

# Good Faith in English Law: Clarifying the Limits of Contractual Duties in *Faulkner v. Vollin*

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## Conclusion Overview:

Good faith is not a general principle implied into contracts under English law unless expressly included. However, where parties do include a good-faith clause, the courts will enforce it, albeit within strict parameters. In *Mark Faulkner & Ors v. Vollin Holdings Limited & Ors* [2022], the Court of Appeal of England and Wales clarified the extent of such duties, stressing that good faith primarily requires honesty and context-specific interpretation of the contract. This case highlighted the court's reluctance to extend good-faith duties beyond the contractual framework, especially in cases where shareholders' rights and corporate structures are at play.

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## Introduction:

The role of good faith in contracts under English law has traditionally been limited, with courts reluctant to imply general duties of good faith in commercial agreements. This approach was recently reaffirmed in the case of *Faulkner v. Vollin*, where the Court of Appeal overturned a High Court decision that expanded the interpretation of a good-faith clause in a shareholders' agreement (SHA). The case underscored the importance of examining the specific context and purpose of the contractual relationship when interpreting good faith, particularly in corporate governance disputes.

This article analyzes the judgments of both the High Court and the Court of Appeal, highlighting their differing interpretations of the good-faith obligation and its implications for contractual relationships.

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## Case Overview:

### Background:

The dispute arose between minority shareholders (the Minorities) and majority investors (the Investors) in Compound Photonics Group Limited (CPGL). Following significant investments, the Investors, whose stake increased to 93%, clashed with the Minorities over the control of CPGL. The Investors ultimately demanded the resignation of Jonathan Sachs, CPGL's CEO, and removed Mark Faulkner, a director, from the board.

In response, the Minorities filed a claim under section 994 of the Companies Act 2006 for unfair prejudice, arguing that the forced resignations breached the good-faith obligation in the SHA, which required the shareholders to "act in good faith in all dealings" with each other and CPGL.

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## The High Court's Judgment:

In the High Court, Mr. Justice Adam Johnson adopted a broad interpretation of the good-faith clause in the SHA, relying on a set of minimum standards derived from prior case law. He concluded that the good-faith obligation required the parties to:

1. Act honestly;
2. Be faithful to the parties' agreed common purpose;
3. Refrain from using their powers for an ulterior purpose;
4. Deal fairly and openly;
5. Take into account their own interests but also have regard to the interests of the other party.

### **Focus on Common Purpose:**

Justice Johnson placed significant emphasis on the second standard—being faithful to the agreed common purpose of the contract. He identified this common purpose as maintaining a “constitutional balance” between the interests of the Minorities and the Investors, particularly through the continued presence of Sachs and Faulkner on the board. The contractual framework, he reasoned, intended to entrench these individuals in decision-making roles to safeguard the balance of power between the two shareholder groups.

The High Court found that even though the Investors genuinely believed their actions were in the best interests of CPGL, their decision to remove Sachs and Faulkner upset this constitutional balance. The court ruled that the Investors had breached the good-faith obligation by overriding this balance for their own advantage, prejudicing the rights of the Minorities. Consequently, Justice Johnson ordered the Investors to buy out the shares of the Minorities as a remedy for this breach.

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## **The Court of Appeal's Judgment:**

The Court of Appeal of England and Wales took a narrower approach to interpreting the good-faith clause, focusing primarily on honesty as the “core” requirement of any good-faith obligation. The court held that the interpretation of good faith must be context-specific, derived from the contract's express terms and its overall commercial setting.

### **Key Findings:**

#### **1. Honesty as the Core of Good Faith:**

The Court of Appeal reiterated that good faith primarily requires parties to act honestly. The duty may also extend to conduct that would be regarded as commercially unacceptable by reasonable people. However, any broader requirements—such as preserving a particular balance of power—must be explicitly stated in the contract.

#### **2. Caution with Overarching Principles:**

The Court warned against importing general notions of fairness or purpose into contracts unless clearly intended by the parties. It emphasized that decisions from other legal systems or unrelated areas of law should be treated with caution when interpreting good-faith obligations in a commercial context.

#### **3. Fidelity to the Common Purpose:**

The Court of Appeal had “considerable reservations” about the High Court's interpretation of fidelity to the parties' common purpose. Specifically, it disagreed with the view that the SHA and Articles of Association were designed to entrench Sachs and Faulkner on the board. Instead, it found that the contractual provisions—including the quorum requirements—were contingent upon Sachs and Faulkner remaining directors. Their removal, therefore, did not inherently violate the agreed common purpose.

#### **4. The Shareholder-Director Distinction:**

The Court also rejected the High Court's conclusion that the Investors were required to take the

Minorities' interests into account when exercising their voting rights as shareholders. While shareholders must consider the company's best interests under company law, their voting rights are distinct from fiduciary duties owed by directors, and there was no contractual requirement to maintain a particular balance of power.

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## Conclusion:

The *Faulkner v. Vollin* case reaffirms the cautious approach that English courts take toward interpreting good-faith obligations. While express duties of good faith will be enforced, they must be interpreted within the specific contractual context, with honesty as the core requirement. The High Court's attempt to expand good-faith duties to include preserving a constitutional balance was rejected, highlighting the courts' reluctance to imply broader fiduciary or fairness obligations without clear contractual wording.

For contractual parties, this case serves as a reminder to carefully draft good-faith clauses, specifying any broader obligations or common purposes they wish to enforce. The courts will not lightly impose general duties of fairness or balance without clear contractual direction.

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