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10. Implied Terms

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Abstract

This chapter discusses implied terms. Terms may be implied into contracts from three principal sources: statute, custom, and the courts. Parliament has, on a number of occasions, implied terms into contracts. The precise reason for the implication of the term depends upon the particular statute. It may be to give effect to the presumed intention of the parties; it may be to reduce uncertainty by enacting a default rule out of which the parties can contract if they do not like the term that Parliament has seen fit to imply; or it may be to protect one party to the transaction from the superior bargaining power of the other. Terms can also be implied into contracts by custom where the custom is certain, reasonable, and notorious. Customs and usages are an important source of obligations in commercial contracts. Terms implied by the courts can be divided into two groups, namely terms implied in fact and terms implied in law. A term is implied in fact when it is implied into the contract in order to give effect to what is deemed by the court to be the unexpressed intention of the parties and is implied because it is necessary to make the contract work. Terms implied in law 'are those terms that are consistently implied into all contracts of a particular type because of the nature of the contract, rather than the supposed intentions of the parties'.

Keywords: English contract law, contract terms, implied terms, Parliament, custom, terms implied in law, terms implied in fact

Central Issues

1. Terms may be implied into contracts from three principal sources, namely statute, custom, and the courts.

2. Terms are frequently implied into contracts by Parliament. These terms can be very important in practice. For example, terms are implied into contracts for the sale of goods which give buyers important rights against sellers. These terms were first enacted in the Sale of Goods Act 1893 and are now to be found in the Sale of Goods Act 1979 (and for consumers in the Consumer Rights Act 2015).
3. Terms can also be implied into contracts by custom where the custom is certain, reasonable, and notorious. Customs and usages are an important source of obligations in commercial contracts.
4. Courts also imply terms into contracts. The jurisdiction of the court to imply terms into a contract is a source of considerable controversy. The difficulty which the courts have experienced lies in locating both the basis and the extent of their jurisdiction to imply terms into a contract. The traditional justification for the implication of terms is that the court is giving effect to the presumed intention of the parties. Terms were therefore implied on the basis that it was necessary to do so. However, it is difficult, if not impossible, to justify the implication of all terms on the basis of necessity. In some cases the courts take account of a wider range of considerations than the presumed intention of the parties and apply a test that is less stringent than necessity. On the other hand, the courts have rejected the proposition that they can imply a term into a contract simply on the basis that it is reasonable to do so.
5. Implied terms are customarily divided into two categories, namely terms implied in law and terms implied in fact. In the case of terms implied in fact it is possible to ascribe the implied term to the intention of the parties, but it is much more difficult to do this where the term is implied in law. In the latter case a term is implied as an incident of every contract of that kind and the courts take account of a wide range of considerations when deciding whether or not to imply such a term into the contract.

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10.1 Introduction

Implied terms are important both in practice and in theory. They are important in practice because a number of important terms in contracts today are there as a result of implication rather than express agreement. The implied terms contained in sections 12–15 of the Sale of Goods Act 1979 and in sections 9–18 of the Consumer Rights Act 2015 impose important obligations upon sellers of goods. The word ‘impose’ is important. These terms can no longer be attributed to the intention of the parties because Parliament has intervened to establish very strict limits within which these terms can be excluded (in the case of consumer contracts they cannot be excluded at all). One of the important terms to be found in contracts of employment is a term to the effect that the parties must not conduct themselves in such a way as to undermine the relationship of ‘trust and confidence’ that exists between an employer and an employee. Again, this implied term does not owe its origin to the express agreement of the parties. Its source is to be found in the willingness of the courts to imply such a term into contracts of employment (*Mahmud* v. *Bank of Credit and Commercial International SA* [1998] AC 20, see further 10.4.2).

Implied terms, also sometimes referred to as default rules to reflect the fact that their function is to fill gaps in the parties' contract and that they do so unless they have been excluded by the parties, play an important role in commercial contracts. As Lord Diplock observed in *Photo Production Ltd* v. *Securicor Transport Ltd* [1980] AC 827, 848 'in practice a commercial contract never states all the primary obligations of the parties in full; many are left to be incorporated by implication of law from the legal nature of the contract into which the parties are entering'. This point was developed by Lord Leggatt in *Barton* v. *Morris* [2023] UKSC 3, [2023] 2 WLR 269, in the following terms:

> [127] ... life is too short to negotiate contract terms designed to cover every contingency that may occur. Even the most comprehensive and carefully drafted written contract cannot anticipate and provide expressly in advance for every possible contingency. And even where contingencies are foreseeable, commerce would be stultified if time and cost was routinely incurred in discussing and making provision for situations that are not thought likely to happen.
>
> [128] Establishing default rules serves to reduce the costs and inconvenience of negotiating terms and also to avoid unfair outcomes in cases where parties, whether through inertia, lack of opportunity or foresight, or deliberate choice, have not negotiated express terms to cover certain significant contingencies. Such default rules are generally optimal when they reflect prevailing social norms and expectations and therefore create rights and obligations which reasonable parties would be likely to agree between themselves.

Two issues of particular significance arise in relation to implied terms. The first relates to the justification for implying terms into contracts. On what basis do the courts and Parliament imply terms into a contract? Is it to give effect to the presumed intention of the parties or is the search for an implied term based on wider considerations of policy? The second issue relates to the test to be applied by the courts when deciding whether or not to imply a term into a contract. This issue is related to the first one. If the justification for implying a term into a contract is to give effect to the presumed intention of the parties, then it can be said that the test is based on necessity. A term will only be implied where it is necessary to give effect to the presumed intention of the parties. On the other hand, if the justification for implying a term is to be located in
p. 337 broader issues of policy, then one would ↵ expect the test applied by the court to reflect these broader policy issues: in short, one would expect a test based upon criteria such as the reasonableness of the implication on the facts of the case.

10.2 Terms Implied by Statute

Parliament has, on a number of occasions, implied terms into contracts. The precise reason for the implication of the term obviously depends upon the particular statute. It may be to give effect to the presumed intention of the parties; it may be to reduce uncertainty by enacting a default rule out of which the parties can contract if they do not like the term that Parliament has seen fit to imply; or it may be to protect one party to the transaction from the superior bargaining power of the other party. Terms have been implied by Parliament into a wide range of transactions: for example, contracts for the sale of goods, hire-purchase

contracts, other contracts for the supply of goods, contracts for the supply of services, and contracts for the construction of a dwelling. We shall use contracts for the sale of goods as our example. Sections 12–15 of the Sale of Goods Act 1979 imply a number of terms into contracts for the sale of goods. These terms are as follows:

Implied terms about title, etc.

12.(1) In a contract of sale, other than one to which subsection (3) below applies, there is an implied term on the part of the seller that in the case of a sale he has a right to sell the goods, and in the case of an agreement to sell he will have such a right at the time when the property is to pass.

(2) In a contract of sale, other than one to which subsection (3) below applies, there is also an implied term that—

(a) the goods are free, and will remain free until the time when the property is to pass, from any charge or encumbrance not disclosed or known to the buyer before the contract is made, and

(b) the buyer will enjoy quiet possession of the goods except so far as it may be disturbed by the owner or other person entitled to the benefit of any charge or encumbrance so disclosed or known.

(3) This subsection applies to a contract of sale in the case of which there appears from the contract or is to be inferred from its circumstances an intention that the seller should transfer only such title as he or a third person may have.

(4) In a contract to which subsection (3) above applies there is an implied term that all charges or encumbrances known to the seller and not known to the buyer have been disclosed to the buyer before the contract is made.

(5) In a contract to which subsection (3) above applies there is also an implied term that none of the following will disturb the buyer's quiet possession of the goods, namely—

(a) the seller;

(b) in a case where the parties to the contract intend that the seller should transfer only such title as a third person may have, that person;

p. 338 (c) anyone claiming through or under the seller or that third person otherwise than under a charge or encumbrance disclosed or known to the buyer before the contract is made.

(5A) As regards England and Wales and Northern Ireland, the term implied by subsection (1) above is a condition and the terms implied by subsections (2), (4) and (5) above are warranties.

...

(7) This section does not apply to a contract to which Chapter 2 of Part 1 of the Consumer Rights Act 2015 applies (but see the provision made about such contracts in section 17 of that Act).

Sale by description

13.—(1) Where there is a contract for the sale of goods by description, there is an implied term that the goods will correspond with the description.

(1A) As regards England and Wales and Northern Ireland, the term implied by subsection (1) above is a condition.

(2) If the sale is by sample as well as by description it is not sufficient that the bulk of the goods corresponds with the sample if the goods do not also correspond with the description.

(3) A sale of goods is not prevented from being a sale by description by reason only that, being exposed for sale or hire, they are selected by the buyer.

...

(5) This section does not apply to a contract to which Chapter 2 of Part 1 of the Consumer Rights Act 2015 applies (but see the provision made about such contracts in section 11 of that Act).

Implied terms about quality or fitness

14.—(1) Except as provided by this section and section 15 below and subject to any other enactment, there is no implied term about the quality or fitness for any particular purpose of goods supplied under a contract of sale.

(2) Where the seller sells goods in the course of a business, there is an implied term that the goods supplied under the contract are of satisfactory quality.

(2A) For the purposes of this Act, goods are of satisfactory quality if they meet the standard that a reasonable person would regard as satisfactory, taking account of any description of the goods, the price (if relevant) and all the other relevant circumstances.

(2B) For the purposes of this Act, the quality of goods includes their state and condition and the following (among others) are in appropriate cases aspects of the quality of goods—

(a) fitness for all the purposes for which goods of the kind in question are commonly supplied,

(b) appearance and finish,

(c) freedom from minor defects,

p. 339 (d) safety, and

(e) durability.

(2C) The term implied by subsection (2) above does not extend to any matter making the quality of goods unsatisfactory—

(a) which is specifically drawn to the buyer's attention before the contract is made,

(b) where the buyer examines the goods before the contract is made, which that examination ought to reveal, or

(c) in the case of a contract for sale by sample, which would have been apparent on a reasonable examination of the sample.

...

(3) Where the seller sells goods in the course of a business and the buyer, expressly or by implication, makes known—

(a) to the seller, or

(b) where the purchase price or part of it is payable by instalments and the goods were previously sold by a credit-broker to the seller, to that credit-broker,

any particular purpose for which the goods are being bought, there is an implied term that the goods supplied under the contract are reasonably fit for that purpose, whether or not that is a purpose for which such goods are commonly supplied, except where the circumstances show that the buyer does not rely, or that it is unreasonable for him to rely, on the skill or judgment of the seller or credit-broker.

(4) An implied term about quality or fitness for a particular purpose may be annexed to a contract of sale by usage.

(5) The preceding provisions of this section apply to a sale by a person who in the course of a business is acting as agent for another as they apply to a sale by a principal in the course of a business, except where that other is not selling in the course of a business and either the buyer knows that fact or reasonable steps are taken to bring it to the notice of the buyer before the contract is made.

(6) As regards England and Wales and Northern Ireland, the terms implied by subsections (2) and (3) above are conditions.

...

(9) This section does not apply to a contract to which Chapter 2 of Part 1 of the Consumer Rights Act 2015 applies (but see the provision made about such contracts in sections 9, 10 and 18 of that Act).

Sale by sample

Sale by sample

15.—(1) A contract of sale is a contract for sale by sample where there is an express or implied term to that effect in the contract.

(2) In the case of a contract for sale by sample there is an implied term—

(a) that the bulk will correspond with the sample in quality;

> ...
>
> p. 340 (c) that the goods will be free from any defect, making their quality unsatisfactory, which would not be apparent on reasonable examination of the sample.
>
> (3) As regards England and Wales and Northern Ireland, the term implied by subsection (2) above is a condition.
>
> ...
>
> (5) This section does not apply to a contract to which Chapter 2 of Part 1 of the Consumer Rights Act 2015 applies (but see the provision made about such contracts in sections 13 and 18 of that Act).

Commentary

These implied terms are of considerable significance for buyers of goods because they give them a number of important rights against sellers of goods. The rule at common law was generally believed to be '*caveat emptor*' (let the buyer beware). Under such a rule the onus was put upon the buyer to seek a specific undertaking from the seller in relation to the quality of the goods. Now that the implied terms have been enacted, the need for buyers to seek express undertakings from sellers has been significantly reduced. The implied terms contained in sections 12–15 of the Sale of Goods Act 1979 provide buyers with a minimum floor of rights and, as we shall see, the law has placed considerable limits on the ability of sellers to contract out of these implied terms. It should be noted that these implied terms no longer apply to contracts of sale concluded between a trader and a consumer. This is because such contracts now fall within the scope of Part 2 of the Consumer Rights Act 2015, which makes provision for the incorporation of broadly similar but slightly differently worded terms into such contracts. In the account that follows we shall focus attention on contracts which fall within the scope of the Sale of Goods Act 1979 and will not enter into the details of sections 9–18 of the Consumer Rights Act 2015.

The aim of section 12 is to give a buyer a remedy against a seller in the event that the seller does not have title to sell the goods that he has contracted to sell to the buyer. In such a case the buyer will generally be entitled to recover from the seller the price which he has paid for the goods. This is so even in the case where the buyer has been able to make use of the goods over a period of time prior to discovery of the fact that the seller did not have title to the goods that have been sold to the buyer (see, for example, *Rowland* v. *Divall* [1923] 2 KB 500). Section 12(2) also implies two warranties into contracts for the sale of goods. The function of the warranties of freedom from encumbrances and quiet possession is, essentially, to enable the buyer to enjoy the use of the goods without interference by third parties. The implied term as to title is a condition, whereas the implied terms relating to freedom from encumbrances and quiet possession are warranties. The difference between a condition and a warranty will be explained in more detail in a later chapter (see 22.3.1). Here it suffices to note that breach of a condition entitles a buyer to reject the goods and terminate the contract, whereas breach of a warranty does not. The only remedy for breach of a warranty is damages.

Section 13 provides protection for the buyer who receives goods that do not correspond with the description. The section is, however, more difficult than it looks at first sight and it has generated a considerable amount
p. 341 of case-law. The section only comes into play ↵ where there has been a contract for sale 'by' description.

In order for the contract to be by description the buyer must have entered into the contract in reliance upon the description provided by the seller (*Harlingdon and Leinster Enterprises Ltd* v. *Christopher Hull Fine Art Ltd* [1991] 1 QB 564). In order to amount to a 'description' the words used must identify the subject matter of the contract (*Reardon Smith Line Ltd* v. *Yngvar Hansen-Tangen* [1976] 1 WLR 989).

Section 14 implies two very important conditions into contracts for the sale of goods. The first, contained in section 14(2), (2A), and (2B), is that the goods must be of 'satisfactory quality' (formerly 'merchantable quality'). It provides a checklist of factors to be taken into account when deciding whether or not goods are of satisfactory quality. The second condition, to be found in section 14(3), is that the goods must be reasonably fit for their purpose. A buyer who wishes to make some unusual use of the goods must disclose that use to the seller prior to entry into the contract of sale if he wishes to be able to invoke the fitness for purpose implied term. The seller does not provide a guarantee that the goods will be fit for all purposes. The goods need only be 'reasonably fit' for their purpose. So, where the goods cannot be used for their intended purpose because of some idiosyncrasy, not made known to the seller, of the buyer or in the circumstances of the use of the goods by the buyer, the seller will not be liable to the buyer under section 14(3) (*Slater* v. *Finning Ltd* [1997] AC 473). These two conditions only come into play where the 'seller sells goods in the course of a business'. The test applied by the court when deciding whether or not the seller sold in the course of a business does not depend upon the regularity of the sale or whether it was integral to the seller's business. In *Stevenson* v. *Rogers* [1999] QB 1028 the Court of Appeal held that, unless the sale was 'a purely private sale of goods outside the confines of the business (if any) carried on by the seller' it is within the course of the seller's business so as to attract the implied terms relating to satisfactory quality and fitness for purpose.

Section 15 implies two conditions in the case of a sale of goods by sample. The first is that the bulk will correspond with the sample in quality and the second is that the goods will be free from any defect making their quality unsatisfactory, which would not be apparent on reasonable examination of the sample (see *Godley* v. *Perry* [1960] 1 WLR 9).

The importance of these implied terms is demonstrated by the fact that Parliament has intervened to place restrictions upon the ability of sellers to exclude their operation. In the case of contracts of sale concluded between a trader and a consumer, the terms implied by sections 9–18 of the Consumer Rights Act 2015 cannot be excluded as against the consumer (see section 31 of the 2015 Act). In commercial sales the implied terms in the Sale of Goods Act can be excluded provided that it is reasonable to do so (except in the case of section 12 where it is not possible to exclude liability for breach of this term). Statutory controls on exclusion and limitation of liability are discussed in more detail later (see 13.3).

What is the basis of these implied terms? Are they based on the presumed intention of the parties? There is some support for this proposition in the authorities. In *Philips Electronique Grand Publique SA* v. *British Sky Broadcasting Ltd* [1995] EMLR 472 Lord Bingham MR stated (at p. 481) that:

> quite apart from statute, the courts would not ordinarily hesitate to imply into a contract for the sale of unseen goods that they should be of merchantable quality and answer to their description and conform with sample. It is hard to imagine trade conducted, in the absence of express agreement, on any other terms.

p. 342 ↵ While it may be 'hard to imagine' trade being conducted on any other terms, it is not impossible. There is still in English law no general implied term that a house is fit for any particular purpose or even for human habitation. Further, as a general rule a landlord does not give an implied undertaking that leased premises will be fit for habitation or for any particular purpose, although in the case of a lease of furnished premises there is an implied condition that the premises are fit for human habitation at the beginning of the tenancy. If contracts for the sale of real property can be concluded without the benefit of extensive implied terms for the benefit of the purchaser, can the same not be said of contracts for the sale of personal property, such as goods? Support for the proposition that contracts for the sale of goods can be concluded without the benefit of such implied terms can be derived from the law of sale in the nineteenth century, where *caveat emptor* played a much more dominant role than it does today. This being the case, the claim that the implied terms are based on the presumed intention of the parties seems very doubtful. It is much more likely that the function of the implied terms is to protect what are perceived to be the legitimate or reasonable expectations of buyers when they enter into contracts for the sale of goods. That this is so is evidenced by the fact that Parliament has intervened to limit the ability of sellers to contract out of these terms. The fact that it is impossible to contract out of some of these implied terms demonstrates that they are not based on the presumed intention of the parties. They are part of a legislative policy to protect the expectations of buyers, especially consumer buyers.

10.3 Terms Implied from Usage or Custom

Terms may be implied into a contract from the usage or custom of the industry or market in which the parties transact. In *Hutton* v. *Warren* (1836) 1 M & W 466 Parke B stated (at p. 475) that:

> [i]t has long been settled, that, in commercial transactions, extrinsic evidence of custom and usage is admissible to annex incidents to written contracts, in matters with respect to which they are silent. The same rule has also been applied to contracts in other transactions of life, in which known usages have been established and prevailed; and this has been done upon the principle of presumption that, in such transactions, the parties did not mean to express in writing the whole of the contract by which they intended to be bound, but a contract with reference to those known usages. Whether such a relaxation of the strictness of the common law was wisely applied, where formal instruments have been entered into, and particularly leases under seal, may well be doubted; but the contrary has been established by such authority, and the relations between landlord and tenant have been so long regulated upon the supposition that all customary obligations, not altered by the contract, are to remain in force, that it is too late to pursue a contrary course; and it would be productive of much inconvenience if this practice were now to be disturbed.

Two points emerge from this statement. The first is that the usage must be a 'known' usage. This does not mean that the parties must actually have been aware of its existence. It suffices that it was so well known that 'an outsider who makes reasonable enquiries could not fail to be made aware of it' (*Kum* v. *Wah Tat Bank Ltd* p. 343 [1971] 1 ↵ Lloyd's Rep 439, 444). The requirement that the custom be 'known' is often expressed in the formula that the custom or usage must be 'notorious, certain and reasonable'. In *Cunliffe-Owen* v. *Teather & Greenwood* [1967] 1 WLR 1421 Ungoed-Thomas J stated (at pp. 1438–1439) that:

> [f]or the practice to amount to such a recognised usage, it must be certain, in the sense that the practice is clearly established; it must be notorious, in the sense that it is so well known in the market in which it is alleged to exist that those who conduct business in that market contract with the usage as an implied term, and it must be reasonable. The burden lies on those alleging usage to establish it. … The practice that has to be established consists of a continuity of acts, and those acts have to be established by persons familiar with them, although, as is accepted before me, they may be sufficiently established by such persons without a detailed recital of instances. Practice is not a matter of opinion of even the most highly qualified expert as to what it is desirable that the practice should be. However, evidence of those versed in a market, so it seems to me, may be admissible and valuable in identifying those features of any transaction that attract usage and in discounting other features which for such purpose are merely incidental and if there is conflict of evidence about this it is subject to being resolved like other conflicts of evidence. Arrangements or compromises to the same effect as the alleged usage do not establish usage; they contradict it. They may be the precursors of usage, but usage presupposes that arrangements and compromises are no longer required. It is, in my view, clearly not necessary that a practice should be challenged and enforced before it can become a usage as, otherwise, a practice so obviously universally accepted and acted on as not to be challenged could never be a usage. However, enforcement would be valuable and might be conclusive in establishing usage. What is necessary is that for a practice to be a recognised usage it should be established as a practice having binding effect.

The last sentence is important because it demonstrates that repetitive behaviour in the market is not sufficient, of itself, to establish a custom: 'it must also be shown that this pattern of behaviour is observed from a sense of legally binding obligation, not from mere courtesy, convenience or expediency' (R Goode, 'Usage and its Reception in Transnational Commercial Law' (1997) 46 *ICLQ* 1, 8). In *General Reinsurance Corp* v. *Försäkringsaktiebolaget Fennia Patria* [1983] QB 856, 874 Slade LJ stated:

> There is, however, the world of difference between a course of conduct that is frequently, or even habitually, followed in a particular commercial community as a matter of grace and a course which is habitually followed because it is considered that the parties concerned have a legally binding right to demand it.

The distinction between courtesy and obligation, while easy to state in theory, can be difficult to draw in practice (see, for example, *Libyan Arab Foreign Bank* v. *Bankers Trust Co* [1989] QB 728). It is nevertheless a distinction of considerable importance.

The second point that can be derived from the judgment of Parke B in *Warren* is that the custom must not have been 'altered by the contract'. A term will therefore not be implied into a contract by custom where the custom is inconsistent with the express terms of the contract (*Palgrave, Brown & Son Ltd* v. *SS Turid (Owners)* [1922] 1 AC 397).

p. 344 ↵ Custom and usage play an important role in commercial law generally as the following extract demonstrates.

Ewan McKendrick, *Goode and McKendrick on Commercial Law* (6th edn, Penguin, 2020), paras 1.21–1.24

> Of great importance as a source of obligation in commercial contracts are the unwritten customs and usages of merchants. The impact of these on the content and interpretation of contract terms cannot be overstated. It is, perhaps, this feature above all which distinguishes commercial from other contracts, a distinction not formally adopted by the law. The fertility of the business mind and the fact that a practice which begins life by having no legal force acquires over time the sanctity of law are key factors to which the commercial lawyer must continually be responsive. Is a particular document a document of title? The House of Lords or other appellate court may have said no, possibly more than once. But how long ago was the ruling given? Cannot it now be said, in another time, that the acceptance of this document as a document of title in mercantile usage is so entrenched as to justify according it legal recognition as such?. ...
>
> What is it that gives binding force to unwritten mercantile usage? Is it the express or implied adoption of the usage by the parties in their contract? Or does mercantile usage have independent normative force? The question has been much debated in the context of international commercial arbitration and the controversy as to the existence of an international *lex mercatoria*. In some legal systems the binding force of mercantile usage does not depend on adoption by contract, but in the theory of English law usage takes effect as an express or implied term of the contract between the parties and is dependent for its validity on satisfying certain legal criteria, namely certainty and consistency of practice, reasonableness, notoriety, and conformity with mandatory law. Moreover, in order to constitute a usage the practice must be observed from a sense of legally binding obligation, not as a matter of mere courtesy or convenience or a desire to accommodate a customer's wishes.
>
> It is in the nature of unwritten custom or usage that its meaning and content may be understood differently by different people; indeed, the very existence of an alleged usage may be challenged. In areas of business or finance with a highly developed and widely used body of custom or usage it is particularly important to avoid disputes of this kind. To that end, national and international trade associations and clearing houses may find it convenient to formulate the relevant usages in a published code or set of rules. These will rarely reflect existing usage in every particular, since the opportunity will usually be taken to make improvements to established practice and procedures, but the intended effect of the code or rules is to state or restate best practice. They may be given effect either by making adherence to them a condition of membership of the relevant association or clearing house or by incorporation into individual contracts. At the international level the prime mover in the codification of international trade usage is the International Chamber of Commerce (ICC), an international nongovernmental organization serving world business. Working through its specialist Commissions, the ICC has produced numerous uniform rules which are adopted by incorporation into contracts. These fall broadly into three groups: banking and insurance, international trade and international transport. The most long-standing and successful of the various ICC formulations is the Uniform Customs and Practice for Documentary Credits (UCP), first promulgated by the ICC in 1933. Bankers throughout the world have adopted the UCP, which is now used almost universally in documentary credit transactions.[1] ...

> In English law codified customs and usages, like those which are uncodified, depend for their operation on express or implied adoption in the contract.

p. 345 ↵ As the last sentence of the extract makes clear, customs, at least in English law, depend for their operation on 'express or implied' incorporation into the contract. Very often that incorporation will be express (and so might properly be said to fall within the scope of Chapter 9). Thus banks will generally incorporate the UCP expressly into their contracts with their customers. The reason for this is that the matter is too important to be left to implication by a court. However, should a bank fail, for some reason, to incorporate the UCP into a contract with one of its customers, it is likely that a court would conclude that it was incorporated into the contract either on the basis of custom or on the basis of a course of dealing between the parties (on which see 9.4).

10.4 Terms Implied by the Courts

It is customary to divide terms implied by the courts into two groups, namely terms implied in fact and terms implied in law. A term is implied in fact when it is implied into the contract in order to give effect to what is deemed by the court to be the unexpressed intention of the parties to that contract. It is a term that is specific to the particular transaction between the parties. Terms implied in law 'are those terms that are consistently implied into all contracts of a particular type because of the nature of the contract, rather than the supposed intentions of the parties' (E Peden, 'Policy Concerns Behind Implication of Terms in Law' (2001) 117 *LQR* 459). For example, the courts have held that there is an implied term of 'trust and confidence' in contracts of employment (see 10.4.2). The existence of this term is not dependent upon it being representative of the unexpressed intention of the parties to the particular employment contract. It is a term that is implied into all contracts of employment unless it has been expressly excluded by the parties.

The distinction between terms implied in fact and terms implied in law is not, however, simply a matter of the generality of the term to be implied. As Lord Leggatt observed in *Barton* v. *Morris* [2023] UKSC 3, [2023] 2 WLR 269, [135]:

> There are two more important differences. First, where a term is implied in law, cases establishing the applicable rule of law have the force of precedent in relation to other contracts of the same type. A term implied in fact, on the other hand, is an individualised term 'which is implied into a particular contract, in the light of the express terms, commercial common sense, and the facts known to both parties at the time the contract was made'. … As with decisions on the interpretation of contract terms, judicial decisions relating to different contracts made in different circumstances are usually of little assistance. Second, there is a difference in who bears what may be called the burden of expression: see E Allan Farnsworth, 'Disputes over Omission in Contracts' (1968) 68 Colum L Rev 860, 884. A contract is presumed to include any term implied in law as a standard incident of a contract of that type, unless such a term is expressly excluded … By contrast, a party contending that a term is to be implied in fact has to overcome a presumption that, at any rate where the parties have entered into a detailed written contract, they have expressed all the terms particular to their individual bargain.

A further point of importance in relation to the distinction between a term implied in fact and a term implied in law is that the test for the implication of a term as a matter of law appears to be less stringent than that applicable to terms implied in fact. Traditionally, the courts have insisted that they will only imply a term into
p. 346 a contract as a matter of fact where ↵ it is 'necessary' to do so. In the case of terms implied in law, however, it would appear that the test is not one of necessity, although the precise nature of the test remains unclear. It appears to be somewhere in between 'reasonableness' and 'necessity'. Thus it might be said that it must be 'reasonably necessary' to imply the term into the contract.

While the distinction between terms implied in fact and terms implied in law is now clearly established in the case-law, it is not always an easy distinction to draw. Nor is there a need for a claimant seeking to imply a term into a contract to choose or elect between the two methods of implication. It not uncommon for claimants to seek to rely on both a term implied in fact and a term implied in law in the hope that the court will accept one or other submission (or even both). A recent example of this phenomenon is the decision of the Supreme Court in *Barton* v. *Morris* [2023] UKSC 3, [2023] 2 WLR 269.

The claimant entered into an oral agreement with the defendant under which the defendant agreed to pay to the claimant the sum of £1.2 million if a property known as Nash House was sold for £6.5 million to a purchaser who was introduced by the claimant. The claimant introduced a purchaser who offered to pay £6.5 million for the property but the price at completion was reduced to £6 million as a result of adjustments made to reflect the impact of the HS2 project on the property concerned. In these circumstances the claimant sought to recover payment from the defendant. The defendant denied any liability to pay on the ground that the sale price of £6.5 million had not been achieved.

The claimant failed in his attempt to recover payment under the express terms of the contract because the contract was held to entitle the claimant to recover payment only if the sale price of £6.5 million was achieved. There being no express term to support his claim for payment, the claimant sought to imply a term into the contract.

His first attempt was to seek to imply a term in fact into the contract that he was entitled to be paid a reasonable fee for the services he had rendered. This claim failed on the ground that it did not satisfy the test that is applicable to terms implied in fact (on which see 10.4.1) because it was not necessary to imply such a term into the contract in order to make it work. The contract was held to work perfectly well on the basis that the claimant would be paid £1.2 million if the property was sold for £6.5 million but would be paid nothing if that price was not achieved. In other words, the claimant was held to have taken the risk that the agreed price would not be achieved and he could not rely on a term implied in fact in order to transfer that risk, or part of that risk, to the defendant.

Having failed to imply a term in fact, the claimant then sought to rely on a term implied in law that the defendant would pay a reasonable sum (assessed as £435,000) for the services which he had rendered. The minority, Lord Leggatt and Lord Burrows, would have implied such a term into the contract between the parties. Lord Leggatt ([138]) put the case for the implication of a term in law on the following basis:

> The obligation to pay a reasonable sum reflects the ordinary expectation that those who, in a commercial context, provide valuable services to others do so for reward and not simply out of charity or benevolence; and by the same token someone who requests such services does so on the understanding that they are to be paid for. The law gives effect to this common understanding by imposing, in the absence of contrary agreement, an obligation to pay a reasonable sum which represents what the services were worth.

However, the majority, in a judgment given by Lady Rose, declined to imply a term in law into the contract between the parties. While the majority recognised the existence of a line of authority under which estate
p. 347 agents have been held to be entitled to recover a fee from the ↵ seller of a property on the completion of the sale, they held that the claimant in the present case was not an estate agent and so not entitled to rely on this line of authority. The majority also attached significance to the size of the fee which was 'several times the reasonable fee' for the introduction and they inferred from the size of the fee that the claimant had taken the risk that he would not be paid at all if he failed to achieve a sale at £6.5 million.

Two points of particular significance emerge from *Barton* v. *Morris*. The first relates to the relationship between the interpretation of the express terms of the contract and the willingness of the court to imply a term into the contract. The interpretation of the contract adopted by the majority was that the parties had agreed that the claimant would be paid £1.2 million only if the property was sold for £6.5 million and that, implicitly, they had agreed that the claimant would not be paid at all if the property was sold for a sum below £6.5 million. On this basis there was no room for the claimant's implied term because not only would it have reversed the contractual allocation of risk but it would have been contrary to the agreement which the trial judge found that the parties had concluded. The minority took a different view. While they agreed that the fee of £1.2 million was only to be paid if the sale price of £6.5 million was achieved, they held that the contract made no provision for what was to happen in the event that the price of £6.5 million was not achieved so that there was no necessary inconsistency between the agreement made by the parties and the implication of a term that the claimant was to be paid a reasonable fee for valuable services rendered and accepted by the defendant in the event that the property was sold for less than £6.5 million.

The second point relates to the difference in approach between the majority and the minority to the implication of a term in law. While the majority accepted that a term may be implied into a contract entitling a party to be paid a reasonable fee for services rendered as an incident of a 'particular kind of contract' ([44]), they adopted a much narrower understanding of the 'particular kind of contract' with which this case was concerned than that adopted by the minority. They regarded the line of authority in which a term has been implied entitling a party to recover the reasonable value of services rendered as 'a series of cases dealing with estate agents' ([51]) and, having held that the claimant was not formally acting as an estate agent, concluded that this line of authority was not applicable on the facts of the case. The minority, by contrast, took a much broader view of the category of case in which the implication is to be made. In their view the implication was to be made into contracts for the supply of services or commission agreements ([144]–[148] and [215]). While estate agents were part of this group, the category of contract into which the term was to be implied extended beyond estate agents and so encompassed the claimant in the present case. This difference of view illustrates the significance of the identification of the 'particular type' of contract into which the implication is to be

made. As the decision of the majority illustrates, a narrow approach to the identification of the term may make it more difficult to make the implication. Conversely, a broader approach of the type adopted by the minority, increases the scope to make the implication.

A final point which emerges from *Barton* v. *Morris* is the significance of the point made by Lord Leggatt, and discussed above, where he drew attention to the practical importance of the burden of proof in the case of terms implied in law. Once the minority concluded that the contract was one into which a term was to be implied in law, the burden switched to the defendant to show that the implied term had been excluded and this the defendant could not do. However, given the majority's conclusion that the present case did not fall within the estate agency cases, the burden in their view remained on the claimant to establish the existence of the implied term and they held that the claimant had not discharged that burden. One reason for the burden
p. 348 of proof assuming such significance in this context is that the ↵ contract is silent on the point in dispute. The inference which the court may draw from silence is that nothing was agreed by the parties so that, if the burden of proof remains on the claimant, it will not be able to discharge that burden and prove the existence of the implied term. But if a claimant can establish that the contract before the court is one of a particular type into which a term has been implied in law, then the task of the claimant suddenly becomes much easier because the burden then switches to the defendant to prove that the term has been excluded and a defendant may find it difficult to establish from silence that the term has been excluded.

Having thus sketched out the differences between a term implied in fact and a term implied in law, we shall now turn to consider the tests which the courts apply when deciding whether or not to imply a term as a matter of fact or of law into a contract between the parties.

10.4.1 Terms Implied in Fact

We shall start with the first leading case on the implication of terms into a contract, namely the decision of the Court of Appeal in *The Moorcock* (1889) 14 PD 64. It articulated a test based on 'necessity' rather than 'reasonableness'. We shall then make the leap to the leading modern decision on terms implied in fact, namely the decision of the Supreme Court in *Marks and Spencer plc* v. *BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72, [2016] AC 742.

The Moorcock
(1889) 14 PD 64, Court of Appeal

The defendants agreed to allow the plaintiff to discharge his vessel at their wharf so that the vessel could discharge and load her cargo. In order for the vessel to be able to discharge her cargo it was necessary for the vessel to be moored alongside the jetty (which was also owned by the defendants). The jetty extended into the River Thames and the bed of the river adjoining the jetty was vested in the Conservators of the River Thames. While the vessel was moored at the end of the jetty, the tide ebbed so that the vessel was no longer waterborne and she suffered damage as a result of the uneven condition of the river bed. The plaintiff brought an action for damages against the defendants. The defendants admitted that they had not taken any steps to ascertain whether or not the ground was level and suitable for the vessel. The trial judge, Butt J, held that the defendants were liable in damages to the plaintiff on the ground that they were in breach of an implied undertaking to take 'reasonable care to ascertain that the bottom of the river at the jetty was in such a condition as not to endanger the vessel using their premises in the ordinary way'. The defendants appealed to the Court of Appeal but the appeal was dismissed.

Bowen LJ

The question which arises here is whether when a contract is made to let the use of this jetty to a ship which can only use it, as is known by both parties, by taking the ground, there is any implied warranty on the part of the owners of the jetty, and if so, what is the extent of the warranty. Now, an
p. 349 implied warranty, or, as it is called, a covenant in law, as ↵ distinguished from an express contract or express warranty, really is in all cases founded on the presumed intention of the parties, and upon reason. The implication which the law draws from what must obviously have been the intention of the parties, the law draws with the object of giving efficacy to the transaction and preventing such a failure of consideration as cannot have been within the contemplation of either side; and I believe if one were to take all the cases, and they are many, of implied warranties or covenants in law, it will be found that in all of them the law is raising an implication from the presumed intention of the parties with the object of giving to the transaction such efficacy as both parties must have intended that at all events it should have. In business transactions such as this, what the law desires to effect by the implication is to give such business efficacy to the transaction as must have been intended at all events by both parties who are business men; not to impose on one side all the perils of the transaction, or to emancipate one side from all the chances of failure, but to make each party promise in law as much, at all events, as it must have been in the contemplation of both parties that he should be responsible for in respect of those perils or chances.

Now what did each party in a case like this know? For if we are examining into their presumed intention we must examine into their minds as to what the transaction was. Both parties knew that this jetty was let out for hire, and knew that it could only be used under the contract by the ship taking the ground. They must have known that it was by grounding that she used the jetty; in fact, except so far as the transport to the jetty of the cargo in the ship was concerned, they must have known, both of them, that unless the ground was safe the ship would be simply buying an

opportunity of danger, and that all consideration would fail unless some care had been taken to see that the ground was safe. In fact the business of the jetty could not be carried on except upon such a basis. The parties also knew that with regard to the safety of the ground outside the jetty the shipowner could know nothing at all, and the jetty owner might with reasonable care know everything. The owners of the jetty, or their servants, were there at high and low tide, and with little trouble they could satisfy themselves, in case of doubt, as to whether the berth was reasonably safe. The ship's owner, on the other hand, had not the means of verifying the state of the jetty, because the berth itself opposite the jetty might be occupied by another ship at any moment.

Now the question is how much of the peril of the safety of this berth is it necessary to assume that the shipowner and the jetty owner intended respectively to bear—in order that such a minimum of efficacy should be secured for the transaction, as both parties must have intended it to bear? Assume that the berth outside had been absolutely under the control of the owners of the jetty, that they could have repaired it and made it fit for the purpose of the unloading and the loading. If this had been the case, then the case of *The Mersey Docks Trustees* v. *Gibbs* Law Rep 1 HL 93 shews that those who owned the jetty, who took money for the use of the jetty, and who had under their control the locus in quo, would have been bound to take all reasonable care to prevent danger to those who were using the jetty—either to make the berth outside good, or else not to invite ships to go there—either to make the berth safe, or to advise persons not to go there. But there is a distinction in the present instance. The berth outside the jetty was not under the actual control of the jetty owners. It is in the bed of the river, and it may be said that those who owned the jetty had no duty cast upon them by statute or common law to repair the bed of the river, and that they had no power to interfere with the bed of the river unless under the licence of the Conservators. Now it does make a difference, it seems to me, where the entire control of the locus in quo—be it canal, or be it dock, or be it river berth—is not under the control of the persons who are taking toll for accommodation which involves its user,
p. 350 and, to a certain extent, the ↵ view must be modified of the necessary implication which the law would make about the duties of the parties receiving the remuneration. This must be done exactly for the reason laid down by Lord Holt in his judgment in *Coggs* v. *Bernard* Ld Raym 909, where he says 'it would be unreasonable to charge persons with a trust further than the nature of the thing puts it in their power to perform'. Applying that modification, which is one of reason, to this case, it may well be said that the law will not imply that the persons who have not the control of the place have taken reasonable care to make it good, but it does not follow that they are relieved from all responsibility. They are on the spot. They must know that the jetty cannot be used unless reasonable care is taken, if not to make it safe, at all events to see whether it is safe. No one can tell whether reasonable safety has been secured except themselves, and I think if they let out their jetty for use they at all events imply that they have taken reasonable care to see whether the berth, which is the essential part of the use of the jetty, is safe, and if it is not safe, and if they have not taken such reasonable care, it is their duty to warn persons with whom they have dealings that they have not done so. This is a business transaction as to which at any moment the parties may make any bargain they please, and either side may by the contract throw upon the other the burden of the unseen and existing danger. The question is what inference is to be drawn where the parties are dealing with each other on the assumption that the negotiations are to have some fruit, and where they say nothing about the burden of this kind of unseen peril, leaving the law to raise such inferences as are

> reasonable from the very nature of the transaction. So far as I am concerned I do not wish it to be understood that I at all consider this is a case of any duty on the part of the owners of the jetty to see to the access to the jetty being kept clear. The difference between access to the jetty and the actual use of the jetty seems to me, as Mr Finlay [counsel for the defendants] says it is, only a question of degree, but when you are dealing with implications which the law directs, you cannot afford to neglect questions of degree, and it is just that difference of degree which brings one case on the line and prevents the other from approaching it. I confess that on the broad view of the case I think that business could not be carried on unless there was an implication to the extent I have laid down, at all events in the case where a jetty like the present is so to be used, and, although the case is a novel one, and the cases which have been cited do not assist us, I feel no difficulty in drawing the inference that this case comes within the line.
>
> ***Lord Esher MR*** and ***Fry LJ*** delivered concurring judgments.

Commentary

The Moorcock is an important case for two reasons. The first relates to the source of the implied term. Bowen LJ attributed it to the 'presumed intention of the parties'. In this way he avoided the conclusion that the court was making the contract for the parties. Instead, the court stated that it was giving effect to the intention of the parties, albeit that the intention was presumed rather than express. However, it should be noted that Bowen LJ does not rest the implication of terms solely upon the 'presumed intention of the parties'. He adds that it is also based 'upon reason'. This appears to suggest a wider basis for the implication of terms, a point to which we shall return. The second point relates to the test put forward by Bowen LJ. It is one based on the need to give 'business efficacy' to the transaction. This has been interpreted subsequently as a test that is based on necessity rather than reasonableness. In other words, the court does not imply a term into the
p. 351 contract on the basis ↵ that it is, in the opinion of the court, reasonable to do so. The court implies a term into the contract on the basis that it is necessary to do so in order to make the contract work. That said, was the term implied in *The Moorcock* one that was necessary to give efficacy to the contract? Could the contract not have worked without such a term? The issue before the court was, in essence, who was to take the risk of the bed of the river being unsuitable for the vessel. Business efficacy does not seem to require that the risk be allocated to one party or the other. Nevertheless, the court took the view that business efficacy supported the implication of a term to the effect that the defendants had undertaken to exercise reasonable care to ascertain that the river bed adjoining the jetty was in such a condition as not to cause injury to the vessel.

In the years following *The Moorcock* the necessity test established itself in the case-law. Two famous judicial statements demonstrate this. The first is taken from the judgment of Scrutton LJ in *Reigate* v. *Union Manufacturing Co (Ramsbottom) Ltd* [1918] 1 KB 592 when he stated (at p. 605):

> A term can only be implied if it is necessary in the business sense to give efficacy to the contract; that is, if it is such a term that it can confidently be said that if at the time the contract was being negotiated some one had said to the parties, 'What will happen in such a case', they would both have replied, 'Of course, so and so will happen; we did not trouble to say that; it is too clear'. Unless the Court comes to some such conclusion as that, it ought not to imply a term which the parties themselves have not expressed.

The second example is a passage from the judgment of MacKinnon LJ in *Shirlaw* v. *Southern Foundries (1926) Ltd* [1939] 2 KB 206 when he said (at p. 227):

> I recognize that the right or duty of a Court to find the existence of an implied term or implied terms in a written contract is a matter to be exercised with care; and a Court is too often invited to do so upon vague and uncertain grounds. Too often also such an invitation is backed by the citation of a sentence or two from the judgment of Bowen LJ in *The Moorcock* (1889) 14 PD 64. They are sentences from an extempore judgment as sound and sensible as all the utterances of that great judge; but I fancy that he would have been rather surprised if he could have foreseen that these general remarks of his would come to be a favourite citation of a supposed principle of law, and I even think that he might sympathize with the occasional impatience of his successors when *The Moorcock* is so often flushed for them in that guise.
>
> For my part, I think that there is a test that may be at least as useful as such generalities. If I may quote from an essay which I wrote some years ago, I then said: 'Prima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common "Oh, of course!"'

This test has become known as the 'officious bystander' test and it emphasizes the fact that the test to be applied by the court is one of necessity, not reasonableness. The significance of these various formulations and the subsequent development of the law were considered by Lord Neuberger in the following case, which is now the leading modern decision on the test to be applied when deciding whether or not to imply a term into a contract as a matter of fact.

p. 352 ***Marks and Spencer plc v. BNP Paribas Securities Services Trust Co (Jersey) Ltd***
[2015] UKSC 72, [2016] AC 742, Supreme Court

15. As Lady Hale pointed out in *Geys* v. *Société Générale* [2013] 1 AC 523, para 55, there are two types of contractual implied term. The first, with which this case is concerned, is a term which is implied into a particular contract, in the light of the express terms, commercial common sense, and the facts known to both parties at the time the contract was made. The second type of implied terms arises because, unless such a term is expressly excluded, the law (sometimes by statute, sometimes through the common law) effectively imposes certain terms into certain classes of relationship.

16. There have, of course, been many judicial observations as to the nature of the requirements which have to be satisfied before a term can be implied into a detailed commercial contract. They include three classic statements, which have been frequently quoted in law books and judgments. ...

> [He then set out extracts from the judgments of Bowen LJ in *The Moorcock*, Scrutton LJ in *Reigate* v. *Manufacturing Co (Ramsbottom) Ltd*, and MacKinnon LJ in *Shirlaw* v. *Southern Foundries (1926) Ltd*, all of which are set out earlier and continued]

17. Support for the notion that a term will only be implied if it satisfies the test of business necessity is to be found in a number of observations made in the House of Lords. Notable examples included ... Lord Wilberforce, Lord Cross, Lord Salmon and Lord Edmund-Davies in *Liverpool City Council* v. *Irwin* [1977] AC 239, 254, 258, 262 and 266 respectively [see 10.4.2]. ...

18. In the Privy Council case of *BP Refinery (Westernport) Pty Ltd* v. *President, Councillors and Ratepayers of the Shire of Hastings* (1977) 52 ALJR 20, [1977] UKPC 13, 26, Lord Simon (speaking for the majority, which included Viscount Dilhorne and Lord Keith) said that:

> '[F]or a term to be implied, the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that "it goes without saying"; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract.'

19. In *Philips Electronique Grand Public SA* v. *British Sky Broadcasting Ltd* [1995] EMLR 472, 481, Sir Thomas Bingham MR set out Lord Simon's formulation, and described it as a summary which 'distil[led] the essence of much learning on implied terms' but whose 'simplicity could be almost misleading'. Sir Thomas then explained that it was 'difficult to infer with confidence what the parties must have intended when they have entered into a lengthy and carefully-drafted contract but have omitted to make provision for the matter in issue', because 'it may well be doubtful whether the omission was the result of the parties' oversight or of their deliberate decision', or indeed the parties might suspect that 'they are

unlikely to agree on what is to happen in a certain … eventuality' and 'may well choose to leave the matter uncovered in their contract in the hope that the eventuality will not occur'. Sir Thomas went on to say this at p. 482:

> 'The question of whether a term should be implied, and if so what, almost inevitably arises after a crisis has been reached in the performance of the contract. So the court comes to the task of implication with the benefit of hindsight, and it is tempting for the court then to fashion a term which will reflect the merits of the situation as they then appear. Tempting, but wrong. [He then quoted the observations of Scrutton LJ
> p. 353 in *Reigate*, and continued] [I]t is ↵ not enough to show that had the parties foreseen the eventuality which in fact occurred they would have wished to make provision for it, unless it can also be shown either that there was only one contractual solution or that one of several possible solutions would without doubt have been preferred. …'

…

21. In my judgment, the judicial observations so far considered represent a clear, consistent and principled approach. It could be dangerous to reformulate the principles, but I would add six comments on the summary given by Lord Simon in *BP Refinery* as extended by Sir Thomas Bingham in *Philips*. … First, in *Equitable Life Assurance Society* v. *Hyman* [2002] 1 AC 408, 459, Lord Steyn rightly observed that the implication of a term was 'not critically dependent on proof of an actual intention of the parties' when negotiating the contract. If one approaches the question by reference to what the parties would have agreed, one is not strictly concerned with the hypothetical answer of the actual parties, but with that of notional reasonable people in the position of the parties at the time at which they were contracting. Secondly, a term should not be implied into a detailed commercial contract merely because it appears fair or merely because one considers that the parties would have agreed it if it had been suggested to them. Those are necessary but not sufficient grounds for including a term. However, and thirdly, it is questionable whether Lord Simon's first requirement, reasonableness and equitableness, will usually, if ever, add anything: if a term satisfies the other requirements, it is hard to think that it would not be reasonable and equitable. Fourthly, as Lord Hoffmann I think suggested in *Attorney General of Belize* v. *Belize Telecom Ltd* [2009] 1 WLR 1988, para 27, although Lord Simon's requirements are otherwise cumulative, I would accept that business necessity and obviousness, his second and third requirements, can be alternatives in the sense that only one of them needs to be satisfied, although I suspect that in practice it would be a rare case where only one of those two requirements would be satisfied. Fifthly, if one approaches the issue by reference to the officious bystander, it is 'vital to formulate the question to be posed by [him] with the utmost care', to quote from Lewison, *The Interpretation of Contracts* 5th ed (2011), para 6.09. Sixthly, necessity for business efficacy involves a value judgment. It is rightly common ground on this appeal that the test is not one of 'absolute necessity', not least because the necessity is judged by reference to business efficacy. It may well be that a more helpful way of putting

Lord Simon's second requirement is, as suggested by Lord Sumption in argument, that a term can only be implied if, without the term, the contract would lack commercial or practical coherence.

22. Before leaving this issue of general principle, it is appropriate to refer a little further to *Belize Telecom*, where Lord Hoffmann suggested that the process of implying terms into a contract was part of the exercise of the construction, or interpretation, of the contract. In summary, he said at para 21 that '[t]here is only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?'. There are two points to be made about that observation.

23. First, the notion that a term will be implied if a reasonable reader of the contract, knowing all its provisions and the surrounding circumstances, would understand it to be implied is quite acceptable, provided that (i) the reasonable reader is treated as reading the contract at the time it was made and (ii) he would consider the term to be so obvious as to go without saying or to be necessary for business efficacy. (The difference between what the reasonable reader would understand and what the parties, acting reasonably, would agree, appears to me to be a notional distinction without a practical difference.) The first proviso emphasises that the
p. 354 question whether a term is implied is to be judged at the date the contract is made. The second proviso is important because otherwise Lord Hoffmann's formulation may be interpreted as suggesting that reasonableness is a sufficient ground for implying a term. (For the same reason, it would be wrong to treat Lord Steyn's statement in *Equitable Life Assurance Society* v. *Hyman* [2002] 1 AC 408, 459 that a term will be implied if it is 'essential to give effect to the reasonable expectations of the parties' as diluting the test of necessity. That is clear from what Lord Steyn said earlier on the same page, namely that '[t]he legal test for the implication of … a term is … strict necessity', which he described as a 'stringent test'.)

24. It is necessary to emphasise that there has been no dilution of the requirements which have to be satisfied before a term will be implied, because it is apparent that *Belize Telecom* has been interpreted by both academic lawyers and judges as having changed the law … the law governing the circumstances in which a term will be implied into a contract remains unchanged following *Belize Telecom.*

25. The second point to be made about what was said in *Belize Telecom* concerns the suggestion that the process of implying a term is part of the exercise of interpretation. …

26. I accept that both (i) construing the words which the parties have used in their contract and (ii) implying terms into the contract, involve determining the scope and meaning of the contract. However, Lord Hoffmann's analysis in *Belize Telecom* could obscure the fact that construing the words used and implying additional words are different processes governed by different rules.

27. Of course, it is fair to say that the factors to be taken into account on an issue of construction, namely the words used in the contract, the surrounding circumstances known to both parties at the time of the contract, commercial common sense, and the reasonable reader or reasonable parties, are also taken into account on an issue of implication. However, that does not mean that the exercise of implication should be properly classified as part of the exercise

of interpretation, let alone that it should be carried out at the same time as interpretation. When one is implying a term or a phrase, one is not construing words, as the words to be implied are *ex hypothesi* not there to be construed; and to speak of construing the contract as a whole, including the implied terms, is not helpful, not least because it begs the question as to what construction actually means in this context.

28. In most, possibly all, disputes about whether a term should be implied into a contract, it is only after the process of construing the express words is complete that the issue of an implied term falls to be considered. Until one has decided what the parties have expressly agreed, it is difficult to see how one can set about deciding whether a term should be implied and if so what term. This appeal is just such a case. Further, given that it is a cardinal rule that no term can be implied into a contract if it contradicts an express term, it would seem logically to follow that, until the express terms of a contract have been construed, it is, at least normally, not sensibly possible to decide whether a further term should be implied. Having said that, I accept Lord Carnwath's point in para 71 to the extent that in some cases it could conceivably be appropriate to reconsider the interpretation of the express terms of a contract once one has decided whether to imply a term, but, even if that is right, it does not alter the fact that the express terms of a contract must be interpreted before one can consider any question of implication.

29. In any event, the process of implication involves a rather different exercise from that of construction. As Sir Thomas Bingham trenchantly explained in *Philips* at p 481:

> 'The courts' usual role in contractual interpretation is, by resolving ambiguities or reconciling apparent inconsistencies, to attribute the true meaning to the language
p. 355 in which the ↵ parties themselves have expressed their contract. The implication of contract terms involves a different and altogether more ambitious undertaking: the interpolation of terms to deal with matters for which, *ex hypothesi*, the parties themselves have made no provision. It is because the implication of terms is so potentially intrusive that the law imposes strict constraints on the exercise of this extraordinary power.'

...

31. It is true that *Belize Telecom* was a unanimous decision of the Judicial Committee of the Privy Council and that the judgment was given by Lord Hoffmann, whose contributions in so many areas of law have been outstanding. However, it is apparent that Lord Hoffmann's observations in *Belize Telecom*, paras 17–27 are open to more than one interpretation on the two points identified in paras 23–24 and 25–30 above, and that some of those interpretations are wrong in law. In those circumstances, the right course for us to take is to say that those observations should henceforth be treated as a characteristically inspired discussion rather than authoritative guidance on the law of implied terms.

Commentary

The principal significance of the decision of the Supreme Court lies in its clear affirmation that the test for the implication of a term into a contract as a matter of fact is based upon necessity, not reasonableness (see [24] and also the judgments of Lord Carnwath and Lord Clarke at [66] and [77] respectively). It is not enough to show that the term is a reasonable one for it to be implied into the contract ([23]), nor does it suffice to show that the term appears to be a fair one to have implied or that it is one that the parties might have agreed to had it been suggested to them ([21]). The test remains one of necessity, albeit not 'absolute necessity' but whether, without the term, the contract would lack commercial or practical coherence ([21]) or whether it is necessary to imply the term 'in order to make the contract work' (see Lord Clarke at [77]). The need to re-assert that the test is one based on necessity arose principally because some judges and commentators believed that Lord Hoffmann in *Attorney-General of Belize* v. *Belize Telecom Ltd* [2009] UKPC 10, [2009] 1 WLR 1988 had attempted to liberalize the rules relating to the implication of terms into a contract ([24]). It is unlikely that this was the intention of Lord Hoffmann but, in any event, the point has now been established beyond all doubt that the test remains one based on necessity and this has been acknowledged in subsequent case-law where the courts have affirmed the strict requirements which must be satisfied before a term will be implied as a matter of fact into a contract, particularly a written contract of some length which has been negotiated with the benefit of legal advice (see, for example, *Impact Funding Solutions Ltd* v. *Barrington Support Services Ltd (AIG Europe Ltd, Third Party)* [2016] UKSC 57, [2017] AC 73, [31] and *Ali* v. *Petroleum Company of Trinidad and Tobago* [2017] UKPC 2, [2017] ICR 531, [5]). When deciding whether the term is necessary to make the contract work or to give the contract practical or commercial coherence, the court must endeavour to put itself in the position of the parties at the time of entry into the contract. It is not appropriate for the court to rely on hindsight and to imply a term into a contract because it appears to the court to be fair or because it is believed that the parties would have agreed to the term if it had been suggested to them (*Bou-Simon* v. *BGC Brokers LP* [2018] EWCA Civ 1525, [2019] 1 All ER (Comm) 955, [12]). It is also no easy task to demonstrate that without the implied term the
p. 356 contract lacks practical or commercial ↵ coherence. In particular, the fact that the contract has turned out to be a less advantageous bargain for one of the parties is not sufficient to establish that the contract is practically or commercially incoherent without the suggested implied term (*Yoo Design Services Ltd* v. *Iliv Realty Pte Ltd* [2021] EWCA Civ 560).

The second point of note which emerges from the decision of the Supreme Court relates to the doubt cast upon the proposition, central to the judgment of Lord Hoffmann in *Belize*, that 'the process of implying a term is part of the exercise of interpretation'. Lord Neuberger's criticisms (at [25]–[31]), combined with his pointed remark that Lord Hoffmann's judgment was to be considered as a 'characteristically inspired discussion' rather than 'authoritative guidance' ([31]) should, notwithstanding Lord Carnwath's continuing support for the approach of Lord Hoffmann (at [74]), consign Lord Hoffmann's analysis to a mere footnote in the development of the law relating to implied terms. Support for the latter proposition can be derived from *Trump International Golf Club Scotland Ltd* v. *The Scottish Ministers* [2015] UKSC 74, [2016] 1 WLR 85, where Lord Hodge stated (at [35]) that 'interpretation is not the same as the implication of terms' and that 'interpretation of the words of a document is the precursor of implication'. Lord Mance was, however, more circumspect in his observations on the relationship between implication and interpretation. Thus he observed (at [42]) that he 'would not encourage advocates or courts to adopt too rigid or sequential an approach to the processes of consideration of the express terms and of consideration of the possibility of an implication' and concluded (at [44]) that it appears to be 'helpful' to recognize 'in broad terms' that 'the processes of consideration of express

terms and of the possibility that an implication exists are all part of an overall, and potentially iterative, process of objective interpretation of the contract as a whole'. Notwithstanding the tentative support of Lord Mance for the approach of Lord Hoffmann, it is suggested that Lord Hodge is correct to state that interpretation is the precursor to implication. In other words, the court must first ascertain the meaning of the express terms of the contract, and it is only once that task has been completed that the court should turn to the question whether or not it is appropriate to imply a term into the contract. The sequential nature of this exercise derives support from the rule that the courts cannot imply a term into a contract which is inconsistent, whether linguistically or in terms of substance, with the express terms of the contract (*Irish Bank Resolution Corporation Ltd* v. *Camden Markets Holding Corp* [2017] EWCA Civ 7). The latter rule suggests that the court must first ascertain the scope of the express terms of the contract because it is only once that task has been completed that the court can meaningfully ask whether the proposed implied term is inconsistent with the express terms of the contract (*Duval* v. *11–13 Randolph Crescent Ltd* [2020] UKSC 18, [2020] AC 845, [26] and [51]). Were the two processes of interpretation and implication to be carried out simultaneously the result would in all probability be confusion rather than clarity.

Although interpretation and implication are different processes which are governed by different rules, the Privy Council in *Byron* v. *Eastern Caribbean Amalgamated Bank* [2019] UKPC 16, [22] recognized that the factors taken into account in each process may be the same. Thus both have regard to the words used, the surrounding circumstances known to both parties at the time of entry into the contract, and considerations of commercial common sense. But it does not follow from the existence of common factors that the processes are identical. As Lady Hale put it (at [22]), construing the words of the contract 'involves deciding what the parties meant by what they did say', while implication 'involves deciding whether they would have said
p. 357 something that they did not in fact say had the ↵ matter occurred to them'. On this basis 'until one has decided what the parties meant by what they did say, it will be difficult to set out about deciding what they would have said'.

However, in the case where the contract is made orally or by conduct it may not be so easy to draw such a clear line of distinction between interpretation and implication. Thus in *Wells* v. *Devani* [2019] UKSC 4, [2020] AC 129 (on which see 4.1) Lord Kitchin stated (at [28]) that 'in most cases' a court will only consider the implication of a term into a contract after it has completed the process of interpreting the express words of the agreement and, to similar effect, Lord Briggs stated (at [59]) that 'very often' interpretation will precede implication. A factor which may have persuaded Lord Kitchin and Lord Briggs to express themselves in more qualified terms is that the contract in *Wells* was made partly orally and partly by conduct. Further, the term which was in dispute in that case was not agreed as part of the oral conversation between the parties but was based on the conduct of the parties and the practice of the property market more generally. In such a case, it may not be entirely easy to ascertain whether the term is identified as a matter of interpretation of what was said and done by the parties or whether it is based on the implication of a term into the contract to fill the gap in what had been expressly agreed between the parties (although it was observed by Lord Leggatt in *Barton* v. *Morris* [2023] UKSC 3, [2023] 2 WLR 269, [154] that the approach adopted in *Devani* is 'problematic' because of the conclusion in *Marks and Spencer* that 'interpretation and implication must be kept distinct and that the process of interpretation is limited to ascertaining the meaning of the express terms of the contract'). However, these difficulties are not so acute in the context of a written contract which has been agreed between the parties where, for the reasons given by Lady Hale in *Byron*, a distinction can meaningfully be drawn between interpretation and implication.

The third point to note regarding the decision of the Supreme Court relates to its application of the principles of law to the facts of the case. The question before the court was whether it should imply into a lease a term which entitled the lessee to recover that part of an advance payment of rent which related to a period after the exercise by the lessee of a break period in the lease. The lessee paid the full quarter's rent due on 25 December 2011 but on 24 January 2012 exercised its right under the break clause to determine the lease. The lessee then sought to recover the rent attributable to the period between 24 January 2012 and the end of the quarter, being 24 March 2012. The Supreme Court declined to imply the proposed term into the lease and it did so for two principal reasons. First, the lease was a very detailed document which had been entered into between two substantial and experienced parties and had been negotiated and drafted by expert solicitors ([38]). Further, the lease made provision for a number of contingencies, but it did not make provision for the return of the balance of an advance payment of rent in the circumstances of this particular case ([39]). Secondly, the existence of such an implied term was not supported by 'the general attitude of the law to the apportionability of rent payable in advance' ([42]). On the contrary, the long-established rule of the common law is that rent, whether payable in arrear or in advance, is not apportionable in time. Given that this was the background rule of law and the parties' expert advisors had not seen fit to insert such a term expressly into the contract, the Supreme Court declined to imply the term.

The final point to note is that Lord Neuberger affirmed the continuing importance of the distinction between a term implied in law and a term implied in fact ([15]). Cases in which it is sought to imply a term into a particular type of contract as a matter of law raise rather more difficult issues, to which we now turn.

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10.4.2 Terms Implied in Law

The basis on which terms are implied into contracts as a matter of law has given rise to considerable difficulty. It would appear that the test applied by the courts in this context is less rigorous than in the context of terms implied in fact, but the difference would appear to be one of degree, not kind. The controversy that exists in this area of law can best be seen by examining one of the leading cases, *Liverpool City Council* v. *Irwin*, a case which is notable for the contrast between the reasoning of Lord Denning in the Court of Appeal and Lord Wilberforce in the House of Lords.

Liverpool City Council v. Irwin

[1976] QB 319, Court of Appeal; [1977] AC 239, House of Lords

The defendant tenants lived in Haigh Heights, a tower block in the district of Everton in Liverpool. The plaintiffs, Liverpool City Council, were their landlords. The defendants stopped paying rent for their maisonette on the ninth and tenth floors of the tower block. The plaintiffs brought an action for possession. The defendants counterclaimed for nominal damages of £10 for (i) breach of the landlord's duty to repair and maintain the common parts of the building retained by the plaintiffs, namely the lifts, staircases, passages, rubbish chutes, playground, etc. and in relation to the maisonette itself; (ii) breach of the covenant for quiet enjoyment; and (iii) breach of the implied covenant in section 32(1) of the Housing Act 1961, specifying defects in and disrepair of the water closet cisterns, damp, defective door frames, and related matters. The plaintiffs denied the existence of any implied obligation to keep the common parts of the building in repair and they also denied breaches of the covenant for quiet enjoyment and of the covenant implied under section 32(1). The trial judge held that the plaintiffs were in breach of all three duties and, while he granted the council an order for possession, he awarded the defendants nominal damages of £10.

The plaintiffs appealed to the Court of Appeal. The Court of Appeal allowed their appeal. It held by a majority (Lord Denning MR dissenting) that the plaintiffs were not under any contractual duty to keep the common parts in repair and, further, that they were not in breach of the implied covenant in section 32(1) of the Housing Act 1961. The majority refused to imply a term into the tenancy contract to the effect that the plaintiffs would keep the common parts in repair on the ground that it was not necessary to imply such an onerous obligation into the tenancy agreement in order to give it business efficacy. Lord Denning took a different approach. He held that the plaintiffs were subject to an implied duty to take reasonable care to keep the common parts reasonably fit for use by the tenants but that the tenants had failed to prove that the plaintiffs had not exercised reasonable care. He therefore concurred in the result, namely that the defendants were not entitled to recover damages from the plaintiffs.

The defendants appealed to the House of Lords. The House of Lords allowed their appeal in part. Their appeal was successful in relation to their claim pursuant to section 32(1) of the Housing Act 1961 and it was held that they were entitled to nominal damages of £5. In relation to their claim that the plaintiffs were in breach of their duty to keep the common parts of the building in repair, the House of Lords held that the plaintiffs were subject to an obligation to take reasonable care to do so but that, on the facts, they had not breached that duty.

Two extracts from the case are set out here. The first is taken from the dissenting judgment of Lord Denning MR in the Court of Appeal and the second from the speech of Lord ↵ Wilberforce in the House of Lords. The extracts do not deal with the scope of section 32(1) of the Housing Act 1961. They deal only with the defendants' submission that the plaintiffs were in breach of their implied duty to keep the common parts of the building in repair.

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Lord Denning MR

It is often said that the courts only imply a term in a contract when it is reasonable and necessary to do so in order to give business efficacy to the transaction: see *The Moorcock* (1889) 14 PD 64, 68. (Emphasis is put on the word 'necessary': *Reigate* v. *Union Manufacturing Co (Ramsbottom) Ltd* [1918] 1 KB 592, 605.) Or when it is obvious that both parties must have intended it: so obvious indeed that if an officious bystander had asked them whether there was to be such a term, both would have suppressed it testily: 'Yes, of course': see *Shirlaw* v. *Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227.

Those expressions have been repeated so often that it is with some trepidation that I venture to question them. I do so because they do not truly represent the way in which the courts act. Let me take some instances. There are stacks of them. Such as the terms implied by the courts into a contract for the sale of goods—*Jones* v. *Just* (1868) LR 3 QB 197: or the hire of goods—*Asley Industrial Trust Ltd* v. *Grimley* [1963] 1 WLR 584: into a contract for work and materials—*Young & Marten Ltd* v. *McManus Childs Ltd* [1969] 1 AC 454: or into a contract for letting an unfurnished house—*Hart* v. *Windsor* (1843) 12 M & W 68: or a furnished house—*Collins* v. *Hopkins* [1923] 2 KB 617: or into the carriage of a passenger by railway: see *Readhead* v. *Midland Railway Co* (1869) LR 4 QB 379: or to enter on premises: see *Francis* v. *Cockrell* (1870) LR 5 QB 501: or to buy a house in course of erection: see *Hancock* v. *B W Brazier (Anerley) Ltd* [1966] 1 WLR 1317.

If you read the discussion in those cases, you will see that in none of them did the court ask: what did both parties intend? If asked, each party would have said he never gave it a thought: or the one would have intended something different from the other. Nor did the court ask: Is it necessary to give business efficacy to the transaction? If asked, the answer would have been: 'It is reasonable, but it is not necessary'. The judgments in all those cases show that the courts implied a term according to whether or not it was reasonable in all the circumstances to do so. Very often it was conceded that there was some implied term. The only question was: 'What was the extent of it?' Such as, was it an absolute warranty of fitness, or only a promise to use reasonable care? That cannot be solved by inquiring what they both intended, or into what was necessary. But only into what was reasonable. This is to be decided as matter of law, not as matter of fact. Lord Wright pulled the blinkers off our eyes when he said in 1935 to the Holdsworth Club:

> 'The truth is that the court … decides this question in accordance with what seems to be just or reasonable in its eyes. The judge finds in himself the criterion of what is reasonable. The court is in this sense making a contract for the parties—though it is almost blasphemy to say so.' (Lord Wright of Durley, *Legal Essays and Addresses* (1939), p. 259.)

In 1956, Lord Radcliffe put it elegantly when he said of the parties to an implied term:

> 'their actual persons should be allowed to rest in peace. In their place there rises the figure of the fair and reasonable man. And the spokesman of the fair and reasonable man, who represents after all no more than the anthropomorphic conception of justice, is and must be the court itself': see *Davis Contractors Ltd* v. *Fareham Urban District Council* [1956] AC 696, 728.

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In 1969, Lord Reid put it simply when he said: ' ... no warranty ought to be implied in a contract unless it is in all the circumstances reasonable,' see *Young & Marten Ltd* v. *McManus Childs Ltd* ↵ [1969] 1 AC 454, 465: and Lord Upjohn echoed it when he said, at p. 471, that the implied warranty was 'imposed by law'.

Is there a term to be implied in this tenancy about the lifts and staircases and other common parts?. ...

[He considered the case-law and other authorities and concluded]

It is clearly the duty of the landlord, not only to take care to keep the lifts and staircase safe, but also to take care to keep them reasonably fit for the use of the tenant and his visitors. If the lifts break down, the landlord ought to repair them. If the lights on the staircase fail, the landlord ought to replace them.

[He then considered whether or not there had been a breach of the duty and concluded that, on the facts, there had been no breach.]

Lord Wilberforce

We have then a contract which is partly, but not wholly, stated in writing. In order to complete it, in particular to give it a bilateral character, it is necessary to take account of the actions of the parties and the circumstances. As actions of the parties, we must note the granting of possession by the landlords and reservation by them of the 'common parts'—stairs, lifts, chutes, etc. As circumstances we must include the nature of the premises, viz., a maisonette for family use on the ninth floor of a high block, one which is occupied by a large number of other tenants, all using the common parts and dependent upon them, none of them having any expressed obligation to maintain or repair them.

To say that the construction of a complete contract out of these elements involves a process of 'implication' may be correct; it would be so if implication means the supplying of what is not expressed. But there are varieties of implications which the courts think fit to make and they do not necessarily involve the same process. Where there is, on the face of it, a complete, bilateral contract, the courts are sometimes willing to add terms to it, as implied terms: this is very common in mercantile contracts where there is an established usage: in that case the courts are spelling out what both parties know and would, if asked, unhesitatingly agree to be part of the bargain. In other cases, where there is an apparently complete bargain, the courts are willing to add a term on the ground that without it the contract will not work—this is the case, if not of *The Moorcock* (1889) 14 PD 64 itself on its facts, at least of the doctrine of *The Moorcock* as usually applied. This is, as was pointed out by the majority in the Court of Appeal, a strict test—though the degree of strictness seems to vary with the current legal trend—and I think that they were right not to accept it as applicable here. There is a third variety of implication, that which I think Lord Denning MR favours, or at least did favour in this case, and that is the implication of reasonable terms. But though I agree with many of

his instances, which in fact fall under one or other of the preceding heads, I cannot go so far as to endorse his principle; indeed, it seems to me, with respect, to extend a long, and undesirable, way beyond sound authority.

The present case, in my opinion, represents a fourth category, or I would rather say a fourth shade on a continuous spectrum. The court here is simply concerned to establish what the contract is, the parties not having themselves fully stated the terms. In this sense the court is searching for what must be implied.

What then should this contract be held to be? There must first be implied a letting, that is, a grant of the right of exclusive possession to the tenants. With this there must, I would suppose, be implied a
p. 361 covenant for quiet enjoyment, as a necessary incident of the letting. ↵ The difficulty begins when we consider the common parts. We start with the fact that the demise is useless unless access is obtained by the staircase; we can add that, having regard to the height of the block, and the family nature of the dwellings, the demise would be useless without a lift service; we can continue that, there being rubbish chutes built into the structures and no other means of disposing of light rubbish, there must be a right to use the chutes. The question to be answered—and it is the only question in this case—is what is to be the legal relationship between landlord and tenant as regards these matters.

There can be no doubt that there must be implied (i) an easement for the tenants and their licensees to use the stairs, (ii) a right in the nature of an easement to use the lifts, (iii) an easement to use the rubbish chutes.

But are these easements to be accompanied by any obligation upon the landlord, and what obligation? There seem to be two alternatives. The first, for which the council contends, is for an easement coupled with no legal obligation, except such as may arise under the Occupiers' Liability Act 1957 as regards the safety of those using the facilities, and possibly such other liability as might exist under the ordinary law of tort. The alternative is for easements coupled with some obligation on the part of the landlords as regards the maintenance of the subject of them, so that they are available for use.

My Lords, in order to be able to choose between these, it is necessary to define what test is to be applied, and I do not find this difficult. In my opinion such obligation should be read into the contract as the nature of the contract itself implicitly requires, no more, no less: a test, in other words, of necessity. The relationship accepted by the corporation is that of landlord and tenant: the tenant accepts obligations accordingly, in relation inter alia to the stairs, the lifts and the chutes. All these are not just facilities, or conveniences provided at discretion: they are essentials of the tenancy without which life in the dwellings, as a tenant, is not possible. To leave the landlord free of contractual obligation as regards these matters, and subject only to administrative or political pressure, is, in my opinion, inconsistent totally with the nature of this relationship. The subject matter of the lease (high rise blocks) and the relationship created by the tenancy demand, of their nature, some contractual obligation on the landlord.

I do not think that this approach involves any innovation as regards the law of contract. The necessity to have regard to the inherent nature of a contract and of the relationship thereby established was stated in this House in *Lister* v. *Romford Ice and Cold Storage Co Ltd* [1957] AC 555. That was a case between master and servant and of a search for an 'implied term'. Viscount Simonds, at p. 579, makes a clear distinction between a search for an implied term such as might be necessary to give 'business efficacy' to the particular contract and a search, based on wider considerations, for such a term as the nature of the contract might call for, or as a legal incident of this kind of contract. If the search were for the former, he says, ' ... I should lose myself in the attempt to formulate it with the necessary precision'. (p. 576.) We see an echo of this in the present case, when the majority in the Court of Appeal, considering a 'business efficacy term'—i.e., a 'Moorcock' term (*The Moorcock*, 14 PD 64)—found themselves faced with five alternative terms and therefore rejected all of them. But that is not, in my opinion, the end, or indeed the object, of the search.

We have some guidance in authority for the kind of term which this typical relationship (of landlord and tenant in a multi-occupational dwelling) requires in *Miller* v. *Hancock* [1893] 2 QB 177. There Bowen LJ said, at pp. 180–181:

> 'The tenants could only use their flats by using the staircase. The defendant, therefore, when he let the flats, impliedly granted to the tenants an easement over the staircase, which he
> p. 362 retained in his own occupation, for the purpose of the enjoyment of the flats so let. Under ↵ those circumstances, what is the law as to the repairs of the staircase? It was contended by the defendant's counsel that, according to the common law, the person in enjoyment of an easement is bound to do the necessary repairs himself. That may be true with regard to easements in general, but it is subject to the qualification that the grantor of the easement may undertake to do the repairs either in express terms or by necessary implication. This is not the mere case of a grant of an easement without special circumstances. It appears to me obvious, when one considers what a flat of this kind is, and the only way in which it can be enjoyed, that the parties to the demise of it must have intended by necessary implication, as a basis without which the whole transaction would be futile, that the landlord should maintain the staircase, which is essential to the enjoyment of the premises demised, and should keep it reasonably safe for the use of the tenants, and also of those persons who would necessarily go up and down the stairs in the ordinary course of business with the tenants; because, of course, a landlord must know when he lets a flat that tradesmen and other persons having business with the tenant must have access to it. It seems to me that it would render the whole transaction inefficacious and absurd if an implied undertaking were not assumed on the part of the landlord to maintain the staircase so far as might be necessary for the reasonable enjoyment of the demised premises.'

Certainly that case, as a decision concerning a claim by a visitor, has been overruled: *Fairman* v. *Perpetual Investment Building Society* [1923] AC 74. But I cite the passage for its common sense as between landlord and tenant, and you cannot overrule common sense.

There are other passages in which the same thought has been expressed. ...

> These are all reflections of what necessarily arises whenever a landlord lets portions of a building for multiple occupation, retaining essential means of access.
>
> I accept, of course, the argument that a mere grant of an easement does not carry with it any obligation on the part of the servient owner to maintain the subject matter. The dominant owner must spend the necessary money, for example in repairing a drive leading to his house and the same principle may apply when a landlord lets an upper floor with access by a staircase: responsibility for maintenance may well rest on the tenant. But there is a difference between that case and the case where there is an essential means of access, retained in the landlord's occupation, to units in a building of multi-occupation, for unless the obligation to maintain is, in a defined manner, placed upon the tenants, individually or collectively, the nature of the contract, and the circumstances, require that it be placed on the landlord.
>
> It remains to define the standard. My Lords, if, as I think, the test of the existence of the term is necessity the standard must surely not exceed what is necessary having regard to the circumstances. To imply an absolute obligation to repair would go beyond what is a necessary legal incident and would indeed be unreasonable. An obligation to take reasonable care to keep in reasonable repair and usability is what fits the requirements of the case. Such a definition involves—and I think rightly—recognition that the tenants themselves have their responsibilities. What it is reasonable to expect of a landlord has a clear relation to what a reasonable set of tenants should do for themselves.
>
> I add one word as to lighting. In general I would accept that a grant of an easement of passage does not carry with it an obligation on the grantor to light the way. The grantee must take the way accompanied by the primeval separation of darkness from light and if he passes during the former must bring his own illumination. ... But the case may be different when the means of passage are constructed, and when natural light is either absent or insufficient. In such a case, to the extent that the easement is useless without some artificial light being provided, the grant should carry with it an obligation to take reasonable care to maintain adequate lighting—comparable to the obligation as
>
> p. 363 regards the lifts. To impose an absolute ↵ obligation would be unreasonable; to impose some might be necessary. We have not sufficient material before us to see whether the present case on its facts meets these conditions.
>
> I would hold therefore that the landlords' obligation is as I have described and in agreement, I believe, with your Lordships I would hold that it has not been shown in this case that there was any breach of that obligation. On the main point therefore I would hold that the appeal fails.
>
> My Lords, it will be seen that I have reached exactly the same conclusion as that of Lord Denning MR, with most of whose thinking I respectfully agree. I must only differ from the passage in which, more adventurously, he suggests that the courts have power to introduce into contracts any terms they think reasonable or to anticipate legislative recommendations of the Law Commission. A just result can be reached, if I am right, by a less dangerous route.

Commentary

The term sought to be implied into the tenancy agreement was one which related to the obligation of the landlord to keep the common parts of the tower block in repair and properly lit. Two principal issues arose in relation to this term. The first was whether or not such an obligation should be implied into the tenancy agreement at all and the second was, if such a term was to be implied, what was its scope? Was it an obligation to take reasonable care to keep the tower block in repair or was it a stricter obligation? The House of Lords concluded that a term was to be implied, that it required the plaintiffs to exercise reasonable care, and that, on the facts, the plaintiffs had not breached their duty.

Two further points are worthy of note. The first relates to the test to be applied when deciding whether or not to imply a term into the contract. Lord Denning advocated a test based on reasonableness but the House of Lords rejected his analysis. Lord Wilberforce did so in a rather restrained fashion in the final extracted paragraph of his speech. Some of the other judges in the House of Lords were more robust. Thus Lord Salmon stated (at p. 262):

> I cannot go so far as Lord Denning MR and hold that the courts have any power to imply a term into a contract merely because it seems reasonable to do so. Indeed, I think that such a proposition is contrary to all authority. To say, as Lord Reid said in *Young & Marten Ltd* v. *McManus Childs Ltd* [1969] 1 AC 454, 465, that ' ... no warranty ought to be implied in a contract unless it is in all the circumstances reasonable' is, in my view, quite different from saying that any warranty or term which is, in all the circumstances, reasonable ought to be implied in a contract. I am confident that Lord Reid meant no more than that unless a warranty or term is in all the circumstances reasonable there can be no question of implying it into a contract, but before it is implied much else besides is necessary, for example that without it the contract would be inefficacious, futile and absurd.

Lord Edmund-Davies stated (at p. 266) that the 'touchstone is always *necessity* and not merely *reasonableness*'. The difficulty with the 'necessity' analysis relates to its application to the facts. Was it really 'necessary' to imply such a term into the tenancy agreement? The reality would appear to be that the House of Lords was deciding a matter of social policy in relation to the extent of the obligations that are to be imposed upon landlords. Are they expected to keep the common parts in repair and to provide facilities to their tenants? If
p. 364 they are, what is the scope of their duty? Are they liable even in the case where the problems were
↵ caused by vandals who damaged the lifts and removed the light bulbs from the stairs? It is by no means clear that there is a 'necessary' answer to these questions. The point has been well made (Atiyah's *An Introduction to the Law of Contract* (6th edn, Oxford University Press, 2006), p. 161) in the following terms:

> [T]he difference between the judges on this point seems somewhat unreal ... It is obviously not strictly or literally *necessary* to have lifts in blocks of flats ten storeys high, though it would no doubt be exceedingly inconvenient not to have them. So 'necessary' really seems to mean 'reasonably necessary', and that must mean, 'reasonably necessary having regard to the context and the price'.

There is a second aspect to *Liverpool City Council* v. *Irwin* which merits further consideration and that relates to the question whether the term implied into the contract was a term implied in law or a term implied in fact. The case is generally regarded as an authority on terms implied in law, on the basis that the term that the landlord was under an obligation to take reasonable care to keep the common parts in repair was to be implied into all tenancy contracts between occupants of flats in tower blocks and their landlords. It was not a term that was peculiar to the relationship between this particular landlord and this particular tenant. However, it would appear that counsel for the defendants put his case on two different bases. First, he argued that such a term ought to be implied into all contracts of this type (in other words, it was a term implied in law) but he also relied upon the 'officious bystander' test. Lord Cross of Chelsea rejected (at p. 258) the submission that the term satisfied the 'officious bystander' test but nevertheless agreed (at p. 259) that the term was to be implied as a general incident of all contracts of this type. Thus Lord Cross seems to have concluded that a term could not be implied as a matter of fact but that it was appropriate to imply a term as a matter of law. If this is correct, it demonstrates that there is a difference between the test to be applied for terms implied in fact and the test applicable to terms implied in law.

The difficulty is that not all of the judges were as clear as Lord Cross on the distinction between terms implied in law and terms implied in fact. This point can be made in relation to Lord Denning's advocacy of the reasonableness test. While he stated that 'stacks' of cases cannot be reconciled with the necessity test most, if not all, of the cases that he cites in support of the proposition that reasonableness is the test applied by the courts, are cases concerned with terms implied in law (that is to say they are terms that are generally implied into all contracts of a particular type). Indeed, his failure to address the distinction between terms implied in law and terms implied in fact was criticized by Lord Cross of Chelsea (at pp. 257–258) in the following passage:

> When it implies a term in a contract the court is sometimes laying down a general rule that in all contracts of a certain type—sale of goods, master and servant, landlord and tenant and so on—some provision is to be implied unless the parties have expressly excluded it. In deciding whether or not to lay down such a prima facie rule the court will naturally ask itself whether in the general run of such cases the term in question would be one which it would be reasonable to insert. Sometimes, however, there is no question of laying down any prima facie rule applicable to all cases of a defined type but what the court is being in effect asked to do is to rectify a particular—often a very detailed—contract by inserting in it a term which the parties have not expressed. Here it is not enough for the court to say that the suggested term is a reasonable one the presence of which would make the contract a
> p. 365 better or fairer one; it ↵ must be able to say that the insertion of the term is necessary to give—as it is put—'business efficacy' to the contract and that if its absence had been pointed out at the time both parties—assuming them to have been reasonable men—would have agreed without hesitation to its insertion. The distinction between the two types of case was pointed out by Viscount Simonds and Lord Tucker in their speeches in *Lister* v. *Romford Ice and Cold Storage Co Ltd* [1957] AC 555, 579, 594, but I think that Lord Denning MR in proceeding—albeit with some trepidation—to 'kill off' MacKinnon LJ's 'officious bystander' (*Shirlaw* v. *Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227) must have overlooked it.

Lord Denning returned to his theme in *Shell UK Ltd* v. *Lostock Garage Ltd* [1976] 1 WLR 1187 when he sought to divide the cases into the following two categories:

> ### Implied terms
>
> The first category comprehends all those relationships which are of common occurrence, such as the relationship of seller and buyer, owner and hirer, master and servant, landlord and tenant, carrier by land or by sea, contractor for building works, and so forth. In all those relationships the courts have imposed obligations on one party or the other, saying they are implied terms. These obligations are not founded on the intention of the parties, actual or presumed, but on more general considerations … In such relationships the problem is not solved by asking: what did the parties intend? Or, would they have unhesitatingly agreed to it, if asked? It is to be solved by asking: has the law already defined the obligation or the extent of it? If so, let it be followed. If not, look to see what would be reasonable in the general run of such cases (see by Lord Cross of Chelsea at p. 570H): and then say what the obligation shall be. The House in *Liverpool City Council* v. *Irwin* [1976] 2 WLR 562 went through that very process. They examined the existing law of landlord and tenant, in particular that relating to easements, to see if it contained the solution to the problem; and, having found that it did not, they imposed an obligation on the landlord to use reasonable care. In these relationships the parties can exclude or modify the obligation by express words, but unless they do so, the obligation is a legal incident of the relationship which is attached by the law itself and not by reason of any implied term. …
>
> The second category comprehends those cases which are not within the first category. These are cases, not of common occurrence, in which from the particular circumstances a term is to be implied. In these cases the implication is based on an intention imputed to the parties from their actual circumstances: see *Luxor (Eastbourne) Ltd* v. *Cooper* [1941] AC 108, 137 per Lord Wright. Such an imputation is only to be made when it is necessary to imply a term to give efficacy to the contract and make it a workable agreement in such manner as the parties would clearly have done if they had applied their mind to the contingency which has arisen. These are the 'officious bystander' type of case: see *Lister* v. *Romford Ice & Cold Storage Co* [1957] AC 555, 594 per Lord Tucker. In such cases a term is not to be implied on the ground that it would be reasonable, but only when it is necessary and can be formulated with a sufficient degree of precision. This was the test applied by the majority of this court in *Liverpool City Council* v. *Irwin* [1976] QB 319, and they were emphatically upheld by the House on this point; see [1976] 2 WLR 562, 571D–H by Lord Cross of Chelsea; p. 578G–579A by Lord Edmund-Davies.
>
> There is this point to be noted about *Liverpool City Council* v. *Irwin*. In this court the argument was only about an implication in the second category. In the House of Lords that argument was not pursued. It was only the first category.

p. 366 ↵ In this passage Lord Denning affirms that the arguments advanced in *Irwin* encompassed both categories but he suggests that, in the House of Lords, the arguments were confined to the first category.

Where then did the decision of the House of Lords in *Liverpool City Council* v. *Irwin* leave the law? In the first place it re-affirmed that the test to be applied when deciding whether or not to imply a term is based on necessity and not simply on reasonableness. But it left some uncertainty in relation to terms implied in law because the term implied into the tenancy contract did not seem to be a necessary ingredient of all contracts

of this type. It might have been ‘reasonably necessary’ but not ‘necessary’. That the test for the implication of terms as a matter of law might be slightly less stringent than that applicable to terms implied in fact is evidenced by the fact that Lord Cross concluded that a term was not to be implied on the basis of the officious bystander test but that it was nevertheless appropriate to imply a term as a matter of law into all contracts of this type.

The basis on which the courts imply terms as a matter of law into contracts was further considered by the House of Lords in the following case:

Scally v. Southern Health and Social Services Board
[1992] 1 AC 294, House of Lords

> The plaintiffs brought an action against the defendants, their employers, for damages for breach of contract, negligence, and breach of statutory duty in failing adequately to advise and inform them about their contractual and statutory rights in relation to the superannuation[2] scheme of which they were members. In order to qualify for a full pension under the original scheme it was necessary for an employee to complete forty years of contributory service. In 1975 a change was made to the scheme which entitled employees to purchase additional years of contributing service at advantageous rates. However this right was only exercisable within twelve months of the change coming into force. The Department of Health and Social Services were initially given a discretion to extend the twelve-month period but that discretion was taken away in 1983 and replaced by a right given to the employee to purchase added years at any time until two years before an employee's retirement on fixed and progressively less favourable terms.
>
> The defendants failed to inform the plaintiffs of their right to purchase additional years of service at advantageous rates. The plaintiffs alleged that the defendants' failure to do so amounted to a breach of an implied term of the contract of employment, breach of a duty of care owed to the plaintiffs, and a breach of statutory duty. The House of Lords held that the defendants had not breached their statutory duty but that they were in breach of an implied term to take reasonable steps to inform the employees of the existence of their right to take steps to enhance their pension entitlement on advantageous terms. The defendants were therefore liable in damages to the plaintiffs and the case was remitted to the trial judge so that the losses suffered by the plaintiffs could be assessed.

Lord Bridge of Harwich

p. 367 Leaving aside the claim based on breach of statutory duty … it seems to me that the plaintiffs' common law claims can only succeed if the duty allegedly owed to them by their ↵ employers arose out of the contract of employment. If a duty of the kind in question was not inherent in the contractual relationship, I do not see how it could possibly be derived from the tort of negligence. …

In the instant case I believe that an attempt to analyse the issue in terms of the law of tort may be positively misleading. … The strong trend of recent authority has been to narrow the range of circumstances which the law of tort will recognise as sufficient to impose on one person a duty of care to protect another from damage which consists in purely economic loss. …

But if the issue is analysed in contract, the starting point is quite different. Here the express terms of the contract of employment confer a valuable right on the employee which is, however, contingent upon his taking certain action. Where that situation is known to the employer but not to the employee, will the law imply a contractual obligation on the employer to take reasonable steps to bring the existence of the contingent right to the notice of the employee? It is true that such an implication may have the consequence of sustaining a claim for purely economic loss. But this consideration would not furnish the essential reason for making the implication. If there is a basis for making the implication, it must lie rather in the consideration that the availability of the

contingent right was intended by those who drew up the terms of the contract for the benefit of the employee; but if the existence of the contingent right never comes to his attention, he cannot profit by it and it might, so far as he is concerned, just as well not exist.

The problem is a novel one which could not arise in the classical contractual situation in which all the contractual terms, having been agreed between the parties, must, ex hypothesi, have been known to both parties. But in the modern world it is increasingly common for individuals to enter into contracts, particularly contracts of employment, on complex terms which have been settled in the course of negotiations between representative bodies or organisations and many details of which the individual employee cannot be expected to know unless they are drawn to his attention. The instant case presents an example of this phenomenon arising in the context of the statutory provisions which regulate the operation of the health services in Northern Ireland. ...

[He set out the terms of these statutory provisions, rejected a submission made by the defendants that the obligation to notify the plaintiffs lay with the Department of Health and Social Services and not themselves and continued]

Will the law then imply a term in the contract of employment imposing such an obligation on the employer? The implication cannot, of course, be justified as necessary to give business efficacy to the contract of employment as a whole. I think there is force in the submission that, since the employee's entitlement to enhance his pension rights by the purchase of added years is of no effect unless he is aware of it and since he cannot be expected to become aware of it unless it is drawn to his attention, it is necessary to imply an obligation on the employer to bring it to his attention to render efficacious the very benefit which the contractual right to purchase added years was intended to confer. But this may be stretching the doctrine of implication for the sake of business efficacy beyond its proper reach. A clear distinction is drawn in the speeches of Viscount Simonds in *Lister* v. *Romford Ice and Cold Storage Co Ltd* [1957] AC 555 and Lord Wilberforce in *Liverpool City Council* v. *Irwin* [1977] AC 239 between the search for an implied term necessary to give business efficacy to a particular contract and the search, based on wider considerations, for a term which the law will imply as a necessary incident of a definable category of contractual relationship. If any implication is appropriate here, it is, I think, of this latter type. Carswell J accepted the submission that any formulation of an implied term of this kind which would be effective to sustain the plaintiffs' claims in this case must
p. 368 necessarily be too wide in its ambit to be acceptable as of general application. I believe ↵ however that this difficulty is surmounted if the category of contractual relationship in which the implication will arise is defined with sufficient precision. I would define it as the relationship of employer and employee where the following circumstances obtain: (1) the terms of the contract of employment have not been negotiated with the individual employee but result from negotiation with a representative body or are otherwise incorporated by reference; (2) a particular term of the contract makes available to the employee a valuable right contingent upon action being taken by him to avail himself of its benefit; (3) the employee cannot, in all the circumstances, reasonably be expected to be aware of the term unless it is drawn to his attention. I fully appreciate that the criterion to justify an implication of this kind is necessity, not reasonableness. But I take the view that it is not merely reasonable, but necessary, in the circumstances postulated, to imply an obligation on the employer to take reasonable steps to bring the term of the contract in question to the employee's attention, so

> that he may be in a position to enjoy its benefit. Accordingly I would hold that there was an implied term in each of the plaintiffs' contracts of employment of which the boards were in each case in breach.
>
> ***Lord Roskill***, ***Lord Goff of Chieveley***, ***Lord Jauncey of Tullichettle***, and ***Lord Lowry*** concurred.

Commentary

The implied term, as set out in the last paragraph of the speech of Lord Bridge, is narrowly drawn. As Professor Freedland has pointed out ((1992) 21 *ILJ* 135, 139):

> [T]he implied term was confined to the case where a particular term of the contract makes available to the employee a valuable right contingent upon action being taken by him to avail himself of its benefit, and where the employee cannot reasonably be expected to be aware of the term unless it is drawn to his attention. There are few if any other situations where this would occur in an employment context, except when the employee is in the position of an investor, for example in relation to employee share purchase schemes.

While the implied term recognized is narrow in scope, Lord Bridge does acknowledge that it is based 'on wider considerations' than whether the term is 'necessary to give business efficacy to a particular contract'. This being the case, there must be a difference between a term implied in law, at least in the sense of a term that is implied as a 'necessary incident of a definable category of contractual relationship', and a term that is implied as a matter of fact into a particular contractual relationship. That this is so can be demonstrated by reference to the cases concerned with the obligation of 'trust and confidence' that is implied into contracts of employment (and which is not implied into contracts of a purely commercial nature: *Chelsfield Advisers LLP* v. *Qatari Diar Real Estate Investment Co* [2015] EWHC 1322 (Ch)). The existence of this implied term was approved by the House of Lords in *Mahmud* v. *Bank of Credit and Commerce International SA* [1998] AC 20 where Lord Steyn stated (at pp. 45–46):

The implied term of mutual trust and confidence

The applicants do not rely on a term implied in fact. They do not therefore rely on an individualised term to be implied from the particular provisions of their employment contracts considered against
p. 369 their specific contextual setting. Instead they rely on a standardised ↵ term implied by law, that is, on a term which is said to be an incident of all contracts of employment: *Scally* v. *Southern Health and Social Services Board* [1992] 1 AC 294, 307B. Such implied terms operate as default rules. The parties are free to exclude or modify them. …

The employee's primary case is based on a formulation of the implied term that has been applied at first instance and in the Court of Appeal. It imposes reciprocal duties on the employer and employee. Given that this case is concerned with alleged obligations of an employer I will concentrate on its effect on the position of employers. For convenience I will set out the term again. It is expressed to impose an obligation that the employer shall not:

> 'without reasonable and proper cause, conduct itself in a manner calculated and likely to destroy or seriously damage the relationship of confidence and trust between employer and employee.'

… A useful anthology of the cases applying this term, or something like it, is given in *Sweet & Maxwell's Encyclopedia of Employment Law* (looseleaf ed), vol. 1, para 1.5107, pp. 1467–1470. The evolution of the term is a comparatively recent development. The obligation probably has its origin in the general duty of co-operation between contracting parties: *Hepple & O'Higgins, Employment Law*, 4th ed. (1981), pp. 134–135, paras. 291–292. The reason for this development is part of the history of the development of employment law in this century. The notion of a 'master and servant' relationship became obsolete. Lord Slynn of Hadley recently noted 'the changes which have taken place in the employer–employee relationship, with far greater duties imposed on the employer than in the past, whether by statute or by judicial decision, to care for the physical, financial and even psychological welfare of the employee': *Spring* v. *Guardian Assurance plc* [1995] 2 AC 296, 335B. A striking illustration of this change is *Scally's* case [1992] 1 AC 294 … where the House of Lords implied a term that all employees in a certain category had to be notified by an employer of their entitlement to certain benefits. It was the change in legal culture which made possible the evolution of the implied term of trust and confidence.

There was some debate at the hearing about the possible interaction of the implied obligation of confidence and trust with other more specific terms implied by law. It is true that the implied term adds little to the employee's implied obligations to serve his employer loyally and not to act contrary to his employer's interests. The major importance of the implied duty of trust and confidence lies in its impact on the obligations of the employer: Douglas Brodie, 'Recent Cases, Commentary, The Heart of the Matter: Mutual Trust and Confidence' (1996) 25 *ILJ* 121. And the implied obligation as formulated is apt to cover the great diversity of situations in which a balance has to be struck between an employer's interest in managing his business as he sees fit and the employee's interest in not being unfairly and improperly exploited.

> The evolution of the implied term of trust and confidence is a fact. It has not yet been endorsed by your Lordships' House. It has proved a workable principle in practice. It has not been the subject of adverse criticism in any decided cases and it has been welcomed in academic writings. I regard the emergence of the implied obligation of mutual trust and confidence as a sound development.

In the light of *Scally* and *Mahmud* it seems appropriate to conclude that the test applied by the courts in cases of terms implied in law is not based on necessity alone. It seems to be based on a slightly lower standard which entitles the court to take account of 'wider considerations'. That this is so can be demonstrated by reference to the following two decisions.

p. 370 ↵ The first is the decision of the Court of Appeal in *Paragon Finance plc* v. *Nash* [2001] EWCA Civ 1466, [2002] 1 WLR 685. The claimant made secured loans to the defendants in 1987 and 1990. Both agreements contained variable interest clauses. The claimant claimed possession from the defendants on the ground that the defendants were in arrears with their mortgage payments. The defendants defended the claim on a number of grounds. One of the issues before the Court of Appeal was whether or not the claimant's power to set the interest rates from time to time was completely unfettered. The Court of Appeal held that it was not. A term was to be implied into both agreements to the effect that the rates of interest would not be set dishonestly, for an improper purpose, capriciously or arbitrarily, or in a way in which no reasonable mortgagee, acting reasonably, would do. *Paragon Finance* is a fascinating case because it demonstrates the willingness of the courts in a private law claim to draw on the analogy of public law for the purpose of placing limits on the discretionary power of a contracting party. On what basis did the Court of Appeal see fit to imply this term into the contract? Was it on the basis of necessity? While some limit on the power of the creditor to vary interest rates is clearly highly desirable, it is not clear that it can be said to be necessary. Dyson LJ, on the other hand, stated (at [36]) that the implied term was 'necessary to give effect to the reasonable expectations of the parties'. However, it would appear that the driving force behind the recognition of the implied term was the 'reasonable expectations of the parties' (on which see 10.5) rather than strict necessity, and a term of this nature is now routinely implied into contracts in order to place a limit upon the exercise of a contractual discretion (*Braganza* v. *BP Shipping Ltd* [2015] UKSC 17, [2015] 1 WLR 1661).

The second case is the decision of the Court of Appeal in *Crossley* v. *Faithful & Gould Holdings Ltd* [2004] EWCA Civ 293, [2004] 4 All ER 447. The issue before the court was whether or not there was an 'implied term of any contract of employment that the employer will take reasonable care for the economic well-being of his employee'. In answering this question Dyson LJ stated (at [36]):

> It seems to me that, rather than focus on the elusive concept of necessity, it is better to recognise that, to some extent at least, the existence and scope of standardised implied terms raise questions of reasonableness, fairness and the balancing of competing policy considerations: see Peden (2001) *LQR* 459, 467–475.

Dyson LJ concluded, after a review of the authorities, that the implied term proposed on behalf of the employee should be rejected. He relied on two principal considerations in reaching this conclusion. First, after referring to *Scally*, he stated that 'it is not for this court to take a big leap to introduce a major extension of the law in this area when only comparatively recently the House of Lords declined to do so'. As we have noted

earlier in this section, the implied term recognized in *Scally* was drawn in very narrow terms and so it was thought to be inappropriate for the Court of Appeal now to imply a term cast in much broader terms. Secondly, he concluded that such an implied term 'would impose an unfair and unreasonable burden on employers'. He continued:

> It is one thing to say that, if an employer assumes the responsibility for giving financial advice to his employee, he is under a duty to take reasonable care in giving that advice ... It is quite a different matter to impose on an employer the duty to give his employee financial advice in relation to benefits accruing from his employment, or generally to safeguard the employee's economic well-being.

p. 371 ↵ Dyson LJ pointed out that the interests of employers and employees can and do conflict and, in such cases, he stated that it would be 'unreasonable' to require the employer 'to have regard to the employee's financial circumstances when he takes lawful business decisions which may affect the employee's economic welfare'. Further, it was held not to be the function of an employer to 'act as his employee's financial adviser' on the ground that it 'is simply not part of the bargain that is comprised in the contract of employment'. This being the case, it was held that there were 'no obvious policy reasons to impose on an employer the general duty to protect his employee's economic well-being'. In this way the conclusion that no term should be implied into the contract of employment obliging the employer to take reasonable care for the economic well-being of an employee was based, not on the need for such a term, but on the appropriateness of the term, having regard to the court's perception of the nature of the relationship that exists between an employer and an employee.

While the test applied by the courts in cases of terms implied in law may no longer be based solely on necessity, it does not follow that the judges have a free hand to imply terms into contracts when they see fit. They do not. As Lord Bingham MR observed in *Philips Electronique Grand Publique SA* v. *British Sky Broadcasting Ltd* [1995] EMLR 472, 481, 'it is because the implication of terms is so potentially intrusive that the law imposes strict constraints on the exercise of this extraordinary power.' In the case of terms implied in fact the test is still based on necessity, and the courts will in general be slow to imply a term into a contract, particularly where the parties have entered into a lengthy and carefully drafted contract but have failed to make provision for a particular issue. And, while the courts take a less stringent approach in the case of a term implied in law, cases such as *Scally*, *Mahmud*, and *Paragon Finance* demonstrate that the threshold for the implication of a term remains a high one.

10.5 Conclusion

What is the justification for implying terms into a contract? This issue is considered in the following two extracts. In the first extract Professor Collins considers a range of possible justifications, while in the second extract Lord Steyn, writing extrajudicially, surveys the different categories of implied terms. Interestingly, they reach a similar conclusion, albeit by different routes, namely that the justification for implied terms is to be found in the court's view of the reasonable expectations of the contracting parties.

H Collins, *The Law of Contract* (4th edn, Butterworths, 2003), pp. 245–246

> How can we explain and justify the … use of implied terms to supplement contractual obligations? In some instances it is apparent that the reference to the joint intention of the parties, as evidenced by the need to give business efficacy to their transaction, supports the implication of terms on grounds which merely complement the traditional justification of contractual obligations based upon the will of the parties. It is true that the will of the parties was never expressed, but the evidence supporting the claim that the term represents a presupposition or necessary implication of the words used can be so overwhelming that few could doubt that the term represents their original intention. But it is clear that the use of implied terms extends beyond any sort of justification of the type that the term merely states expressly what was silently understood by the parties.
>
> p. 372 ↵ Economic analysis of law suggests a good reason why the courts should provide a set of default rules to govern contractual relations in the absence of express terms. Default rules save transaction costs by permitting the parties to avoid the costs of negotiating every detail of their arrangement every time they make a contract, because they know that the courts will fill in the gaps in the usual way. This makes good sense, but it is arguable whether or not participants in the market deliberately avail themselves of this opportunity to save transaction costs. On the contrary, the proliferation of the standard form contract suggests that any party with sufficient resources is likely to devise a standard set of express terms to suit his or her purposes exactly. Many cases we have discussed so far concerning implied terms, such as … *Liverpool City Council* v. *Irwin*, comprise instances where the claim that an implied term exists is used to combat the one-sided standard form contract of the other party.
>
> Nor does the economic analysis suggest a satisfactory account of the grounds for the selection of terms by the courts. Under the efficiency analysis, the court should select those implied terms to which the parties would have agreed but for the presence of transaction costs. Although this criterion makes sense for terms which give a contract business efficacy, it is far from clear that it provides an intelligible guide in other cases. Consider the bargaining situation in *Liverpool City Council* v. *Irwin*. The council was presumably reluctant to agree to an obligation to maintain the common premises, so it would have held out against such an obligation, and, depending upon the local forces of supply and demand for tower block local authority housing, it might or might not have been successful. But even if it had agreed to the obligation, it could have insisted upon an increased rent to cover those costs, so to imply a term requiring a maintenance obligation without adjusting the rent produces a contract to which the parties never would have agreed.
>
> Further this economic analysis does not appear to correspond to the reasons ventured by the courts for the selection of implied terms. What seems to be at the heart of the model reasoning surrounding the implication of terms is the courts' endeavour to structure contracts so that they incorporate a fair and practical allocation of risks. The court imposed the duty to maintain the premises upon Liverpool City Council almost certainly because this was the most practical and efficient means of achieving the result. In the context of the employment relationship, the recent introduction of implied terms which impose obligations upon employers surely reflects changing views about the fair treatment of employees and the risk of losing a job. Similarly, the duty imposed upon

> professional sellers of goods to ensure that they are of satisfactory quality cannot be justified as the term which would have been agreed in the absence of transaction costs, for sellers would almost certainly seek to avoid such liability for latent defects. The reason for this allocation of risk is surely that it fits both the purpose of consumer protection and it places the risk of defects on the person in the better position to avoid the advent of such risks occurring.
>
> The notion of a default rule is therefore a misleading description of the use of implied terms. Through the implication of terms the courts can achieve what they regard as a fair and practical allocation of risks between the contracting parties, a view which may alter over time as illustrated by the changing implied terms inserted into the contract of employment. In this process the courts can seek to equalise the obligations of the parties, even in the teeth of express terms of standard form contracts, and so pursue ideas of fairness. The justification for implied terms therefore rests ultimately not on the intentions of the parties but rather the court's view of the reasonable expectations of the parties to the transaction.

p. 373 **Lord Steyn, 'Contract Law: Fulfilling The Reasonable Expectations of Honest Men'**
(1997) 113 *LQR* 433, 441–442

> In our system ... the implication of terms fulfils an important function in promoting the reasonable expectations of parties. Three categories of implied terms can be identified. First, there are terms implied by virtue of the usages of trade and commerce. The assumption is that usages are taken for granted and therefore not spelled out in writing. The recognition of trade usages protects the reasonable expectations of the parties. Secondly, there are terms implied in fact ... Such implied terms fulfil the role of ad hoc gap fillers. Often the expectations of the parties would be defeated if a term were not implied, e.g. sometimes a contract simply will not work unless a particular duty to co-operate is implied. The law has evolved practical tests for the permissibility of such an implication ... The legal test for the implication of a term is the standard of strict necessity. And it is right that it should be so since courts ought not to supplement a contract by an implication unless it is perfectly obvious that it is necessary to give effect to the reasonable expectations of parties. It is, however, a myth to regard such an implied term as based on an inference of the actual intention of the parties. The reasonable expectations of the parties in an objective sense are controlling: they sometimes demand that such terms be imputed to the parties. The third category is terms implied by law. This occurs when incidents are impliedly annexed to particular forms of contracts ... Such implied terms operate as default rules. By and large such implied terms have crystallised in statute or case law. But there is scope for further development. In such new cases a broader approach than applied in the case of terms implied in fact must necessarily prevail. The proposed implication must fit the generality of cases. Indeed, despite some confusion in the authorities, it is tolerably clear that the court may take into account considerations of reasonableness in laying down the scope of terms to be implied in contracts of common occurrence. This function of the court is essential in providing a reasonable and fair framework for contracting. After all, there are many incidents of contracts of common occurrence which the parties cannot always be expected to reproduce in writing. This type of supplementation of contracts also fulfils an essential function in promoting the reasonable expectations of the parties.

Further Reading

GOODE, R, 'Usage and its Reception in Transnational Commercial Law' (1997) 46 *ICLQ* 1.

PEDEN, E, 'Policy Concerns Behind Implication of Terms in Law' (2001) 117 *LQR* 459.

RAKOFF, T, 'The Implied Terms of Contracts: Of "Default Rules" and "Situation-Sense"' in J BEATSON AND D FRIEDMANN (eds), *Good Faith and Fault in Contract Law* (Oxford University Press, 1995), p. 191.

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Notes

[1] Letters of credit are discussed in more detail at 5.4, where their essential nature is described.

[2] A superannuation scheme is a form of pension scheme.