



Section of Litigation Business Torts & Unfair Competition

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What You Should Know about the Implied Duty of Good Faith and Fair Dealing

Imagine you're a franchisee of a large chain and, according to your franchise agreement, you owe a monthly franchise fee. To make enough money to pay that fee, you ask the franchisor for help with marketing or to speak to your potential investors. The franchisor, however, refuses to help. As a result, you are unable to pay your franchise fee.

In this situation, the franchisor may be liable to you for breach of the duty of good faith and fair dealing—even though you didn't perform your end of the bargain. This is because every contract contains an implied duty of good faith and fair dealing in the performance and enforcement of the contract. Most executives and companies—and even attorneys—however, do not realize that this duty may require that parties *not interfere with or fail to cooperate in the other party's performance*. This is important because even if your contract does not explicitly require you to cooperate or if your contract does not explicitly state that you must not interfere, the duty of good faith and fair dealing may require you to do so or else you risk breaching the agreement.

This post will explain what the duty of good faith and fair dealing is and how a party can breach that duty by interfering with or failing to cooperate in the other party's performance.

The Duty of Good Faith and Fair Dealing

In general, every contract contains an implied duty of good faith and fair dealing. This duty requires that neither party will do anything that will destroy or injure the right of the other party to receive the benefits of the contract. There is no specific definition, however, of this duty and courts have discretion to determine its scope. When deciding whether the duty of good faith and fair dealing was breached, courts analyze the facts and determine what is fair under the circumstances.

"Good faith" has generally been defined as honesty in a person's conduct during the agreement. The obligation to perform in good faith exists even in contracts that expressly allow either party to terminate the contract for any reason. "Fair dealing" usually requires more than just honesty. It generally requires that a party cannot act contrary to the "spirit" of the contract, even if you give the opposing party notice that you intend to do so.

In general, the duty of good faith and fair dealing means, for example, that parties cannot evade the spirit of the bargain, lack diligence or slack off, perform incorrectly on purpose, abuse their power when specifying the terms of a contract, or *interfere with or fail to cooperate in the other party's performance*. Let's further analyze this last example because, as stated above, most executives and attorneys do not realize that some jurisdictions include it in the duty of good faith and fair dealing.

Interfering with or Failing to Cooperate in the Other Party's Performance

As stated above, each party to a contract has a duty to do everything that the contract assumes he or she will do to accomplish its purpose. This means that your performance under a contract is excused—or does not need to happen—if your performance is prevented or hindered by the other party to the contract. In other words, your performance in a contract does not need to be completed—and you won't be considered to have breached the contract—if the other party is interfering with or fails to cooperate with your performance. The theory behind this principle is that a party cannot interfere with or fail to cooperate with your performance and then complain about it.

Thus, in the example above, when the franchisor failed to help you with marketing or refused to meet with your investors, the franchisor may have breached the duty of good faith and fair dealing and you may be excused from paying the franchise fees.

Final Thoughts

It is important that you and your business understand what your obligations are under a contract—not just the actual contract terms, however, but also the implicit terms, like the duty of good faith and fair dealing. This is because, during the course of a contract, if the other party asks you for help and you do not provide it because the contract terms do not require you to do so, you may have unintentionally breached the agreement.

Whether you are about to enter into a contract or are already a party to numerous agreements, talk to an attorney to understand what the duty of good faith and fair dealing requires of you and your company.

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