

## Obligation-Contract Law

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### *Introduction*

The recent case of NHS Trust v. Compass Group [2013] has highlighted how any failure by the dealing parties towards an outsourcing arrangement could result in the complete breakdown of a positive commercial relationship. In this case, the contract made a compulsion upon the dealing parties to allow flourishing of cooperation in between, and this has to be in good faith. Here, the parties were observed to have a confrontational approach towards strict contractual performance as well as an overly complex regime of service levels amongst them. Bialy<sup>1</sup> argues that the courts most often fail to understand the complexities between the parties which are involved in a mutual contract, though Campbell<sup>2</sup> disagrees.

However, the aim of this essay is to critically evaluate and understand the judgement in the case of Mid Essex Hospital Services NHS Trust v. Compass Group UK [2013] EWCA Civ 200.

### *Discussion*

Compass – which was trading as Medirest – entered into a contract with the NHS Trust, this contract was stated to be liable for 7 years. According to the contract, Compass was to provide its catering services for 2 of the hospitals mentioned in the contract, this process was to commence on the start of April 2008. The contract between the parties was seen to be as a complex one, here Poole<sup>3</sup> argues that complexity in contracts is often critical

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<sup>1</sup> Harvey Bialy, 'Good Faith Gone Bad—Gone Good Again'. Nat Biotechnol; (2008), p.18

<sup>2</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

<sup>3</sup> Jill Poole, *Textbook On Contract Law* (Oxford University Press 2012). p.1-10

for the courts to understand, though Quagliato<sup>4</sup> disagrees. The contract was assembled in a total of four documents, it consisted of a standard NHS contract which was joined with a PFI-based mechanism according to which Compass was obliged on its behalf to record any sort of service failures and therefore must allocate 'points' for each failure. This would allow deductions to be made from the monthly payments of the NHS Trust.

During the initial stages, the Trust was facing below-average performances by Compass, specifically in relation to staff shortages, below-average levels of cleanliness of kitchens at the ward, and due to the presence of expired or unhealthy food. In addition to this, Compass failed to monitor performance or report service failures during the initial few months. SCHWARTZ and Wen<sup>5</sup> believe that performance monitoring must be done by all the parties involved in a contract, though Umetsu<sup>6</sup> disagrees. Afterwards, the Trust started its own monitoring mechanism and therefore allocated service failure points as well as calculated deductions. This was done in a manner which made the High Court describing it as being 'patently absurd'.

According to the contract, both of the parties were obliged to "*... perform co-operation with each other which is in good faith and therefore should take all the reasonable actions that are necessary for the overall efficient transmission of instructions and information*".

In referring the principles of English law that pointed out that a notion of good faith is embedded in major legal principles, as Leggatt J held that in 'relational' contracts, a duty of good faith should be readily implied by a court should be as part of the ordinary process of

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<sup>4</sup> Pedro Barasnevicius Quagliato, 'The Duty To Negotiate In Good Faith'. *International Journal of Law and Management*; (2008). p.213-225

<sup>5</sup> JESSE A. SCHWARTZ and QUAN WEN, 'WAGE NEGOTIATION UNDER GOOD FAITH BARGAINING'. *International Game Theory Review*; (2007). P.555

<sup>6</sup> Akihiko Umetsu, 'Good Faith And Fair Dealing: The Ulmost Good Faith'. *Hokengakuzasshi (JOURNAL of INSURANCE SCIENCE)*; (2009), p.33

contractual construction on the basis of parties' presumed intention<sup>7</sup>. The content of that duty of good faith may include honesty, impartial dealing and a duty to collaborate with a contractual counterparty, but would be fact-specific as to the exact extent of the duty.

The Court of Appeal in this case referred to the decision held by Leggatt J in *Yam Seng* when taking both the effect of an express obligation to cooperate in good faith and whether there was an implied term that the employer would not act in an 'arbitrary, illogical or capricious way in evaluating the performance of contractor'<sup>8</sup>.

At first instance, the court held upon the notion that it is an obligation upon the involved parties to co-operate with each other in good faith, and this should not just be in relation to the regular provision of associated information. According to Varges and Connor<sup>9</sup> the provision of information from one party to another in relation to the matters of professional duties must be made as a part of the contract, though Williamson and Kleiner<sup>10</sup> disagrees with such a notion and believes that such a constraint would only complicate the existing matters between the parties. Bialy<sup>11</sup> believes that the courts must relate the factor of good faith with the flow of information that have taken place between the parties when giving its judgement, though Campbell<sup>12</sup> disagrees with such a notion.

This was due to the complex and long-term nature of the contract along with the point that the contract was implemented for not just the Trust but for the greater benefits of the patients. It was observed by the Court of Appeal that the Trust's overall conduct in performing calculations of the deductions, refusing to amend them, demanding payment for

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<sup>7</sup> David Campbell, 'Good Faith And The Ubiquity Of The 'Relational' Contract'. *The Modern Law Review*; (2014).

<sup>8</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

<sup>9</sup> Gabe Shawn Varges and J. F. O'Connor, 'Good Faith In International Law.' *The American Journal of International Law*; (1992), p.121

<sup>10</sup> Jeffrey A. Williamson and Brian H. Kleiner, 'New Developments Concerning The Covenant Of Good Faith And Fair Dealing'. *Management Research News*; (2003), p.37

<sup>11</sup> Harvey Bialy, 'Good Faith Gone Bad—Gone Good Again'. *Nat Biotechnol*; (2005).

<sup>12</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

them, and failing to properly respond to the approaches of Compass were of substantial nature in terms of breaches.

The first question which was addressed by the Court of Appeal was the overall extents of the discretion of Trust in the allocation of calculation deductions and service failure points. The court believed that the overall wording of the contract at first sight was very much inconsistent. Dorsett and Lafferty<sup>13</sup> have mentioned about the factor of inconsistency at the contracts and how such an action can complicate the matters between the parties, though Fayyad<sup>14</sup> disagrees and believes that such inconsistencies may not complicate the matters for the parties.

One clause present in the contract was seen to be justifying the actions of the Trust that it was rightfully entitled to act in this manner, though a different document set out precise and detailed mechanisms for performing calculations which left no chance for any sort of discretion to occur. Bialy<sup>15</sup> believes that a contract must fully justify the complete authorities of the involved parties; Campbell<sup>16</sup> disagrees and believes that such justification is not always essential.

It was observed by the court that the only sensible way to construe the mentioned provisions was to follow upon the exact rules and not just the general wordings. Fayyad<sup>17</sup> have criticised the abilities of courts when they tend to address the exact rules of the contract, though Quagliato<sup>18</sup> does not fully agree with this notion. In this case, this context was

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<sup>13</sup> S. Dorsett and G. Lafferty, 'Good Faith And The Fair Work Act: Its Potential, In Light Of The New Zealand Experience'. *The Economic and Labour Relations Review*; (2001).

<sup>14</sup> Mahmoud Fayyad, 'Measures Of The Principle Of Good Faith In European Consumer Protection And Islamic Law, A Comparative Analysis'. *Arab Law Quarterly*; (2014), 205-230

<sup>15</sup> Harvey Bialy, 'Good Faith Gone Bad—Gone Good Again'. *Nat Biotechnol*; (2005).

<sup>16</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

<sup>17</sup> Mahmoud Fayyad, 'Measures Of The Principle Of Good Faith In European Consumer Protection And Islamic Law, A Comparative Analysis'. *Arab Law Quarterly*; (2014), 205-230

<sup>18</sup> Pedro Barasnevičius Quagliato, 'The Duty To Negotiate In Good Faith'. *International Journal of Law and Management*; (2005).

relevant: "*the NHS Trust is a public authority which is responsible for delivering an essential service to vulnerable members of the general society*".

Therefore, the Trust could not be criticised for making the maximum deduction, or its allocation of the overall number of points. Its only point of "discretion" was either to exercise contractual right or not. Bialy<sup>19</sup> believes that the courts in Europe are more lenient towards the health care providers, though Campbell<sup>20</sup> disagrees with such a notion.

Audi<sup>21</sup> describes how ideals (standards 'that can hypothetically met by different types of conduct and at varying levels of intimacy to perfect realisation') provide such grounds because "*there is a level of ... [attainment] —which may be higher or lower in different circumstances—such that we ought to achieve it even though we have a right to fall short of it*"<sup>22</sup> (p.185). That such standards exist and are a crucial part of the moral world is the principal theme of much fresh moral theory, specifically feminist theory. This approach emphasises the confines of moralities of justice, including Kantianism and Utilitarianism, with their strong concentration on abstract and impersonal responsibilities, and emphasises their supplementation or even replacement by an 'ethics of care'.

However, the court described the clause which contained the good faith obligation as "*a mixture of different statements, which are set out in an unclear/incoherent order*". In the establishment of the correct construction, one of the judges was guided by the notion that there exist no general role of good faith in the contract laws of England and if the parties want to impose one then they have to do so expressly.

Bialy<sup>23</sup> have mentioned in detail the flaws of the contract laws of England, and how the courts often find it difficult to produce a judgement upon a disputed matter due, though

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<sup>19</sup> Harvey Bialy, 'Good Faith Gone Bad—Gone Good Again'. Nat Biotechnol; (2005).

<sup>20</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

<sup>21</sup> Robert Audi, *The Good In The Right* (Princeton University Press 2009).

<sup>22</sup> Robert Audi, *The Good In The Right* (Princeton University Press 2009).

<sup>23</sup> Harvey Bialy, 'Good Faith Gone Bad—Gone Good Again'. Nat Biotechnol; (2005).

Campbell<sup>24</sup> somewhat disagrees with such a statement and believes that the courts in England have little or no trouble in dealing with the contract laws. The court maintained that if this had been the intention of the parties then they should have stated this in a separate stand-alone clause at the contract. Additionally, this was described as a very detailed contract by the court in which the obligations of the involved parties as well as the consequences related to the breach had been spelled in very precise amount of detail. It has been noted that as a general rule, the extent of the duties are greatly dependent upon context of such duties. In this case, there seemed to exist no general duty; it was all being limited to the overall purposes which were set out in the contract's clauses, namely passing on the relative information and thereby enabling the Trust to acquire the benefit of the contract. Quagliato<sup>25</sup> have mentioned in detail the responsibilities of the courts when addressing the issues of information sharing between the contractually obliged parties.

According to the law authorities present almost anywhere in the world, honesty is an essential component of good faith. In this case, the factor of obligation meant that the involved parties should "*work together in an honest manner in order to achieve the stated purposes*". By analysing the conduct of Trust, the court came to the opinion that it had made deductions which were not agreed by it with Compass. This was because it went on to exceed the total overall amounts that it was contractually entitled to deduct. Therefore it had breached some provisions of the contract - though not the clause of good faith.

It was ruled by the court that the Trust had not acted in a dishonest manner; and the total deductions were completely irrelevant to the two specific purposes which were stated clearly in the mentioned clause. Also, when it went on to repay the wrongful deductions, then it actually "cured" its breaches rather effectively before Compass could purport to terminate.

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<sup>24</sup> UNSW Australia Business School, 'UNSW Business School - Where Great Minds Do Business' (2014) <<https://www.business.unsw.edu.au/#page=55>> accessed 16 December 2014.

<sup>25</sup> Pedro Barasnevicius Quagliato, 'The Duty To Negotiate In Good Faith'. *International Journal of Law and Management*; (2008).

The following issues were also discussed by the Court:

- In any contractual obligation where one party has any form of discretion, there exist an implied term that the party will not exercise that specific discretion in an "*irrational, arbitrary or capricious*" manner; though such a term is very difficult, but not impossible, to exclude.
- Context tends to be the key when working upon the extent of any duty related to the issue of good faith - the quoted authorities were not comparable directly with the situation of the Trust
- When considering any form of discretion, the adding of a qualifier like "*reasonable*" would import an objective element; this may operate as an adequate form of control mechanism.
- It is very important to make sure by the parties that the contractual documents are consistent and are also as precisely drafted; here, the process of drafting that was relative to the case went on to face a considerable amount of criticism, especially due to the fact that the contract was substantial and complex in nature. In this reference, the Court of Appeal's utilisation of words like "*incoherent*" spoke volumes. Here, a comment was also made by a Judge that the process of drafting itself went on to give rise to the underlying conflict between the two parties.

### ***Summary***

It was held by the Court of Appeal that the High Court was wrong in its implication of a general obligation upon the contractually obliged parties. This was in reference to the factor of good faith in relation to the long-term catering contract. There existed no such duty which can be applied generally in laws being applicable at England. Also, if the parties wanted to



include one, then the onus is on them to expressly draft something. The obligation of good faith in this agreement was applicable only at the two specific purposes which were clearly identified in the clause in question. Because to this, the respondent was not granted the entitlement to terminate the contract due to the result of the appellant's conduct.

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