

THE CHALLENGE OF PRINCIPLED GAP-FILLING – A STUDY OF IMPLIED TERMS IN COMPARATIVE CONTEXT

Introduction

Implied Terms and Gap-Filling

Last-Resort or Gap-Filling?

Sembcorp Marine Ltd v PPL Holdings Pte Ltd [2013] SGCA 43 at [94]:

... Although the prayer to imply a term might imply that there is a gap in a contract, which needs to be filled, not all gaps in a contract are “true” gaps in the sense that they can be remedied by the implication of a term. There are at least three ways in which a gap could arise:

- (a) the parties did not contemplate the issue at all and so left a gap;
- (b) the parties contemplated the issue but chose not to provide a term for it because they mistakenly thought that the express terms of the contract had adequately addressed it; and
- (c) the parties contemplated the issue but chose not to provide any term for it because they could not agree on a solution.

The Categories of Implied Terms

“Terms Implied in Fact”

General

Forefront Medical Technology (Pte) Ltd v Modern-Pak Pte Ltd [2006] 1 SLR(R) 927 at [41] (emphasis in the original text):

There are practical consequences to such an approach, the most important of which is that the implication of a term or terms in a particular contract *creates no precedent for future cases*. In other words, the court is only concerned about arriving at a just and fair result via implication of the term or terms in question in that case – *and that case alone*.

The “Business Efficacy” Test

Per Bowen LJ in *The Moorcock* (1889) 14 PD 64 at 68:

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 ...

The “Officious Bystander” Test

Per MacKinnon LJ in *Shirlaw v Southern Foundries (1926), Limited* [1939] 2 KB 206 at 227:

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!”’

Andrew Phang, “Implied Terms, Business Efficacy and the Officious Bystander – A Modern History” [1998] JBL 1 at 1 (abstract):

Adopting a primarily historical as well as biographical approach, the present article examines the underlying rationale and development of the two major tests for terms implied in fact: the business efficacy and officious bystander tests, respectively. Apart from interesting individual points that arise (such as the suggested origin of the officious bystander test as opposed to the source traditionally cited), this approach also provides us with valuable information as to the probable relationship between both tests. This probable relationship, it will also be argued, also finds support in the more recent caselaw. The article also explores some broader underpinnings and implications that might serve as points of departure for further research in this area.

Justice MacKinnon, *Some Aspects of Commercial Law – A Lecture Delivered at the London School of Economics on 3 March 1926* (1926) at p 13 (emphasis added):

But in most of these cases the Court has, as a matter of construction to find what is the implied term, if any, *i.e.* the obvious common agreement, *upon a matter as to which it must have the strongest suspicion that neither party ever thought of it at all, and that, if they had, they would very likely have been in hopeless disagreement what provision to make about it.*

Per MacKinnon LJ in *Shirlaw v Southern Foundries (1926), Limited* [1939] 2 KB 206 at 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 L.J. in *The Moorcock*. 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.*

Lord Hoffmann, “Anthropomorphic Justice: The Reasonable Man and His Friends” (1995) 29 Law Teacher 127 at 138 (emphasis added):

With the omnibus passing down the Clapham Road and approaching its destination, we must hurry on to the trio at the back who are engaged in fixing a charterparty. Mackinnon L.J. invented them [*viz.* the parties and the officious bystander in relation to the “officious bystander” test] in a *public lecture* and afterwards came them wider currency in his judgment in *Shirlaw v. Southern Foundries Ltd.* [1939] 2 K.B. 206. This time we have not merely one imaginary person but an entire musical hall act, in which the officious bystander asks his question and the two reasonable contracting parties reply in carefully rehearsed unison with their stock catch phrase “But of course!” Lord Justice Mackinnon was a witty and cultured man, for many years president of the Jane Austen Society. *His little scene is plainly based upon the contemporary cartoons of Bateman, in which some unfortunate person is always asking a question which causes general astonishment all around him.* But I do not imagine Lord Justice Mackinnon ever thought how seriously this little *jeu d’esprit* would be taken, how many times it would be cited, analysed, applied or distinguished in courts all over the world.

The Belize Test

Per Lord Hoffmann in *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 at [21] (emphasis added):

It follows that in every case in which it is said that some provision ought to be implied in an instrument, *the question for the court is whether such a provision would spell out in express words what the instrument, read against the relevant background, would reasonably be understood to mean.* It will be noticed from Lord Pearson’s speech [in *Trollope & Colls Ltd v North West Metropolitan Regional Hospital Board* [1973] 1 WLR 601 at 609] that this question can be reformulated in various ways which a court may find helpful in providing an answer—the implied term must “go without saying”, it must be “necessary to give business efficacy to the contract” and so on—but these are not in the Board’s opinion to be treated as different or additional tests. *There is only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?*

Foo Jong Peng v Phua Kiah Mai [2012] 4 SLR 1267 at [34], [36] and [43] (emphasis in the original text for [34] and [36]; emphasis added in italics and bold italics for [43]):

34 ... It is true that the very nature of an *implied* term necessitates some investigation of sorts on the part of the court. *However, it bears reiterating that the court does not substitute its own view of what the contracting parties should have intended had the gap in their contract been brought to their attention at the time they entered into the contract.*

...

36 In summary, although the process of the implication of terms does involve the concept of interpretation, it entails a *specific form or conception of interpretation* which is *separate and distinct from the more general*

process of interpretation (in particular, interpretation of the *express* terms of a particular document). Indeed, the process of the implication of terms *necessarily* involves a situation where it is precisely because the *express* term(s) are *missing* that the court is compelled to ascertain the presumed intention of the parties via the “business efficacy” and the “officious bystander” tests (both of which are premised on the concept of necessity). In this context, terms will not be implied easily or lightly. Neither does the court imply terms based on its idea of what it thinks *ought* to be the contractual relationship between the contracting parties. The court is concerned only with the *presumed* intention of the contracting parties because it can ascertain the *subjective* intention of the contracting parties *only* through the *objective evidence which is available before it* in the case concerned. *In our view, therefore, although the Belize test is helpful in reminding us of the importance of the general concept of interpretation (and its accompanying emphasis on the need for objective evidence), we would respectfully reject that test in so far as it suggests that the traditional “business efficacy” and “officious bystander” tests are not central to the implication of terms. On the contrary, both these tests (premised as they are on the concept of necessity) are an integral as well as indispensable part of the law relating to implied terms in Singapore ...*

...

43 In summary, therefore, *neither the English case law nor the academic literature furnishes clear support for the Belize test. The entire picture is mixed at best and ambiguous at worst, and constitutes further support for the approach adopted by this court* (set out above at [36]).

Sembcorp Marine at [79] and [82]:

79 In our judgment, it is possible to bridge the gap with *Belize* on this point, if one concludes that Lord Hoffmann was saying that the implication of terms is to be seen as part of the overall process of *construing the document as a whole*, and no more. In this regard, it is pertinent that the relevant passages in *Belize* do not use the word “interpretation”, but rather, “construction”. Moreover, they also speak of the construction of the instrument or document as a whole rather than of specific express terms ...

...

82 But this does not help us with the other parts of *Belize*. In so far as Lord Hoffmann in *Belize* proposed a standard of reasonableness for the implication of terms, we had respectfully registered our disagreement in *Foo Jong Peng* (at [36]), and we reaffirm that disagreement here.

Wayne Courtney, “Implied Terms: What is the Role of Construction?” (Paper delivered at the *Journal of Contract Law Conference* held at the Singapore Management University on 2 and 3 May 2013 (entitled “Future Developments of Contract Law and the Relationship Between the Contract Laws of the Commonwealth”), and forthcoming in the *Journal of Contract Law*) at p 22:

Because *Belize* ignores the distinction between construction (to determine linguistic meaning) and the application of doctrine by construction, it does not come to terms with the question of the role which doctrine was designed to fulfill. As has been explained, the major role is the introduction of system – something which is inherent in doctrine. But by eliminating doctrine, and focusing simply on the linguistic issue of what a contract means, the decision in *Belize* denies to courts the comfort of doctrine. The fact that nothing is put in its place means that the whole issue of implication in fact is based on construction rules which are themselves underdeveloped.

It would be easy to understand eliminating doctrine in favour of construction if implied terms formed an exception to the rules which deny the use of raw material such as the prior negotiations of the parties. But given the rationale in *Belize* – that the issue is one of meaning – it would not be possible to do that without changing the whole law of construction. Perhaps that is why Lord Hoffmann does not debate the issue.

Professor J W Carter, *The Construction of Commercial Contracts* (Hart Publishing, 2013) at para 3-27 (emphasis added):

Lord Hoffmann’s views in *Attorney General of Belize v Belize Telecom Ltd* are significant and clearly have important implications, not all of which have been worked out. *First, it is difficult to deny that the existence of specific requirements has been regarded as providing a degree of certainty in relation to implication. Although the degree of certainty may be slight, treating the whole issue as one of construction tends to beg the question whether the role of the specific requirements for implied terms is to facilitate implication or to limit implication.*

Second, under Lord Hoffmann’s approach, extrinsic evidence is not admissible in the implication of a term. Whether that is correct may vary according to the basis for implication. However, the authorities do not support the view that extrinsic evidence is never admissible.

Third, and perhaps most important of all, if specific rules do not need to be applied, because the content of the implied term is worked out simply by construing the contract, any term which is implied must be largely formal or

even redundant. It is simply the formal expression of an intention which can be inferred by construction of the document in the light of context.

Reigate v Union Manufacturing Company (Ramsbottom), Limited and Elton Copdyeing Company, Limited [1918] 1 KB 592 at 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.

Forefront at [36]:

An even cursory perusal of the above statement of principle by Scrutton LJ will reveal the *integration as well as complementarity* of the "business efficacy" and "officious bystander" tests. This is especially evident by the learned judge's use of the *linking* phrase "that is" in the above quotation. Indeed, the plain and natural meaning of this quotation is too clear to admit of any other reasonable construction or interpretation. And it is this: that the "officious bystander" test is the *practical mode by which* the "business efficacy" test is implemented. It is significant that the observations of Scrutton LJ in *Reigate* ([35] *supra*) *antedated* the more prominent pronouncement of the "officious bystander" test by MacKinnon LJ in *Shirlaw* ([31] *supra*) by *some two decades*. Of not insignificant historical interest, in this regard, is the fact that MacKinnon LJ was in fact Scrutton LJ's pupil and had close ties with him: on both professional as well as academic levels ...

Foo Jong Peng at [46] (emphasis in the original text) (**application of the "business efficacy" test**):

We did not think it was necessary for the effective management of the Association's affairs for the Management Committee to be given the power to remove particular office bearers. The Management Committee still retains the decisive power to supervise the conduct of the office bearers, manage finances and to formulate the general policy direction for the Association.

Foo Jong Peng at [47]–[48] (emphasis in the original text) (**application of the "officious bystander" test**):

47 Further, the power of removal was not, in our view, so obvious that it would go without saying that such a term ought to be implied under the "officious bystander" test. The Rules include specific rules governing the removal of trustees and expulsion of members for misconduct (see rr 14 and 19, respectively) and therefore contemplate the possibility that individuals with certain positions of responsibility or members may need to be removed in the interests of the Association. It is thus difficult to believe that the members did not advert themselves to the possibility of removal of office bearers or did not expressly say so because they had considered it so obvious that it would go without saying. We also do not think that the members would have considered it obvious that the Management Committee itself should have free rein to remove an office bearer. The members could have preferred the power of removal to be vested in the General Meeting or for the power to be exercised only when stringent voting margins or procedural pre-conditions are met; alternatively, as the Judge observed, the members could equally have intended that this apparent "gap" in the Rules should mean precisely that office bearers cannot be removed and must be allowed to serve out their complete two-year term of office in order to ensure stability and continuity in the management of the Association.

48 Indeed, if the officious bystander had asked whether the Management Committee had the power to remove the office bearers at will, the members would not have unequivocally thought that the term was obviously necessary for the effective management of Association and unanimously suppressed him with a testy "Oh, of course!" The limited term of office - both for office bearers and members of the Management Committee - ensures that control of the Association will not always fall into the hands of a single individual, and a fixed period of office without the threat of removal encourages consensus and unity, instead of divisive power struggles and acrimony. If the Management Committee or general members have irreconcilable differences with a particular office bearer, the solution is to vote him out at the next election for a new Management Committee and/or office bearers. And, if an office bearer has behaved in a particularly egregious manner, the last resort would and should be expulsion.

Sembcorp Marine at [101]:

It follows from these points that the implication of terms is to be considered using a three-step process:

- (a) The first step is to ascertain how the gap in the contract arises. Implication will be considered only if the court discerns that the gap arose because the parties did not contemplate the gap.
- (b) At the second step, the court considers whether it is necessary in the business or commercial sense to imply a term in order to give the contract efficacy.

(c) Finally, the court considers the specific term to be implied. This must be one which the parties, having regard to the need for business efficacy, would have responded “Oh, of course!” had the proposed term been put to them at time of the contract. If it is not possible to find such a clear response, then, the gap persists and the consequences of that gap ensue.

BP Refinery (Westernport) Pty Ltd v President, Councillors and Ratepayers of the Shire of Hastings (1977) 180 CLR 266 at 282–283:

Their Lordships do not think it necessary to review exhaustively the authorities on the implication of a term in a contract which the parties have not thought fit to express. In their view, for 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.

“Terms Implied in Law”

General

Forefront at [42]–[44] (emphasis in the original text):

42 There is a *second* category of implied terms which is wholly different in its nature as well as practical consequences. Under this category of implied terms, once a term has been implied, such a term will be implied in *all future* contracts of *that particular type*. ... [T]he central idea is clear: it is that the term implied is implied in a *general* way for *all* specific contracts that come within the purview of a broader umbrella category of contracts ...

43 To distinguish this particular category of implied terms from the first, legal scholars have referred to it as the category of “terms implied in law” ... The first or former category has, in turn, been referred as to the category of “terms implied in fact” ...

44 The *rationale as well as test* for this broader category of implied terms is, not surprisingly, quite *different* from that which obtains for terms implied under the “business efficacy” and “officious bystander” tests. In the first instance, the category is much broader inasmuch (as we have seen) the *potential* for application *extends* to *future* cases relating to the same issue with respect to the *same category* of contracts. In other words, the decision of the court concerned to imply a contract “in law” in a particular case *establishes a precedent* for similar cases in the future for *all* contracts of *that particular type*, unless of course a higher court overrules this specific decision. Hence, it is my view that courts ought to be as – if not more – careful in implying terms on this basis, compared to the implication of terms under the “business efficacy” and “officious bystander” tests which relate to the *particular contract and parties only*. Secondly, the test for implying a term “in law” is broader than the tests for implying a term “in fact”. This gives rise to difficulties that have existed for some time, but which have only begun to be articulated relatively recently in the judicial context, not least as a result of the various analyses in the academic literature (see, for example, the English Court of Appeal decision of *Crossley v Faithful & Gould Holdings Ltd* [2004] 4 All ER 447 at [33]–[46]).

Jet Holding Ltd v Cooper (Singapore) Pte Ltd [2006] 3 SLR(R) 769 at [90]–[91] (emphasis in the original text):

90 The category of “terms implied in law” is not without its disadvantages. A certain measure of uncertainty will always be an integral part of the judicial process and, hence, of the law itself. This is inevitable because of the very nature of life itself, which is – often to a very large extent – unpredictable. Such unpredictability and consequent uncertainty is of course a double-edged sword. It engenders both the wonder and awe as well as the dangers and pitfalls in life. Given this reality, however, one of the key functions of the courts is not to add unnecessarily to the uncertainty that already exists.

91 However, the category of “terms implied in law” has now been firmly woven into the tapestry of our local contract law. It also aids, on occasion at least, in achieving a just and fair result. Most importantly, perhaps, it has formed both the theoretical as well as practical basis for *statutory* implied terms, such as those found in the UK Sale of Goods Act 1979 (c 54) ...

Ng Giap Hon v Westcomb Securities Pte Ltd [2009] 3 SLR(R) 518.

HSBC Institutional Trust Services (Singapore) Ltd (trustee of Starhill Global Real Estate Investment Trust) v Toshin Development Singapore Pte Ltd [2012] 4 SLR 738.

Yam Seng Pte Ltd v International Trade Corporation Ltd [2013] 1 Lloyd’s Rep 526 at [124] and [125], *per* Leggatt J (emphasis added in italics and bold italics):

In refusing, however, if indeed it does refuse, to recognise any such general obligation of good faith, this jurisdiction would appear to be *swimming against the tide*. As noted by Bingham LJ in the *Interfoto* case, a general principle of good faith (derived from Roman law) is recognised by most civil law systems – including those of Germany, France and Italy. From that source references to good faith have already entered into English law via EU legislation. ... There can be little doubt that the penetration of this principle into English law and the pressures towards a more unified European law of contract in which the principle plays a significant role will continue to increase.

...

Under *English law* a duty of good faith is *implied by law* as an incident of certain categories of contract, for example contracts of employment and contracts between partners or others whose relationship is characterised as a fiduciary one. ***I doubt that English law has reached the stage, however, where it is ready to recognise a requirement of good faith as a duty implied by law, even as a default rule, into all commercial contracts. Nevertheless***, there seems to me to be no difficulty, following the established methodology of English law for the *implication of terms in fact*, in implying such a duty in any ordinary commercial contract based on the presumed intention of the parties.

Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd (Trading as Medirest) [2013] EWCA Civ 200 at [105], *per* Jackson LJ (emphasis added in italics and bold italics):

... I start by reminding myself that there is ***no general doctrine*** of “good faith” in English contract law, although a duty of good faith is implied by law as an incident of certain categories of contract: see *Horkulak* at paragraph 30 and *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB) at paragraphs 120-131. *If the parties wish to impose such a duty they must do so expressly.*

The Implied Term As A Theoretical Concept

Andrew Phang, “On Linkages in Contract Law – Mistake, Frustration and Implied Terms Reconsidered” (1996) 15 *Trading Law* 481 at 482–483 (emphasis added):

Courts imply “terms in law” when broader considerations of policy and reasonableness require such terms to be implied in contracts of a certain type. It is submitted that this broad basis for the implication of “terms in law” would be eminently suitable as a juridical basis for frustration. Indeed, it is precisely because of considerations of policy and reasonableness that contracts are held to be discharged by the doctrine of frustration. And just as the implication of “terms in law” is within the sole purview of the court (which may even imply such a term when it would not otherwise do so “in fact”, or when it would even override the presumed intention of the parties to the contract), *so also is the doctrine of frustration with the sole purview of the court, operating to discharge the contract by operation of law as opposed to any action on the part of the contracting parties themselves. That the doctrine of “terms implied in law” has not really been linked to the doctrine of frustration is not surprising in view of the fact that the former doctrine has only been prominent relatively recently. The only problem might lie in the requirement that a term be implied “in law” in relation to a certain category of contract, but can it not be argued that contracts that ought to be frustrated would constitute the required category? Admittedly, such reasoning may be a fiction of sorts, but so is the entire classification of “terms implied in law” themselves; the main purpose, it would appear, is not to ensure doctrinal coherence as such but, rather, to allow justice to be achieved in certain (especially extreme) situations. To this end, it is not envisaged that terms will be easily implied under this category, and this is entirely consistent with the application of the doctrine of frustration, since it is generally well-known that frustration is a doctrine not to be liberally applied. ... Indeed, and this is an important point, the present possible juridical bases for frustration will in fact be substantially incorporated within the theory of “terms implied in law”, involving (as it does) not only construction and implication, but also fairness to the parties owing to a radical change in obligation.*

One final objection might, however, be phrased thus: that it is *really not very important to determine what the precise juridical basis of frustration is*. Once again, the present writer *has no quarrel with this view*, having expressed a similar view elsewhere; *however*, inasmuch as this is perceived to be a relatively less important issue, *it is suggested that it would be far better to lay it completely to rest via the suggestion proffered here, rather than to let it remain a thorn in the contractual side, even if only in the academic context. More importantly, it is submitted that the line between the juridical basis on the one hand and the process of application on the other is a rather artificial one to begin with; indeed, ... the very concept of the implied term (here, it is submitted, “in law”) would necessarily entail all the so-called ‘practical’ tests for frustration, the foremost amongst which is the “radical change in obligation” test. Indeed, it might be added that the courts do not draw any real distinction between juridical basis and practical test insofar as a “radical change in obligation” is concerned, treating this concept as both the basis as well as a test for frustration.*

Conclusion