the expression of a compound notion by treating its two constituents as though they were independent and connecting them with a conjunction instead of subordinating one to the other (see Fowler, Dictionary of Modern English Usage); or, alternatively,

(ii) was a simple common legal use of near synonyms or associated ideas to express an idea, which Fowler calls "Siamese twins".

Thus, it was submitted that the phrase meant "substantially good repair". However, I think the weight of authority is against this contention particularly in so far as it ignores the fact that, in the present case, the lease was of a newly erected building. In the paragraph he substituted in the report, Windeyer J acknowledged that the twenty-eight year old building was not to be made new but went on to say that so far as repair can make good or protect against the ravages of time and the elements, it must be undertaken to such a degree as to put the building in the condition it would have been in if good and substantial repair had been undertaken during the period of the lease. I agree.

The appellant called in aid the decision of the Full Victorian Supreme Court in *Jeffray v Buckland* (1873) 4 AJR 163 on an application to reduce a jury's award of damages for breach of a covenant in a lease which required the defendant to keep the premises in repair. The jury did not allow for wear and tear. The Court held that the covenant in the lease only required the defendant to keep the premises in substantial repair and that an allowance should be made for wear and tear. But the language of the covenant was significantly different and, accordingly, the decision of no present assistance.

Finally, the appellant said that it should not be barred from raising an alternative case, on the facts, that some, if not all, of the defects pre-dated the respondents' purchase of the reversion and in some way would have enabled the respondents to rely on waiver of any breaches. This does not seem to have been raised before Windeyer J and it is not open to be raised on this appeal.

The first appeal should be dismissed with costs.

THE SECOND APPEAL

The building on the demised premises contained two staircases, one on the south western corner which was fire proofed and an open staircase further to the east on the southern wall which was not fire proofed. The respondents commissioned a report from a "fire engineer", Mr McMonnies, which was dated 24 May 1994 and, when received, was sent both to the appellant and to the South Sydney City Council. In his report, Mr McMonnies said that the existing internal stairway was non-fire-isolated and must be converted into a fire-isolated stairway.

For the purpose of ensuring that adequate provision for fire safety is made in or in connection with a building, s317D of the *Local Government Act 1919* empowered the Council, by notice in writing, to order the owner to carry out, within the period specified in the notice, such work as might be so specified.

On 8 July 1994 the respondents wrote to the Council asking for a fire safety inspection. On 10 August 1994 the Council general manager wrote to the respondents advising that a Council officer had inspected the premises and they were found not to comply with the building regulations. The letter continued:

"However, given that the building is existing, an adequate fire safety level will be achieved if the works listed in the attached schedule are carried out."

The list contained twenty-four items, the first of which was that the existing stairway located on the eastern side of the building should be enclosed for its full height with construction having a fire resistance level of at least -/120/120 to serve all levels of the building and discharging directly to open space.

On 20 October 1994 the appellant wrote saying it accepted responsibility for the requirements of Ordinance 70, which governed the construction and maintenance of buildings, but at that time it was as least likely that it was unaware that the respondents had initiated action on fire safety requirements. The appellant did not immediately

carry out the listed work. On 31 July 1995 the respondents gave the appellant a notice of default claiming that the Council requirements had not been carried out as required by cl 2 (f) of the lease. On 14 August 1996 the solicitors for the respondents wrote to the Council referring to the contents of its letter of 10 August 1994 and said:

"It has been over 2 years since the letter was first issued and we confirm that Alcatel has not yet complied with your Schedule of Works as required under the lease.

Our clients have raised serious concerns over the property in its ability of being a fire trap having regard to the recent history of the `Backpacker's Fire'.

Out clients request Council provide a current status report and take urgent mandatory action in having the building comply with fire regulation."

By letter of 23 September 1996, the building services manager of the Council wrote to the respondents enclosing a copy of a proposed order the Council intended to issue under s124 of the *Local Government Act 1993*. Representations to Council were invited from the respondents. On 3 October 1996 the respondents' solicitors sent a facsimile enclosing the report of 24 May 1994 stating it wished to have it incorporated in the order. On 26 November 1996 the Council sent a fire safety order to the respondents. The respondents required that the appellant carry out the work necessary to comply with this fire safety order. The Council order incorporated requirements for some work not included in its draft order. The order as issued stated that the parties affected could appeal. That information was incorrect. By that time the *Local Government Amendment Act 1996* had come into effect and operated to limited that type of appeal to owners.

On 19 December 1996 the appellant filed an appeal with the Land and Environment Court and on 24 December 1996 sent a copy of its application to the respondents. The first return date in the Land and Environment Court was 24 January 1997 when the matter was adjourned until 19 February. On 19 February 1997 the appellant's application to stand over the proceedings was resisted both by the respondents and the Council and refused and the matter fixed for hearing on 20 and 21 April 1997. The appellant was ordered to provide particulars of the items in the order to which it objected. This it failed to do. The appellant filed a notice of motion seeking an adjournment. The respondents filed a notice of motion seeking to be joined or to have leave to appear. The Council filed a notice of motion seeking to have the application of the appellant struck out. All these matters were listed for hearing on 17 April 1997 when the Chief Judge of the Land and Environment Court struck out the appellant's application, presumably on the ground that it had no standing.

On 29 April 1997 the appellant wrote to the respondents' solicitors seeking authority to bring an appeal in the name of the respondents. The reply dated 30 April 1997 questioned the basis for the assertion of the right to appeal in the name of the owners and asked what work had been done and what work was questioned. Finally, the solicitors stated the appeal did not operate as a stay and that the respondents required the work to be done in any event.

On 13 April 1997 the appellant began proceedings against the respondents by statement of claim seeking, inter alia, a declaration that it was entitled to be and had been relieved from having to perform its contract of indemnity relating to the fire safety order or, alternatively, that the respondents were bound to indemnify it against its liability to indemnity them.

The hearing before Windeyer J began on 17 September 1997. Part of the evidence consisted of an affidavit of Mr McMonnies sworn on 15 August 1997. Mr Motbey, who appeared for the appellant, indicated to Windeyer J that he had only been informed at 4.45pm the previous day that the respondents proposed to tender the evidence of Mr McMonnies, and that he had omitted to inform Mr Gray, who appeared for the respondents, that Mr McMonnies would be required for cross-examination. He had informed Mr Gray that morning that if he did propose to lead evidence from Mr McMonnies he would wish to cross-examine him. When the respondents came to give evidence they tendered the affidavit of Mr McMonnies annexing his report, which was admitted. His Honour was not prepared to give leave to read the affidavit but said he would revisit the matter on the next day.

On the following day, Mr Motbey informed Windeyer J that there were a couple of serious questions he wished to take up with Mr McMonnies in regard to "the balance of the material received" and requested leave to issue a subpoena addressed to Mr McMonnies for 2pm that day. Windeyer J stated he was the defendant's witness and his

report was in evidence. He said the only question was whether he allowed paras 5, 6 and 7 of his affidavit to be read without his being present for cross-examination. The first four paragraphs of the affidavit were formal matters leading up to the annexure of the report of 24 May 1994 in para 4. His Honour allowed the affidavit to be read. The paragraphs objected to went to two matters; first, a comparison between his report and the requirements of the Council fire safety order and second, a statement that at no time between 24 May 1994 and the date of the affidavit did he have any communication with any officer of the South Sydney City Council in relation to his report or the extent to which the building failed the comply with the fire safety requirements of the Building Code of Australia or the action which would be required to make that building comply with those requirements.

During the course of the hearing on 17 September 1997, Windeyer J asked Mr Gray, who was appearing for the respondents, to relay to his clients his Honour's suggestion that the 1997 proceedings be resolved on terms that would see the appellant, the Council and the respondents all agreeing to enliven the proceedings in the Land and Environment Court. This led to the filing of a notice of motion by the appellant for, inter alia, an order authorising the appellant to apply to the Land and Environment Court for an order that the name of the appellant as applicant be substituted for the names of the respondents as applicants in the 1996 application on terms. Further consequential orders were sought. This notice of motion came before Windeyer J on 26 September. His Honour ordered it to be amended. The amended form sought an order granting the appellant leave to file an amended statement of claim. In this proposed amended statement of claim, the appellant said that, as the contract of indemnity obliged it to comply only with lawful requirements or orders of local authorities and as the only means of determining whether purported requirements or orders were in truth lawful was by means of an appeal to the Land and Environment Court, it was an implied condition of the contract of indemnity that the respondents would co-operate with the appellant so as to facilitate the bringing of appeal proceedings in the respondents' names to test whether the order or requirement was in truth lawful. It was claimed that the respondents had failed and refused so to co-operate and had deliberately prevented the bringing of an appeal.

On 17 October 1997 the respondents' solicitors wrote to Windeyer J's Associate enclosing a letter dated 29 September 1997 from South Sydney City Council, in which the area building manager referred to the fire safety order, advised that the date due for completion had passed and threatened to take all legal steps available to ensure compliance. By letter of 21 October 1997 the Associate wrote to the solicitors stating that the Judge had directed that the material be returned to them and continued:

"The proceedings before the Court are to be decided upon evidence given in Court. What was intended to be done as a result of the transmission is quite unclear, but his Honour has read the letter and he has directed that you be requested to send a copy of it to the plaintiff's solicitors."

This direction appears not to have been complied with.

On 3 November 1997 Pike, Pike and Fenwick, solicitors, wrote to the Judge's Associate informing him that they acted for South Sydney City Council. They said they took "this slightly unusual step of writing" because of separate allegations made to them by the solicitors for both parties in the proceedings and, amongst other things, that it would be unlikely that the Council would consent to the proceedings in the Land and Environment Court being reopened. By the time the writer, Adrian M Hawkes, reached the penultimate paragraph of his letter, he referred to "the highly unorthodox step of writing directly" to the Judge.

On 12 November 1997 the notice of motion came before Windeyer J, before his Honour delivered judgment in the proceedings. Mr Motbey, who appeared for Alcatel, referred to the letter of 3 November 1997 and expressed concern about it and the suggestion in it that the parties' representatives had been highly critical of the Council actions in issuing the fire notice. Mr Hawkes was in Court and withdrew that assertion. Mr Hawkes claimed that he believed that a letter from the solicitor for the respondents indicated that the Judge was awaiting Council's decision as to re-opening the Land and Environment Court proceedings before coming to a determination in the matter. A Judge disabused him of that notion. His Honour dismissed the notice of motion and gave this reason:

".....prior to the application being made and because of the way this matter had proceeded, I had already come to the conclusion that the right of subrogation claimed and the claim for an implied term should not succeed. In those circumstances, in accordance with the normal practice in these matters, if an amendment would be futile, then

the Court should not allow it to be made and as will be seen from what I have just said, such amendment would be futile."

The notice of motion was dismissed with costs. In his judgment delivered on the same day, Windeyer J dismissed the statement of claim.

REASONS FOR JUDGMENT

At the trial the appellant advanced a number of arguments on the basis of which it claimed to avoid compliance with or the affects of cl 2 (f) of the lease based on the respondents' conduct in pressing the Council to issue a fire order and failing to appeal against the fire order or support the appellant in such appeal. In his judgment Windeyer J referred to a conspiracy claim by the appellant which was not pressed. His Honour said that if pressed it would have failed.

"It was not established that the dominant purpose of the conduct complained of was to harm the plaintiff; in fact in my opinion it is more likely that its purpose was to enhance the value of the defendant's asset, albeit that might have been triggered during a dispute about other lease matters; see *McKernan v Fraser* [1931] HCA 54; (1931) 46 CLR 343."

Of an argument based on the insurance analogy that there was an implied term not to cause the event insured against, his Honour said:

"It is true that there is an implied term of a contract of insurance that the insured will not cause the event giving rise to the loss against which he is entitled to be indemnified by his insurer. A person whose life is insured under a life insurance policy cannot, if owner of the policy, take his own life and thereby give rise to a claim under the policy by his estate. A boat owner can insure the boat and burn the boat, but if he does so he cannot seek indemnity from his indemnity insurer: *Beresford v Royal Insurance Company Limited* [1938] AC 586 at 595. That principle, however, does not apply to the facts in this case. There is obviously no valid reason for causing the destruction of the property insured or for taking one's life if insured and it is clear enough that a term should be implied that in such cases there is no right to recover under the policy. It is quite possible that there could be a valid reason for seeking advice of the relevant authority on fire protection matters and perhaps even in sooling Council on if the person contractually responsible for the work does not attend to it. The implied condition claimed is not made out in such a case. It is not necessary for that implication to arise. Whether or not there is an implied condition of fair dealing is a separate matter."

Dealing with a claim to relief on the ground of unconscionable conduct by the respondents, his Honour said the claim, if it could lead to any relief, was not made out.

"Relationships between landlord and tenant are not always harmonious; their rights and obligations are determined by the contract. There can be no complaint if one party insists on the fulfilment by the other of the contractual obligations of that other. Unconscionable conduct claims cannot be waved around as an answer to onerous contractual obligations. Either the owners were acting in accordance with their rights or they were not."

Dealing with the claim to be entitled to be subrogated, his Honour said:

"In clause 2 (f) there is first an obligation to comply with the order and second an obligation to indemnify the owner against liability in respect of that order. That liability would arise either if the landlords themselves carried out the work on failure of the tenants to do so or if Council carried out the work and sought to recover the cost from the landlords. The question must be considered without regard to the actions of the landlords in bringing about the liability which falls upon the tenant under the lease. It could not be said, I think, that the tenant should, in the name of the landlord, be entitled to resist all the demands of that order whether reasonable or not, nor to take some technical objection which might cause the notice to be set aside. Insurers under liability policies defend actions for damages brought by those parties against the insured person pursuant to rights given under the policy and not pursuant to rights of subrogation. Liability to comply with the requirements of a properly given notice is entirely different from liability to indemnify another against some loss. This is not a question of loss, but a question of responsibility or the extent of the responsibility. Expenditure of

money is not necessarily a loss. Leaving aside the question of an implied term no right of subrogation arises in this case under the general equitable principles. No reading of the main passages in *Castellain v Preston* (1883) 11 QBD 380 at 388 and 404 nor the decision in *Napier v Hunter* [1993] AC 713 suggests otherwise."

Finally, his Honour dealt with the question of whether there was an implied term of co-operation and said:

"The term or condition said to be implied is that `the defendants would co-operate with the plaintiff so as to facilitate the bringing of appeal proceedings in the name of the defendants to test whether the order as set out was lawful.' This is really a claim for an implication of a term of fair dealing. In relation to the general law of terms to be implied in fact it is not a term which is necessary for the effective operation of a contract; nor does it go without saying; *BP Refinery (Westernport) Pty Limited v Hastings Shire Council* (1977) 180 CLR 266; *Renard Constructions (ME) Pty Limited v Minister for Public Works* (1992) 26 NSWLR 234 at 256. It would be difficult to imply the existence of a term that if a right of appeal given to a tenant by statute is removed by statute then that right should be reinstated in some other way. On its face clause 2 (f) is quite clear. Is then, this term implied by law? That presupposes that the question of whether orders are lawful or not can only be ascertained by bringing about appeal proceedings. That cannot be correct. An order of that nature is lawful unless it is set aside."

Windeyer J concluded by saying that he had found the matter a difficult one.

"A tenant should not be left at the mercy of the landlord acting in a capricious manner calculated to bring about a result which would not otherwise arise. No Council is likely to resist a request for an all embracing fire safety order. Thus while I do not think that one can find an implied term as pleaded it is possible that, if on a claim for indemnity the tenant could prove that some of the requirements of the order were such that on an appeal they would have been held unreasonable and the order varied, then to that extent the claim for indemnity might fail if the landlord had refused to co-operate in allowing an appeal which was shown to have reasonable prospects of success to be brought in its name with proper protection on costs. That might amount to relevant unconscionable conduct. The point however is that the relief sought in this action would not be available. What it means is that the tenant might be able to resist the making of a mandatory order in the nature of an order for specific performance of the particular contractual term in question and to the extent to which there was a claim for damages might be able to resist part of the claim for damages. On no basis could this give rise to a present declaration that the plaintiff was entitled to be relieved of having to perform its contract of indemnity. It is important to understand there is no evidence that any part of the required work is unreasonably required."

His Honour dismissed the statement of claim. The appellant appeals from that dismissal.

GROUNDS OF APPEAL

On the hearing of the appeal the appellant relied on the following grounds in its supplementary notice of appeal:

"5. His Honour ought to have granted leave to amend on 12 November 1997.

6. His Honour erred in holding that there was no implied term which restrained the Respondents from `sooling' the Local Council onto the Appellant in order to have the Appellant, at its expense, do work improving their building.

7. His Honour erred in holding that, by unconscionable conduct, the Respondents could not lose the right to enforce contractual promises given to them by the Appellant.

8. His Honour ought to have found that the Respondents had engaged in unconscionable conduct which deprived them of the right to enforce the Appellant's promise in relation to the current fire order.

9. His Honour erred in holding that the Appellant could not be subrogated into the Respondents' rights of appeal.

10. His Honour erred in holding that there was not an implied term which authorised the Appellant, in the events which had occurred, to appeal the fire order in the names of the Respondents.

10. [sic] His Honour erred in finding that the Appellant had not established that it had a good arguable appeal (from the fire order) on the merits.

11. His Honour erred in holding that although the Appellant may well have grounds in equity to resist a claim against it by the Respondents (for indemnity in relation to the fire order) it could not take up the initiative as Plaintiff and, relying on those same grounds, obtain relief in equity from the Respondents' demand (out of court) for indemnity.

12. His Honour erred in failing to notice and determine the Appellant's submission from the implication of the term set forth in paragraph 12 of its written submissions handed up to His Honour on 18 September 1997."

Paragraph 12 in the written submission was as follows:

"The clause should be read as if it contained a commitment by the landlord to the effect that in the event an order issues in relation to the building or any part thereof at a time when, under the then relevant legislation, any right of appeal or review in relation to the order might be vested in the landlord alone, the landlord would not unreasonably withhold its consent to the use of its name thereby enabling the tenant to exercise the right of appeal."

IMPLIED TERMS

In summary terms, the appellant claimed that because the respondents had pressured the Council into imposing stricter and unreasonable fire requirements, it was not obliged to comply with covenant 2 (f) of the lease. This result flowed from an implied term of good faith or reasonableness in the respondents' performance of their lease obligations or exercise of their lease rights which bound them to co-operate in a reasonable way to ensure that the appellant was not subjected to the expense and impact of an unreasonable fire order.

The appellant relied upon the reasons for judgment of Priestley JA in *Renard Constructions (ME) Pty Limited v Minister for Public Works* (1992) 26 NSWLR 234 at 255 and following and of Finn J in *Hughes Aircraft Systems International v Airservices Australia* [1997] FCA 558; (1997) 146 ALR 1 at 36 and following. In *Renard Constructions*, a clause in a building contract empowered the principal to take over the whole or any part of the work or to cancel the contract if the contractor neglected to comply with any direction given by the principal, however minor, accidental or temporary that neglect might be, and regardless of the importance or otherwise of the subject matter. Priestley and Handley JJA held that the power so conferred on the principal must be exercised reasonably. Priestley JA at 255-6 used the terms "implication in fact" and "implication by law". His Honour said that the so-called implication in fact is really implication by the Judge based on the Judge's view of the actual intention of the parties drawn from the surrounding circumstances of the particular contract, its language and its purposes, as they emerge from the language and in the circumstances or, as it has been called, implication ad hoc. The rules governing such implication are found in *BP Refinery (Westernport) Pty Limited v Hastings Shire Council*, *Secured Income Real Estate (Australia) Limited v St Martins Investments Pty Limited* [1979] HCA 51; (1979) 144 CLR 596 and *Codelfa Construction Pty Limited v State Rail Authority of New South Wales* [1982] HCA 24; (1982) 149 CLR 337. Priestley JA said at 256:

"Those rules are that the implied term must be reasonable and equitable; necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; so obvious that `it goes without saying'; capable of clear expression; and must not contradict any express term of the contract; see *United States Surgical Corporation v Hospital Products International Pty Limited* [1983] 2 NSWLR 157 at 196, and in the same case on appeal, *Hospital Products International Pty Limited v United States Surgical Corporation* [1984] HCA 64; (1984) 156 CLR 41 at 66 per Gibbs CJ."

Implication by law is based on imputed intention as opposed to actual intention, and implies a term as a legal incident of a particular class of contract; *Castlemaine Tooheys Limited v Carlton & United Breweries Limited* (1987) 10 NSWLR 468 at 486-490 per Hope JA, with whom Samuels and Priestley JJA agreed. In *Renard Constructions*, Priestley JA at 263 implied "reasonableness in performance" in the exercise of the contractual power to take over or cancel the contract. His Honour said at 263-4:

"The kind of reasonableness I have been discussing seems to me to have much in common with the notions of good faith which are regarded in many of the civil law systems of Europe and in all States in the United States as necessarily implied in many kinds of contract. Although this implication has not yet been accepted to the same extent in Australia as part of judge made Australian contract law, there are many indications that the time may be fast approaching when the idea, long recognised as implicit in many of the orthodox techniques of solving contractual disputes, will gain explicit recognition in the same way it has in Europe and the United States."

Section 1-203 of the *United States Uniform Commercial Code* provides:

"Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement."

Section 1-201 (19) defines "good faith" as "honesty in fact in the conduct or transaction concerned". Section 2-103 (1) (b) defines "good faith", in the case of a merchant, as "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." Section 205 of the Restatement of Contracts, 2nd, provides:

"Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement."

Priestley JA referred to the published lecture of Steyn J, The Role of Good Faith and Fair Dealing in Contract Law: A Hair-Shirt Philosophy? (1991) Denning Law Journal 131.

Handley JA at 279-80 said that he agreed generally with "much of what Priestley JA has written" on the issue and pointed to three other matters which supported the existence of some restraint on the exercise of power apart from the normal requirement of honesty; the contractor's opportunity to show cause, the necessary satisfaction of the principal and the comprehensive provision for arbitration. His Honour cited *Hillas & Co Limited v Arcos Limited* [1932] UKHL 2; (1932) 38 Com Cas 23 at 43-44 where Lord Wright referred to "..... the legal implication in contracts of what is reasonable, which runs throughout the whole of modern English law in relation to business contracts" and *Minster Trust Limited v Traps Tractors Limited* [1954] 1 WLR 963 at 973 where Devlin J said:

"..... there may be a question (again depending upon the implication to be drawn from the contract) whether the dissatisfaction must be reasonable, or whether it can be capricious or unreasonable so long as it is conceived in good faith ..... The tendency in modern cases seems to be to require the dissatisfaction to be reasonable."

His Honour also referred to *Stadhard v Lee* [1863] EngR 209; [1863] 3 B & S 364; 122 ER 138 at 371-2; 141 and *Amann Aviation Pty Limited v Commonwealth of Australia* [1990] FCA 55; (1990) 22 FCR 527 at 532, 542-4 and in the High Court, now [1991] HCA 54; (1991) 174 CLR 64. In *Hughes Bros Pty Limited v Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (1993) 31 NSWLR 91 Kirby P and Priestley JA applied *Renard Constructions*. Kirby P said at 93 that he was bound by the decision.

In *Hughes Aircraft*, Finn J at 36 referred to the judgment of Gummow J in *Service Station Association Limited v Berg Bennett & Associates Pty Limited* [1993] FCA 445; (1993) 45 FCR 84 at 96 where his Honour, after considering the acceptance by North American jurisprudence of an implied duty of good faith and fair dealing, observed:

"Anglo Australian contract law as to the implication of terms is heretofore developed differently, with greater emphasis upon specifics, rather than the identification of a genus expressed in wide terms. Equity has intervened in matters of contractual formation by remedy of rescission, upon the grounds mentioned earlier. It has restrained freedom of contract by inventing and protecting the equity of redemption, and by relieving against forfeiture and penalties. To some extent equity has regulated the quality of contractual performance by the various defences available to suits for specific performance and for injunctive relief. In some, but not all, of this, notions of good conscience play a part. But it requires a leap of faith to translate these well established doctrines and remedies into a new term as to the quality of contractual performance, implied by law."

Finn J was prepared to take that leap encouraged by the reasoning of Priestley JA. At 37 his Honour said:

"Fair dealing is a major (if not openly articulated) organising idea in Australian law. It is unnecessary to enlarge upon that here. More germane to the present question, the implied duty is, as is well known, an accepted idea in the contract law of the United States and, probably of Canada: see E A Farnsworth, `Good Faith in Contract Performance'. In J Beatson & D Friedmann (eds), `Good Faith and Fault in Contract Law', Clarendon Press, Oxford, 1995; for a convenient collection of some of the voluminous literature in the United States debating the meaning of the implied duty, see Farnsworth on Contracts, Vol 2, Little, Brown & Co, Boston 1990, para 7.17 (a); for an English view see eg Right Hon Lord Justice Staughton, `Good Faith and Fairness in Commercial Contract Law' (1994) 7 Jo Contract Law 193; and see *Livingstone v Roskilly* (1992) 3 NZLR 230 at 237-8. Its status in civil law is well recognised: see eg H K Lucke, `Good Faith and Contractual Performance' in P D Finn (ed) `Essays on Contract', Law Book Company, Sydney 1987; J F O'Connor `Good Faith in English Law', Dartmouth, 1990, Ch 8. It has been propounded as a fundamental principle to be honoured in international commercial contracts: see eg Unidroit, `Principles of International Commercial Contracts', International Institute for the Unification of Private Law, Rome 1994, Art 1.7. Its more open recognition in our contract law is now warranted: compare Sir Anthony Mason, `Contract and its Relationship with Equitable Standards and the Doctrine of Good Faith', The Cambridge Lectures, 1993 (8 July 1993); notwithstanding the significant adjustments this would occasion to some of the contract laws apparent orthodoxies: see eg Lucke above pp 177 and following.

I should add that, unlike Gummow J, I consider a virtue of the implied duty to be that it expresses in a generalisation of universal application, the standard of conduct to which all contracting parties are to be expected to adhere throughout the lives of their contracts. It may well be that, on analysis, that standard would be found to advance little the standard that presently may be exacted from contracted parties by other means: compare the standard applied in *Conoco v Inman Oil Co* 774 F 2d 895 (1985) at 908. But setting the appropriate standard of fair dealing is, in my view, another matter altogether from acceptance of the duty itself."

With great respect, there is much to be said for a generalisation of universal application, an ideal which the High Court has pursued and sometimes achieved in other areas of the law, such as the reach of the duty of care in the law of negligence and the principles of estoppel. But equally the determination of the appropriate standard of fair dealing in the particular contractual context is difficult, though probably no more difficult than identifying general standards set by such legislation as the *Trade Practices Act 1975* (misleading and deceptive conduct and unconscionable conduct) and the *Contracts Review Act 1980* (unjust and hence, unconscionable, contracts).

Finn J went on to deal with the question whether in that case the type of contract or the relationship of the parties or both might require the implication as a matter of law. In this part of his reasons for judgment his Honour touched, at 38, upon the requirement of "necessity" explained by McHugh and Gummow JJ in *Byrne v Australian Airlines Limited* (1995) 185 CLR 410 at 450:

"Many of the terms now said to be implied by law in various categories of case reflect the concern of the courts that, unless such a term be implied, the enjoyment of the rights conferred by the contract would or could be rendered nugatory, worthless, or, perhaps, be seriously undermined. Hence, the reference in the decisions to `necessity' ..... This notion of `necessity' has been crucial in the modern cases in which the courts have implied for the first time a new term as a matter of law."

In *Gateway Realty Limited v Arton Holdings Limited (No 3)* (1991) 106 NSR (2d) 180 Kelly J at 192 held in apparently general terms that contracting parties are obliged to exercise their rights under an agreement honestly, fairly and in good faith. "In most cases, bad faith can be said to occur when one party, without reasonable justification, acts in relation to the contracts in a manner where the result would be to substantially nullify the bargained objective or benefit contracted for by the other, or to cause significant harm to the other, contrary to the original purpose and expectation of the parties"; 197.

In *Livingstone v Roskilly* (1992) 3 NZLR 230 at 237 Thomas J stated that, in general, the concept that "the parties to a contract must act in good faith in making and carrying out the contract" is part of the law of New Zealand. In his 1993 Cambridge Lecture, to which Finn J referred, Sir Anthony Mason commented that this may be going too far and doubted that the House of Lords would endorse it; see *Walford v Miles* [1992] 2 AC 128 at 136-8.

On the other hand, in *Dorrough v Bank of Melbourne* (1995) (unreported) Federal Court of Australia, 27 September 1995, Cooper J said, that in the light of a number of authorities to which he referred:

"..... it is not open to this Court to hold that a contract of insurance (except by virtue of the provisions of s13 of the *Insurance Contracts Act 1994 (C'th)* nor here relevant) contains an implied term that the parties will deal fairly and in good faith. Nor is there in this jurisdiction any general principle by which a duty of good faith is implied in every contract".

In *GSA Group Limited v Siebe* (unreported) Supreme Court of New South Wales, 24 April 1993, Rogers CJ CommD was not persuaded to accept that commercial interest should be required to act in good faith towards each other.

".....why should commercial entities each with strong bargaining power, not be permitted to drive the best bargain they can, provided that they act within the law? "The courts should not be too eager to interfere in the commercial conduct of the parties, especially where the parties are all wealthy, experienced, commercial entities able to attend to their own interests."

His Honour referred to the increasing expectation in consumer contracts that the stronger party in the transaction will behave fairly, an expectation fostered or enforced by legislation such as the *Credit Act 1984 (NSW)* and the *Contracts Review Act 1980 (NSW)*. However the Chief Judge accepted:

"It is likely that, ultimately, Australian courts will embrace the American and civil law concept of the obligation that each contracting party should show good faith in the performance of contractual obligations. However the present case is not one where, even if such an obligation is implied, in the usual course of events, it should be implied, or even if implied would have the effect sought by the plaintiffs."

English writing at the time while on occasion receptive to the principle of good faith performance, did not advocate a generalised duty of good faith; see the lecture of Steyn J referred to by Priestley JA in *Renard Constructions.*

In his 1993 Cambridge Lecture, Sir Anthony Mason said that he thought it probable that the "concept of good faith" embraced no less than three related notions:

(1) an obligation on the parties to co-operate in achieving the contractual objects (loyalty to the promise itself);

(2) compliance with honest standards of conduct; and

(3) compliance with standards of contract which are reasonable having regard to the interests of the parties.

The movement away from the classical concept in contract law was towards one which focused on the reasonable expectations of the parties. In particular areas of the law this was not new. The common law imposed a duty of good faith in insurance contracts based on what the insured knows and the insurer does not and cannot. Another aspect of this was the rule that an insurer settling claims under a limited liability policy must act in good faith towards the insured and must have regard to his or her interests both in the defence of actions against the insured and in their settlement; *Distillers Co Biochemicals (Aust) Pty Limited v Ajax Insurance Co Limited* [1974] HCA 3; (1974) 130 CLR 1 at 31 and *Fredrikson v Insurance Corporation of British Columbia* (1990) 69 DLR (4^{th}) at 431.

In contracts for the sale of land the vendor is under a duty to disclose material matters relating to the title which are known to the vendor but which the purchaser has no means of discovering; *Carlish v Salt* [1906] 1 Ch 335; *Beyfus v Lodge* [1925] Ch 350 at 359; *In re Scott & Alvarez's Contract* [1895] 2 Ch 603 at 612. Other examples of cases where a party is required to take account of the interests of another party are:

* the mortgagee's exercise of a power of sale;

* majority shareholders acting honestly and having regard to the interests of the company; *Peters American Delicacy Co Limited v Heath* [1939] HCA 2; (1938) 61 CLR 457;

* the directors of an insolvent company or one verging on insolvency in disposing of assets to the detriment of creditors; *Walker v Wimborne* [1976] HCA 7; (1976) 137 CLR 1 at 7;

* the doctor who advises a patient in relation to proposed treatment; *Rogers v Whitaker* [1992] HCA 58; (1992) 175 CLR 479 (compare *Sidaway v Governors of Bethlem Royal Hospital* [1985] UKHL 1; [1985] AC 871);

* the application of the principles of equity governing fiduciaries;

* undue influence and unconscionable conduct in estoppel, including promissory estoppel; and

* the duty to refrain from making misrepresentations.

Moreover, the common law imposes a duty on the parties to a contract to co-operate in achieving the objects of the contract. See *Mackay v Dick* (1881) 6 App Cas 251 at 263; *Secured Income Real Estate (Australia) Limited v St Martins Investments Pty Limited* [1979] HCA 51; (1979) 144 CLR 596 at 607; *Perri v Coolangatta Investments Pty Limited* [1982] HCA 29; (1982) 149 CLR 537; *Meehan v Jones* [1982] HCA 52; (1982) 149 CLR 571. Sir Anthony Mason said that such cases come close to a recognition of the good faith doctrine described as "loyalty to the promise itself". But such an obligation cannot override the express provisions of the contract.

If a contract confers power on a contracting party in terms wider than necessary for the protection of the legitimate interests of that party, the courts may interpret the power as not extending to the action proposed by the party in whom the power is vested or, alternatively, conclude that the powers are being exercised in a capricious or arbitrary manner or for an extraneous purpose, which is another was of saying the same thing. Thus, a vendor may not be allowed to exercise a contractual power where it would be unconscionable in the circumstances to do so; *Pierce Bell Sales Pty Limited v Frazer* [1973] HCA 13; (1973) 130 CLR 575 at 587.

Sir Anthony Mason was of the view that due partly to the absence of good faith doctrine regulating contract performance it had become the subject of statutory regulation such as is found in the *Contracts Review Act 1980* and the *Trade Practices Act 1975*. But see also *Commercial Bank of Australia v Amadio* [1983] HCA 14; (1983) 151 CLR 447; *Taylor v Johnson* [1983] HCA 5; (1983) 151 CLR 422 and *Legione v Hateley* [1983] HCA 11; (1982) 152 CLR 406. Part of this development is the fiduciary principle. However, that principle cannot be superimposed upon the contract in such a way as to alter the operation which that contract was intended to have according to its true construction; *Hospital Products Limited v United States Surgical Corporation & Ors* [1984] HCA 64; (1984) 156 CLR 41 at 97 and *Kelly v Cooper* [1993] AC 205 at 215.

Steyn J in the lecture to which I have referred said that the first imperative of good faith and fair dealing is that contracts ought to be upheld. In *Kirke La Schelle Co v Paul Armstrong Co* 188 NE 163 (1993) the New York Court of Appeals said at 167:

"……in every contract there is an implied covenant that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract, which means that in every contract there exists an implied covenant of good faith and fair dealing."

See also *Wood v Lucy Duff-Gordon* 222 NY 88 per Cardozo J. In *Royal Brunei Airlines SdnBhd v Tan* [1995] UKPC 4; [1995] 2 AC 378 at 381 the proper role of equity in commercial transactions and the desirability of the infusion of minimum standards of fairness, good faith and good conscience into our law, were described simply as "topical questions". Gleeson CJ, in an article entitled "Individualised Justice - The Holy Grail" 1995 69 ALJ 421 at 428, remarked that "for a number of reasons, some to do with the work of legislatures, some to do with judicial law making, and some to do with the temper and spirit of the times, we can no longer say that, in all but exceptional cases, the rights and liabilities of parties to a written contract can be discovered by reading the contract."

The decisions in *Renard Constructions* and *Hughes Bros* mean that in New South Wales a duty of good faith, both in performing obligations and exercising rights, may by implication be imposed upon parties as part of a contract. There is no reason why such a duty should not be implied as part of this lease. But it remains to decide whether the implication of that duty has any consequence in the resolution of the dispute the subject of this appeal.

CONCLUSION

The trial Judge voiced his concern at a tenant's being left at the mercy of the landlord acting in a capricious manner but recognised that a claim for indemnity to meet unreasonable requirements of a fire order might to that extent fail. This may or may not be correct. But the appellant has not demonstrated that the requirements of the fire order were unreasonable.

The legislature has prescribed a procedure for challenging a fire order in the Land and Environment Court. That procedure has not been adopted, a problem to which the appellant directed grounds 5 and 9 of the appeal. The application to the Equity Division for an order authorising the appellant to make application to the Land and Environment Court for an order that the name of the appellant as applicant be substituted for the names of the respondents as applicants was doomed to failure. The fate of such an application was entirely a matter for the Land and Environment Court. The authority sought could not affect the matter and was entirely futile. In any event, there was evidence that the other party would oppose it.

Unchallenged, the law requires that the Council fire order be complied with. There is no evidence to suggest that the order was unreasonable in a way which might have led, on an appropriate application of administrative law, to its being struck down. The evidence was that its terms fell within the recommendations of Mr McMonnies, a qualified fire engineer with twenty years experience. His report was not challenged either by cross-examination or the evidence of some other expert. No doubt, for this reason, late in the day counsel for the appellant sought to bring Mr McMonnies before Windeyer J on a subpoena. As a matter of discretion, Windeyer J refused to issue a subpoena. No reason is shown to suggest that this exercise of discretion miscarried. While it might be thought that the events leading up to the imposition of the fire order were unusual that is a long way from saying that the Council, acting at the behest of the respondents in imposing requirements which fell within Mr McMonnies' recommendations, acted so unreasonably that the fire order was bad.

The result is that, in my opinion, the grounds of appeal relied on whether expressed as a requirement of an implied term in the contract or as allegations of unconscionable conduct by the respondents fail. In a commercial context it cannot be said, in my opinion, that a property owner acts unconscionably or in breach of an implied term of good faith in a lease of the property by taking steps to ensure that the requirements for fire safety advised by an expert fire engineer should be put in place. It was the duty of the Council to ensure that adequate provision for fire safety was made in the building (s317D of the *Local Government Act 1919*) and the contractual duty of the appellant to observe and perform the requirements of the Council, if lawful, and to do and execute or cause to be done and executed such works as were required by the Council. The respondents had a legitimate interest in ensuring that the building was properly protected. If the respondents felt that the Council requirements were insufficient, as it had been advised, I can see no reason why they should not press for more stringent requirements.

In my opinion, the appeal fails and accordingly, the second appeal should be dismissed with costs.

ORDER

Both appeals are dismissed with costs.

POWELL JA: I agree with Sheller JA.

BEAZLEY JA: I agree with Sheller JA.