

January 2008

# Wood v. Lucy: The Overlap between Interpretation and Gap-Filling to Achieve Minimum Decencies

Nicholas R. Weiskopf

Follow this and additional works at: <http://digitalcommons.pace.edu/plr>



Part of the [Contracts Commons](#), and the [Legal History Commons](#)

---

### Recommended Citation

Nicholas R. Weiskopf, *Wood v. Lucy: The Overlap between Interpretation and Gap-Filling to Achieve Minimum Decencies*, 28 Pace L. Rev. 219 (2008)

Available at: <http://digitalcommons.pace.edu/plr/vol28/iss2/4>

# ***Wood v. Lucy*: The Overlap Between Interpretation and Gap-Filling to Achieve Minimum Decencies\***

**Nicholas R. Weiskopf+**

*Wood v. Lucy* is a wonderful teaching tool because it uses a combination of interpretive and gap-filling techniques to create a contractual duty as to which the parties had been silent—the terms of *Wood*'s exclusive said nothing about any affirmative obligation on his part to market, or attempt to market, the famous Lady Duff-Gordon's creations. Instead of concluding that *Wood* had been left to act in his own self-interest, Cardozo spins an intricate web to come up with an obligation of good faith efforts. His avowed purpose is to avoid placing one party at the "mercy" of the other.

Given the precedential respect *Wood* has enjoyed for almost a century,<sup>1</sup> one ought be surprised at how many newer decisions, especially New York law decisions, flatly refuse to treat good faith as any sort of independent duty—as a source of "new" obligations not specified by the agreement as interpreted. We will see that an Official Comment to the Uniform Commercial Code appears to be in accord with these cases. Under this restrictive approach, good faith precepts shape the performance of actual undertakings, but no more. Silence in the face of the foreseeable bespeaks a shared intent not to regulate or restrict. For instance, according to the Eleventh Circuit applying Florida

---

\* Copyright © 2007 Nicholas R. Weiskopf.

+ Professor of Law, St. John's University School of Law. J.D., Columbia University School of Law, 1969; A.B. Columbia College, 1966.

1. Uniform Commercial Code section 2-306(2) provides that a goods transaction based on exclusive dealing "imposes unless otherwise agreed an obligation by the buyer to use best efforts to supply the goods and by the buyer to use best efforts to promote their sale." U.C.C. § 2-306(2) (1993). This rule has been applied by direct analogy to exclusive distributorship cases, and the New York Annotations to section 2-306(2) provide that it "is apparently based upon *Wood v. Lucy, Lady Duff-Gordon*, 222 N.Y. 88, 118 N.E. 214 (1917)." N.Y. U.C.C. § 2-306 (McKinney 2007).

law,<sup>2</sup> there can be no good faith restriction on a franchisor's opening of a fast food operation which substantially competes with those of an existing long-time franchisee unless there is an actual term of agreement on that subject in the franchise contract. Most would find such a conclusion problematic.

While I leave the specifics of other such decisions for later discussion, it is interesting to speculate as to what promotes them. What leads to a conclusion that an implied good faith obligation cannot be used to create obligations beyond those actually specified in the contract? It would appear that many courts are confusing principles of interpretation, including parol evidence restrictions, with "minimum deficiencies" to be read into contracts as a matter of law. This leads to the view that absent a bargain in fact derived from words of agreement or implied in fact from party conduct, there is no hook for any sort of good faith requirement to attach itself. Under such an approach, there can be no tandem use of interpretation and gap-filling in the setting of terms.

New York's Appellate Division, by unanimous vote of five to zero, adopted this restrictive approach in *Wood*,<sup>3</sup> as did three dissenters on the Court of Appeals. In rejecting any idea that Wood's exclusive impliedly obligated him to use reasonable affirmative efforts on Lucy's behalf, the intermediate appellate court considered the terms of actual agreement, but then simply stopped. If interpretation failed to yield a legally enforceable promise by each party, there was no contract:

The enforcement of his promise to collect and pay over is thus made to depend upon an act which he has not agreed to perform and which the defendant cannot compel him to perform. . . . It is quite apparent that in this respect the defendant gives everything and the plaintiff gives nothing and there is a lack of mutuality in the contract.<sup>4</sup>

It fell to Cardozo to take the next step:

---

2. *Burger King Corp. v. Weaver*, 169 F.3d 1310, 1316 (11th Cir. 1999) (holding that there was no action for breach of the implied covenant of good faith and fair dealing "where the party alleged to have breached the implied covenant has in good faith performed all of the express contractual provisions").

3. *Wood v. Lucy, Lady Duff-Gordon*, 164 N.Y.S. 576 (App. Div. 1917).

4. *Id.* at 577.

The implication of a promise here finds support in many circumstances. The defendant gave an exclusive privilege. She was to have no right for at least a year to place her own indorsements or market her own designs except through the agency of the plaintiff. The acceptance of the exclusive agency was an assumption of its duties. . . . We are not to suppose that one party was to be placed at the mercy of the other. . . . Many other terms of the agreement point the same way.<sup>5</sup>

To further enforce the meshing of factual and legal implication (a combination of actual and presumed intent) Cardozo explained that “[w]ithout an implied promise, the transaction cannot have such business efficacy as both parties must have intended that at all events it should have.”<sup>6</sup>

The processes of interpretation and gap-filling can, if one wishes, be portrayed in the abstract as distinct; unless interpretation cannot provide an answer, there is no need to gap-fill because there is no omitted case to resolve by implication as a matter of law.<sup>7</sup> Yet, while “[t]he supplying of an omitted term is not technically interpretation . . . the two are closely related.”<sup>8</sup> As a leading text explains:

[T]he borderline between terms implied-in-fact (*i.e.*, agreed to in some meaningful sense by the parties themselves) and implied-in-law (imposed by the court) is not an easy one to draw. Certainly one of the reasons militating in favor of an implied-in-law term may be its apparent consistency with the intention of the parties . . . .<sup>9</sup>

---

5. *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214, 214 (N.Y. 1917) (citations omitted).

6. *Id.*

7. The comments to section 204 of the Restatement (Second) of Contracts which provides for the supplying of “omitted essential terms,” portray gap-filling of omitted terms as a post-interpretive step. RESTATEMENT (SECOND) OF CONTRACTS § 204 (1981). Comment C states that “[i]nterpretation may be necessary to determine that the parties have not agreed with respect to a particular term, but the supplying of an omitted term is not within the definition of interpretation.” *Id.* at cmt. c. See also ALAN FARNSWORTH ET AL., CONTRACTS 604 (Foundation Press 2001) (there is a “gap” if the contract, “when interpreted, does not cover the case at hand” ).

8. RESTATEMENT (SECOND) OF CONTRACTS § 204 cmt. a (1981).

9. CHARLES KNAPP ET AL., PROBLEMS IN CONTRACT LAW 431-32 (5th ed. 2003).

Despite the fact that gap-fillers may be supported by presumed party intent, they are also supplied to further community standards of fairness and policy. Says a leading treatise:

There are those who preach the sometimes discordant gospels of economic efficiency, the implementation of communitarian values, the inference of norms implicit in the parties' relationship, or implicitly consented to . . . . It cannot be said that the legal system has adopted any of these criteria as exclusive.<sup>10</sup>

The implied covenant of good faith may be seen as the patriarch of all gap-fillers. According to one study, the phrase "implied covenant of good faith" is found in more than 10,000 cases decided between 1985 and 1994.<sup>11</sup> A quarter century ago, Professor Summers referenced this covenant "as a kind of 'safety valve' to which judges may turn to fill gaps and qualify or limit rights and duties otherwise arising under . . . specific contract language."<sup>12</sup> Despite efforts to bring structure and predictability to the concept and its application, it is simply too talismanic to be susceptible to precise definition.<sup>13</sup> Unlike other implied at law terms, good faith is not a default concept used to fill only one particular sort of omitted case.<sup>14</sup> Instead, good faith precepts are typically infused into contractual arrangements in an effort to preserve "minimum decencies." Subspecies of the good faith principle include implied obligations of reasonable (or

---

10. JOSEPH M. PERILLO, CALAMARI AND PERILLO ON CONTRACTS 55 (5th ed. 2003).

11. Harold Dubroff, *The Implied Covenant Of Good Faith In Contract Interpretation and Gap-Filling: Reviving A Revered Relic*, 80 ST. JOHN'S L. REV. 559, 561 (2006).

12. Robert S. Summers, *The General Duty of Good Faith – Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810, 812 (1982).

13. See RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a (1981).

The phrase "good faith" is used in a variety of contexts, and its meaning varies somewhat with the context. Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a variety of types of conduct characterized as involving "bad faith" because they violate community standards of decency, fairness or reasonableness. The appropriate remedy for a breach of the duty of good faith also varies with the circumstances.

*Id.*

14. By a "particular sort of omitted case," I refer, for instance, to one of impossibility or impracticability of performance where the omitted term sought to be supplied is an implied at law condition excusing performance.

best) efforts, those of cooperation and those of non-prevention of performance or satisfaction of a condition.

It is true that a good faith requirement is often engrafted onto an express covenant to prevent opportunism. Purchase guarantees under a requirements contract must be set in keeping with commercial good faith.<sup>15</sup> Similarly, a promise to receive evidence as part of a review process entails the obligation to consider it.<sup>16</sup> There are also, however, classic fact patterns involving possible prevention in which good faith does not attach to any particular express undertaking by the party to be restrained. Even if a construction contract is silent on the subject, a refusal by "Owner" to permit "Contractor" reasonable access to the work site will be treated as a breach by prevention. To take it a step further, Judge Posner has held that breach of an implied good faith covenant can sometimes rest on an opportunistic failure to warn a counterparty that it is overlooking a critical part of an existing contract to its material detriment.<sup>17</sup>

Of course, in some situations, there is a blurry distinction between use of good faith precepts to "round out" an express covenant and such use to create a new obligation. This is generally less so when a court is asked to deal with the unforeseen.<sup>18</sup> The distinction can take on the most clarity, however, when the issue is whether to supply a good faith obligation as a matter of law to regulate contractual interaction between those of unequal power, either by virtue of their position in the marketplace, or because of the facial structuring of their ostensible agreement. It is here that implications of good faith requirements may have little to do with already existing actual terms of understanding. There are obviously cases in which "big brother" is actually seeking to preserve the very sharp edge the express words of agreement seem clearly to provide, and the

---

15. See U.C.C. § 2-306(1) (2003).

16. *Dalton v. Educ. Testing Serv.*, 653 N.E.2d 617 (N.Y. 1995).

17. *Market Street Assocs. Ltd. P'ship v. Frey*, 941 F.2d 588 (7th Cir. 1991).

18. A famous case of this type is *Kirke La Shelle Co. v. Paul Armstrong Co.*, 188 N.E. 163 (N.Y. 1933). Good faith and fair dealing required plaintiff, who was to share in receipts from a play and hence had to approve other uses of the work "except movie rights," to nonetheless have approval and revenue entitlement with respect to a talking motion picture based on the play. *Id.* This conclusion was because the parties could not contemplate the advent of "talkies" when they made their deal, and this new development would otherwise detract from revenues from the play itself. *Id.*

weaker counterparty may have every reason so to understand. In such cases, the supplying of good faith restrictions becomes a *sub rosa* sort of equitable reformation.

### Authorities Limiting Good Faith Restrictions To Performance of Actual Undertakings

In 1994, the Uniform Commercial Code Permanent Editorial Board created an Official Comment to what was then section 1-203's provision that "[e]very contract or duty within this Act imposes an obligation of good faith in its performance or enforcement."<sup>19</sup> That Comment, to what is now section 1-304, provides:

This section does not support an independent cause of action for failure to perform or enforce in good faith. Rather, this section means that a failure to perform or enforce, in good faith, a specific duty or obligation under the contract, constitutes a breach of that contract or makes unavailable, under the particular circumstances, a remedial right or power. This distinction makes it clear that the doctrine of good faith merely directs a court towards interpreting contracts within the commercial context in which they are created, performed, and enforced, and does not create a separate duty of fairness and reasonableness which can be independently breached.<sup>20</sup>

While the Comment is indeed curious, the Code at least tempers truncation of the good faith concept by taking a very expansive view of the concept of "Agreement," defining it in section 1-201(3) to include "the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance."<sup>21</sup> If the reference to "implication" is designed to go beyond the traditional interpretive feeds which are specified—if "implication" refers to the reading in of mercantile "minimum decencies" as a matter of law—then perhaps there is little harm done. Still, this needs clarification. Worse still is that certain case decisions go even further in the wrong direction. These case decisions limit the use of good faith to the shaping of only those duties *explicitly* set forth.

---

19. U.C.C. § 1-203 cmt. (1994) (current version at U.C.C. § 1-304 (2003)).

20. U.C.C. § 1-304 cmt. n.1 (2003).

21. U.C.C. § 1-201(3) (2003).

Here are some examples of cases refusing to use good faith except to round out explicit duties. Each is based on New York law. A federal court, asked to hold securities brokers in breach for allegedly bad faith misconduct, stated that the duty of good faith “cannot be used to create independent obligations beyond those agreed upon . . . in the express language of the contract.”<sup>22</sup> A research scientist who cannot show discrimination has no claim for bad faith termination because the implied covenant of good faith and fair dealings cannot create any sort of restrictions not enumerated in the parties’ actual agreement.<sup>23</sup> A lender is not required by implied good faith obligation to negotiate a loan extension because “the implied covenant . . . does not create any new contractual rights.”<sup>24</sup> Nor does the alleged bad faith call of a loan state a claim because there is no such cause of action absent violation of express contractual restrictions.<sup>25</sup>

The roll call continues. In one case, when a terminated distributor sued the manufacturer for improperly taking its customers, the court dismissed the claim for legal insufficiency because the contract was silent on the subject.<sup>26</sup> The same approach was taken in another case with respect to allegations of bad faith under an acquisition agreement.<sup>27</sup>

---

22. *Granite Partners, L.P. v. Bear, Stearns & Co.*, 17 F. Supp. 2d 275, 306 (S.D.N.Y. 1988).

23. *Sundaram v. Brookhaven Nat'l Labs*, 424 F. Supp. 2d 545, 584 (E.D.N.Y. 2006) (“[T]he duty does not create new contractual rights that are not enumerated in the express contract . . . . Nor does the implied covenant provide an ‘independent basis of recovery.’”).

24. *Geler v. Nat'l Westminster Bank*, 770 F. Supp. 210, 215 (S.D.N.Y. 1991).

25. *Fasolino Foods Co. v. Banca Nazionale del Lavoro*, 961 F.2d 1052, 1056 (2d Cir. 1992) (“Under New York law, parties to an express contract are bound by an implied duty of good faith, ‘but breach of that duty is merely a breach of the underlying contract.’”).

26. *Ari & Co. v. Regent Int'l Corp.*, 273 F. Supp. 2d 518, 523 (S.D.N.Y. 2003) (“Finally, the breach of the covenant of good faith claim must be dismissed because it seeks to recover for obligations that were not explicitly part of the Agreement. New York law is clear that the implied covenant cannot be used to create independent obligations beyond the contract.”).

27. *Wolff v. Rare Medium, Inc.*, 210 F. Supp. 2d 490, 497 (S.D.N.Y. 2002) (“[T]he obligation of good faith does not create obligations that go beyond those intended and stated in the language of the contract.”).



## A Critique

It may well be that the results in all or most of the cases I have just referenced are correct on the merits, but their reasoning is suspect. With the enactment of Article 2 of the Uniform Commercial Code, and the preparation and adoption of Restatement (Second) of Contracts, it is said that contract law has evolved from set rules of across-the-board application to standards which address the potentially unique realities of transactional context.<sup>28</sup> Hence, the implied covenant of good faith especially protects the so-called “dependent party” from the exercise of bad faith discretion by the other. A prolific author on this topic, Professor Burton, went so far as to suggest that good faith restrictions are a true policing mechanism most directly activated when the stronger party actually intends to recapture the freedom of action he has relinquished to induce the bargain.<sup>29</sup>

While there has been criticism of the Burton approach,<sup>30</sup> there is certainly a moralistic flavor to implications of good faith requirements. Perhaps that justifies a focus on the subjective intent of the party accused of bad faith.<sup>31</sup> Cardozo may have been ahead of his time in this regard. Where the transactional context was that of “all eggs in one basket” dependency, the holder of the exclusive could not deliberately leave the other in the lurch given her perceived contrary expectations. We are left with an amalgam of the objective and the subjective, and with a joining of the manifested and the presumed. Interpretation and gap-filling are not sequenced but melded. The exhaustion of all interpretive steps is not needed to create a “gap” designed to

---

28. See generally Richard E. Speidel, *Restatement Second: Omitted Terms and Contract Method*, 67 CORNELL L. REV. 785 (1982).

29. Stephen J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 378-94 (1980). According to this work, the subjective intent of one alleged to have acted in bad faith is of “central importance.” *Id.* at 384 n.7.

30. Summers, *supra* note 12, at 830-34.

31. *E.g.*, *Zilg v. Prentice-Hall, Inc.*, 717 F.2d 671 (2d Cir. 1983) (using the “honesty in fact” test to define certain good faith obligations of a publisher). See *Market Street Assocs. Ltd. P’ship v. Frey*, 941 F.2d 588, 594 (7th Cir. 1991) (Where Judge Posner, after rejecting altruism as a good faith standard, states that “[i]t is another thing to say that you can take deliberate advantage of an oversight by your contract partner.”). See also U.C.C. § 2-103 (2005) (defining good faith to include “honesty in fact”).

leave room for mandated observance of perceived minimum deficiencies in the course of performance.

It may also be that cases limiting good faith restrictions to the performance of actual undertakings are making the unsafe assumption that omission of reference to foreseeable issues bespeaks the shared intent to let the chips fall where they may.<sup>32</sup> “Gaps” also arise, however, where both parties, or at least the weaker one, choose not to place a potential “deal breaker” on the table. This may well be what happened in the franchise case discussed early on in this piece.

### Cases Using Gap Filling to Create Causes of Action Based on Judicially Created Terms

Obviously, there are many New York law cases fitting this description. Under the implied at law duties of cooperation and non-prevention, courts, for a long time, have seen fit to create obligations (and prohibitions) rather than merely to shape those which are already there. At times, there will be reference to some ill-defined custom and usage, but at times not. The fact that a publishing contract says nothing about releasing a competing work on the same subject does not mean there is no breach of the implied duty of good faith if it does so.<sup>33</sup> One who offers to pay a commission if his counterparty can purchase a parcel below a certain price cannot overbid that party at auction to deprive him of any payment.<sup>34</sup> One who is to pay commission “on closing” still owes that payment if she breaches the contract of sale. Implicit in the grant of an exclusive concession is the licensee’s obligation to attempt to secure the requisite permits.<sup>35</sup> Implicit in a grant of conversion rights to bondholders is the obligation to provide notice of intended redemption so that

---

32. *See, e.g.*, *Transatlantic Fin. Corp. v. United States*, 363 F.2d 312 (D.C. Cir. 1966) (for a traditional approach in cases of claimed “cost impracticability”). *See generally* U.C.C. § 2-615, cmt. 1 (2003) (noting that there can be impracticability “because of unforeseen supervening circumstances”).

33. *Van Valkenberg v. Hayden Pub. Co.*, 330 N.Y.S.2d 329 (1971).

34. *Patterson v. Meyerhofer*, 97 N.E. 472 (N.Y. 1912) (this decision predates *Wood*).

35. *Swartz v. War Mem’l Comm’n of Rochester*, 267 N.Y.S.2d 253 (App. Div. 1966).

conversion rights may be exercised.<sup>36</sup> Surely, in such cases, as in *Wood*, the courts are not dealing with the unforeseen or the remote. Said one court by way of explanation in a case finding a breach despite the absence of a specific covenant dealing with the issue at hand:

Under New York law, there exists in every contract an implied covenant of good faith and fair dealing. The covenant is violated when a party to a contract acts in a manner that, although not expressly forbidden by any contractual provision, would deprive the other of the right to receive the benefits under their agreement.

. . . .

[I]t seems doubtful that the covenant of good faith—even as informed by industry customs—permits a promoter, who has contracted to advance the fortunes of two fighters who compete in the same class, both of whom the promoter has under exclusive contract, actively to further one fight *outcome* over another in a title bout the promoter has arranged between them . . . . To hold it acceptable for such a promoter to lead a fighter to the ring, only to then act partially to influence the fight outcome against the same fighter's interest, does not appear to comport with the notion of fair dealing that inheres in every contract.<sup>37</sup>

As one might expect, there are decisions which have had to confront directly an assertion that good faith cannot create "new" duties to coexist with those in the contract. These cases hold that an independent claim/cause of action does in fact exist for breach of the implied duty of good faith even when no actual breach of express terms is, or can be, set forth.

In *Chase Manhattan Bank, N.A. v. Keystone Distributors, Inc.*,<sup>38</sup> a court was faced with a bank's assertion that it had unlawfully been deprived of revenues under a contract arrangement with several mutual funds. The court granted summary judgment dismissing a claim for breach of contract, but refused to dismiss a claim for breach of the implied covenant of good faith and fair dealing because "[a] party may be in breach of the

---

36. *Metro. Life Ins. Co. v. RJR Nabisco, Inc.*, 716 F. Supp. 1504, 1517 (S.D.N.Y. 1989) (applying New York law).

37. *Don King Prods., Inc. v. Douglas*, 742 F. Supp. 741, 767-68 (S.D.N.Y. 1990) (citations omitted).

38. *Chase Manhattan Bank, N.A. v. Keystone Distribs., Inc.*, 873 F. Supp. 808 (S.D.N.Y. 1994) (applying New York law).

implied duty of good faith and fair dealing even if it is not in breach of its express contractual obligations.”<sup>39</sup>

Highly instructive is a very recent federal case applying New York law in which a distributor of luxury cars asserted that the manufacturer of Lamborghini vehicles had wrongfully stripped it of exclusivity and arbitrarily refused to approve its application for a second dealership.<sup>40</sup> The dealership agreement said nothing about either subject, and contained a merger clause as one would expect.<sup>41</sup> The court concluded that a combination of the merger clause and the statute of frauds barred claims for “breach of express contract” and dismissed them.<sup>42</sup> However, the court permitted plaintiff’s grievance to go forward as a separately pled “cause of action for breach of the implied covenant of good faith and fair dealing.”<sup>43</sup> In so doing, the court held sufficient the complaint’s allegations of bases for the reasonable expectations said to be violated, in part relying on oral representations otherwise unactionable because of the statute of frauds.<sup>44</sup>

An even more recent trial court discussion of why a cause of action can be based directly on an implied covenant, even absent violation of express provision, is very emphatic on that point:

Plaintiffs have not alleged that defendants breached a specific provision of their provider agreements, but that they breached their duty of good faith and fair dealing by (1) belatedly seeking payment refunds on claims that were previously authorized orally, of which they had notice, and which they had months or years to investigate; (2) withholding payments on false pretenses (with respect to Empire and Horizon); (3) withholding payments on unrelated claims; and (4) doing all of these things in consultation and coordination with each other. In my May 18 Order, I concluded that the complaint properly stated a cause of action for

---

39. *Id.* at 815.

40. *See* Manhattan Motorcars, Inc. v. Automobili Lamborghini, S.p.A., No. 07 Civ. 978, 2007 WL 1988144, at \*1 (S.D.N.Y. July 9, 2007).

41. *Id.* at \*2.

42. *Id.* at \*7.

43. *Id.* at \*8.

44. *Id.*

breach of an implied covenant of good faith and fair dealing, and I now affirm that opinion.<sup>45</sup>

The New York Court of Appeals has spoken as well. In a 2002 case, the sponsor of a cooperative conversion was alleged to have stymied shareholder expectations by failing to dispose of its unsold shares within a reasonable time.<sup>46</sup> The trial court had dismissed the cause of action because the offering plan was silent on this subject.<sup>47</sup> In response to a certification from the appellate division, the court of appeals, for those lower courts which were listening, had this to say:

While the duties of good faith and fair dealing do not imply obligations "inconsistent with other terms of the contractual relationship," they do encompass "any promises which a reasonable person in the position of the promisee would be justified in understanding were included."<sup>48</sup>

In still additional cases, even express reservations of discretion do not thwart implied at law requirements of fairness.<sup>49</sup> A watch manufacturer's express reservation of discretion on filling orders does not prohibit a cause of action based on bad faith delays in doing so.<sup>50</sup> A securities broker's power to liquidate customer holdings, stated to be at its full discretion, must nonetheless be exercised in good faith.<sup>51</sup> Indeed, in a very revealing case, a franchisee had alleged that franchisor's actions, while left to franchisor's discretion by agreement, were nonetheless wrongful.<sup>52</sup> The Second Circuit held it to be reversible error not to give an independent charge on the implied duty of good faith in addition to an express contract charge:

DMG claims that Carvel, in its dealings with DMG, unjustifiably frustrated DMG's efforts to perform under the distributor-

---

45. *Gross v. Empire Healthchoice Assurance, Inc.*, No. 602848-2005, 2007 WL 2066390, at \*1 (N.Y. Sup. Ct. July 18, 2007).

46. *511 W. 232nd Owners Corp. v. Jennifer Realty Co.*, 773 N.E.2d 496 (N.Y. 2002).

47. *Id.* at 498.

48. *Id.* at 500-01 (citations omitted).

49. *E.g.*, *Zilg v. Prentice-Hall, Inc.* 717 F.2d 671 (2d Cir. 1983).

50. *Maddaloni Jewelers, Inc. v. Rolex Watch U.S.A., Inc.*, 838 N.Y.S.2d 536 (App. Div. 2007).

51. *Modern Settings, Inc. v. Prudential-Bache Secs., Inc.*, 936 F.2d 640, 644 (2d Cir. 1991).

52. *Carvel Corp. v. Diversified Mgmt. Group, Inc.*, 930 F.2d 228 (2d Cir. 1991).

ship agreement and thus breached the implied duty of good faith. . . .

. . . While the distributorship agreement gave Carvel considerable discretion with regard to advertising, store location, wholesale sales, and other matters, this did not relieve Carvel of its duty to act in good faith.

. . . .

Under the circumstances, a simple, direct instruction on the implied duty of good faith was called for; a “subsumed” good faith charge was not sufficient. . . . Without this specific guidance from the court, the jury was left with no legal context in which to assess the significance of the bad faith evidence offered by DMG.<sup>53</sup>

Here, the tandem interaction of the express and implied-at-law creates a tension in which the latter prevails. We have, in effect, “interpretation as a matter of law.”

### A Reconciliation

Admittedly, the use of good faith to create obligations as to which the actual agreement is silent lends an air of unpredictability to the outcome of certain types of disputes. But what is the alternative? There are obviously countless potential situations in which rigid adherence to express terms would either thwart reasonable expectations or else foreclose any sort of “minimum decencies” analysis. Putting a good faith gloss on express terms is only a partial solution, and even the willingness to go that far will create uncertainty in cases of competing equities. That is the nature of norms which cannot be reduced to mathematical equation.

There are, of course, wholly legitimate reasons to refuse to engraft implied at law terms onto an actual agreement, but a conclusion that such implication is improper whenever it would create “new” duties rather than to regulate performance of actual undertakings is not a good one. The most common reason to refuse legal implication of additional unspecified undertakings is that the claimant fails to plead facts supporting a meaningful inference of violation of reasonable expectations. Similarly, the absence of a “gap” to be plugged with unwritten good faith restrictions may be shown by prevailing party prac-

---

53. *Id.* at 230-31.

tice, or accepted (and acceptable) custom and usage.<sup>54</sup> It might also be that the requested gap filler would be inconsistent with public policy, or of a type best suited to legislative or agency intervention. This would explain those cases refusing to impose restrictions on at-will employment.<sup>55</sup> Also, in many instances, one can directly extrapolate from what Cardozo termed actual intentions “imperfectly expressed,” thus to render at law supplementation less paramount or even unnecessary.

Part of the confusion about the proper use of at-law good faith requirements may be attributable to the fact that different types of “gap fillers” serve very different functions. Where interpretation permits a conclusion that a party assumed the risk of a harsh supervening contingency, a court normally ought not use implication as a matter of law to supply an omitted term excusing performance. Here, we would have a classic example of where a court should “interpret, then stop.” This would not be merely because of contractual silence as to what happened, but because contract law and underlying policy recognize that contracting parties should usually be free to allocate these types of risk.<sup>56</sup>

On the other hand, the law has increasingly seen to it that certain types of contracts are to be governed by various subspecies of good faith type gap-fillers (affirmative efforts, cooperation and non-prevention) designed to do more than regulate how actual terms of agreement are performed. This is increasingly true of long-term relational contracts, even those not deemed fiduciary. It is here, in fact, that courts are most apt to construe as a matter of law to deal with evolving circumstances. So too, when it comes to the use of standardized agreements, the Restatement (Second) of Contracts goes so far as to require that meaning be determined based on prototypical “reasonable expectations,” irrespective of what the contract actually says, or even whether the party provided with the form has actually

---

54. *E.g.*, *E. Air Lines, Inc. v. Gulf Oil Corp.*, 415 F. Supp. 429 (S.D. Fla. 1975) (“fuel freighting” by airline is not a violation of its obligation to set its fuel requirements in commercial good faith).

55. *E.g.*, *Murphy v. American Home Prods. Corp.*, 448 N.E.2d 86 (N.Y. 1983).

56. Even this approach has potential “minimum decencies” limitations. *See, e.g.*, U.C.C. § 2-615 cmt. 8 (2003) (dealing with impracticability). “[T]his section itself sets up the commercial standard for normal and reasonable interpretation and provides a minimum beyond which agreement may not go.” *Id.*

read it.<sup>57</sup> Legislatures and administrative agencies increasingly dictate contractual content, or else ban certain types of provisions. Whatever one's views on the matter, particularly where it comes to the non-arm's length, contractual construction has taken on a highly mandatory flavor steeped in legislated content.

In *Wood v. Lucy*, Cardozo was early to realize that gap-fillers do far more than to shape performance of express terms. Contractual silence, even in cases of the eminently foreseeable, did not preclude legal implication of good faith requirements. Such implication should only be thwarted if the overall transactional dynamic, under a holistic assumption of risk or some other "reasonable expectations" analysis, so dictate. It took quite some time for other courts to accept this approach, and there are still surprising pockets of resistance to this day.

---

57. RESTATEMENT (SECOND) OF CONTRACTS § 211(2)(3) (1981).