

IMPLIED TERMS IN AUSTRALIAN CONTRACT LAW: A REAPPRAISAL AFTER *UNIVERSITY OF WESTERN AUSTRALIA v GRAY*

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I INTRODUCTION

Implied terms are found in most, if not all, contracts. Parties do not, and cannot, expressly provide for all events that may arise in the course of their dealings with each other. There are gaps which courts are ‘asked to fill ... by implying a term in favour of one or other of the parties’.¹ In Anglo-Australian contract law, terms are said to be implied on two bases — either as individual terms introduced on ‘an ad-hoc (factual) basis to make a *particular contract* work’ or as pre-established terms which have become more generalised ‘incidents of *particular classes* of contract’.² Whether a term is to be implied-in-fact or implied-in-law, the prior question that arises for judicial determination is what test should be applied to make the implication sought. Current orthodoxy proposes a test based generally on necessity, but says that the test of necessity required for implied-in-fact terms is grounded in notions of business efficacy, and that this differs from the type of necessity required for implied-in-law terms which is said, somewhat unhelpfully, to be based on ‘wider considerations’.³ In our view, the distinction is a questionable one which simply leads to confusion. It should be discarded in favour of a more coherent approach that fits with the fundamental idea of contract as an expression of the parties’ objectively determined intention. This end may now be a real possibility in light of the recent⁴ decisions of the Full Federal Court of Australia in *University of Western Australia v Gray*⁵ and of the Privy Council in *Attorney-General of Belize v Belize Telecom Ltd*.⁶ In this paper we examine first the decision in *Gray* in some detail, noting the reasoning of both the Full Court and of French J, as he then was, at first instance. We then examine the notion of a test of necessity as the basis for the implication of terms, including at this point an analysis of the decision in *Belize*. This leads into a concluding section where we argue that there is no basis for trying to maintain any distinction of substance between terms implied-in-law and terms implied-in-fact, since all judicially implied terms are properly understood as justifiable only on the basis

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1 J Paterson, ‘Terms Implied in Fact: The Basis for Implication’ (1998) 13 *Journal of Contract Law* 103, 103.

2 J Carter, E Peden and G Tolhurst, *Cases and Materials on Contract Law in Australia* (LexisNexis Butterworths, 5th ed, 2007) 246 (emphasis in original).

3 *Liverpool City Council v Irwin* [1977] AC 239, 255 (Lord Wilberforce); *Lister v Romford Ice and Cold Storage Co Ltd* [1957] AC 555, 576 (Viscount Simonds).

4 The reference to ‘recent’ decisions in this article must be considered in light of the fact that this article was accepted for publication in November 2010.

5 (2009) 179 FCR 346 (‘*Gray*’).

6 [2009] 1 WLR 1988 (‘*Belize*’).

of the test expressly announced by Lord Hoffmann in *Belize* in the context of a case dealing with what would traditionally be regarded as a term implied-in-fact.

II UNIVERSITY OF WESTERN AUSTRALIA v GRAY

A The Facts

Dr Gray was employed as a Professor of Surgery at the University of Western Australia ('UWA') in January 1985 and remained there as a full time employee until 1997, when he accepted a 0.3 fractional appointment until his resignation in November 1999. His terms of employment, in common with most university academic staff, revolved around teaching and research. In the course of carrying out the latter, Gray was alleged to have made inventions which generated the intellectual property rights which became the subject of the dispute. Both prior to and during his tenure at UWA, Gray had carried out extensive research into the treatment of liver cancer by using microspheres which were injected into a patient's blood vessels in the liver to target tumours in the organ with anti-cancer treatments. During his time at UWA, Gray invented, in conjunction with various colleagues, three microsphere technologies — described as the SIRT, the DOX and the THERMO invention streams.⁷ A number of provisional applications for patents in respect of the various technologies were made. In 1997, Gray assigned the intellectual property rights that he purported to own in the inventions to Sirtex Medical Limited ('Sirtex') in return for a substantial number of shares in the company. By 2000, he was a director of Sirtex which in that same year was publicly floated, its remit being to commercialise and market the microsphere technologies. Despite UWA's becoming aware of Gray's involvement in Sirtex as early as 1999,⁸ the institutional wheels turned slowly. It was not until December 2004 that UWA issued proceedings in the Federal Court⁹ against Gray and Sirtex, claiming ownership of the patented inventions Gray had made during his employment at UWA. UWA sought declaratory relief against Gray that he 'held his shares and options to take up shares in Sirtex on trust for UWA' and orders that he 'transfer ... [the shares] to UWA and account to it in respect of the benefits obtained by him by reason of the shares and the options'.¹⁰ As against Sirtex, UWA likewise sought declaratory relief that Sirtex held all its proprietary interests in the patents on trust for UWA and orders that it transfer the patents to

7 *Gray* (2009) 179 FCR 346, 351 [6], 353 [23].

8 *Ibid* 356 [44].

9 The litigation, attended by 20 interlocutory hearings, was extremely long and complex, involving UWA's claims against three parties, Gray, Sirtex and the Cancer Research Institute (the last mentioned party settling prior to trial); counterclaims by the three parties against UWA; and cross claims by Sirtex against Gray for breach of director's duties and contravention of the *Fair Trading Act 1987* (WA). It culminated in a trial lasting 50 days, the tendering of 1000 documentary exhibits, the generation of 4568 pages of transcript and a written judgment by French J of 1619 paragraphs: *University of Western Australia v Gray (No 20)* (2008) 246 ALR 603.

10 *Gray* (2009) 179 FCR 346, 352 [9].

the latter.¹¹ French J at first instance, dismissed UWA's claims against both Gray and Sirtex and, save for upholding Sirtex's cross claim against Gray for breach of director's duty and breach of the *Fair Trading Act 1987* (WA), dismissed all other cross claims. UWA appealed. Its appeal was based solely on its failed case against Gray.

B The Pleadings

The central elements of UWA's pleaded case against Gray were claims in breach of fiduciary duty by Gray and breach of the express terms of the contract of employment between it and Gray.¹² Despite this, '[t]he primary claims ultimately prosecuted by UWA, and rejected by French J, were founded upon a contractual term said to be implied by law into Dr Gray's contract of employment with UWA'.¹³ The lack of specific pleading of an implied term, a precise articulation of which never appeared at trial and was only proffered on the third day of the appeal hearing, was, so UWA argued, not of real concern because it was enlivened by the 'pleading as a whole'.¹⁴ The focus by UWA on the express terms of its contract with Gray and more particularly on Gray's purported breach of fiduciary duty (which was 'limited to a claim for misuse of UWA's property rights and interests ... [rather than] one of Dr Gray misappropriating an "opportunity" offered to UWA'¹⁵) might well have been at the expense of other matters which were not pleaded. Potential causes of action might have included breach of a term implied-in-fact (rather than implied-in-law) as founding UWA's right to the patented inventions,¹⁶ breach of an implied duty of good faith and fidelity,¹⁷ and breach of a duty of confidence.¹⁸ The Full Court expressly stated that it was not venturing a view on the likely outcome of the case had these other matters been pleaded. It listed them solely to emphasise how legally and factually confined was the principal question that actually arose for determination both at trial and on appeal.¹⁹

11 Ibid 352 [10].

12 Ibid 359–61 [73]–[83], where the Full Court highlighted certain aspects of the pleaded claims drawing from UWA's 'second further substituted statement of claim — a document that comprised 164 paragraphs extending over 70 pages': at [72].

13 Ibid 361 [84].

14 Ibid 362 [86].

15 Ibid 363 [93].

16 Ibid 363 [91].

17 Ibid 363 [92].

18 Ibid 363 [93].

19 Ibid 363 [94]. Had some of these issues been ventilated, various concerns that have been articulated about innovation and what role universities play may well have been addressed. See also Chris Arup, 'Employee Inventions: Labour Law Meets Intellectual Property' (2008) 21 *Australian Journal of Labour Law* 208.

C The Claim in Breach of Contract

The original 1985 contract of employment between UWA and Gray did not require Gray to assign any rights in intellectual property that he generated to his employer. Indeed, he was not even required to report any inventions that he made to UWA. The legal foundation for UWA's claim to ownership of the intellectual property rights associated with the inventions was founded, so it argued, upon an 'implied term of Dr Gray's contract of employment that intellectual property developed in the course of his employment belonged to UWA'.²⁰

UWA argued that the implied term derived from the duties ordained by the standard conditions of employment imposed on Gray as a professor of the University. These expressly required him:

- (i) to teach, to conduct examinations and to direct and supervise the work in his field in accordance with the Statutes and regulations of the University and the directions of the Senate;
- (ii) to undertake research and to organise and generally stimulate research among the staff and students; and
- (iii) to perform such other appropriate work as the Senate from time to time determined.²¹

UWA argued in particular that Gray's duty expressly to undertake research carried with it, in the words of French J, 'a duty to invent'²² which, in turn, founded the basis for implying a further term vesting ownership of Gray's inventions in UWA as his employer. The alleged duty to invent was central to the case as a whole. UWA contended on appeal (a contention that was not put at trial) that 'in the applied sciences, the duty to invent is relevant to a duty to research in the sense that the latter comprehends "a duty to make advances in the art" and that such a duty is, in fact, a duty to invent'.²³ While in form it might have been different, the substance of UWA's argument was the same as it had been before French J at trial and, in the event, it enjoyed as little success in its second airing in the appeal.

1 Implied Terms

The implied term sought by UWA was an implied-in-law term. This raised two principal matters for the Full Court's attention: 'first, the requirement that there be a recognised or commonly occurring class, type or kind of contract ... and, secondly, the test to be satisfied if the implication is to be made'.²⁴

In relation to the first matter, the Full Court emphasised that the case involved an employment contract between a university and an academic staff member as

20 *Gray* (2009) 179 FCR 346, 357 [53].

21 *Ibid* 371 [122].

22 *Ibid* 357 [53].

23 *Ibid* 372 [124].

24 *Ibid* 375 [137] (footnotes omitted).

a ‘recognisable sub-category of ... [the] larger class’²⁵ of employment contracts as a whole. This meant that the type of term that UWA was proffering could be implied against Gray, as an academic staff member, even if it would not be a feature of employment contracts in the way that other more generalised terms, such as an ‘employee’s duty to obey lawful and reasonable directions given by the employer that fall within the scope of the employment’,²⁶ were applicable to all employees. Moreover, were the implied term to be accepted, it ‘would in time become a legal incident of the category of contract involved’²⁷ with binding effect, at its narrowest, on academic staff members who created patentable inventions or, more widely, on academic staff members who created any form of intellectual property whatsoever.

Of great moment, therefore, was the test that should be applied when implying terms into a contract as a matter of law where such a term had not previously been recognised as an incident of the type of contract in question. The Full Court noted that more than reasonableness was required; that the test was the ‘elusive’²⁸ one of necessity,²⁹ and that its primary concern was ‘whether the enjoyment of contractual rights could be rendered nugatory or worthless, or seriously undermined if no implication is made’.³⁰ The Full Court stated that the test of necessity for implied-in-law terms differed from the necessity concept required for business efficacy in implied-in-fact terms in that the former was informed by ‘more general considerations’.³¹ These general considerations had been said to require regard to be had to the nature of the contract; that public policy and justice issues be taken into account; and that an implied term be refused if the social consequences would be detrimental. Indeed, the very wide and significant role ascribed to such general considerations and in particular to ‘[t]he necessary tie between implications in law and considerations of policy’³² had resulted in the frank suggestion by Samuels JA in *Simonius Vischer & Co v Holt & Thompson*³³ ‘that the imposition of terms as a matter of law amounts to no more than the imposition of a legal duty where the law thinks policy requires it’.³⁴ The Full Court was not prepared to overrule or discard the ‘necessity’ test, preferring instead to leave that matter to the High Court.³⁵ It nonetheless emphasised the considerable latitude in the application of the test and endorsed Samuels JA’s statement as being particularly helpful in demonstrating the role that policy considerations

25 Ibid 375–6 [138].

26 Ibid.

27 E Peden, ‘Policy Concerns behind Implication of Terms in Law’ (2001) 117 *Law Quarterly Review* 459, 459.

28 *Gray* (2009) 179 FCR 346, 377 [141].

29 *Liverpool City Council v Irwin* [1977] AC 239; *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410; *Breen v Williams* (1996) 186 CLR 71.

30 *Gray* (2009) 179 FCR 346, 377 [140].

31 Ibid 377 [142] (footnotes omitted).

32 Ibid 378 [144].

33 (1979) 2 NSWLR 322, 348.

34 *Gray* (2009) 179 FCR 346, 378–9 [145].

35 Ibid 379 [147].

played in determining ‘whether *or not*’ to imply a term as a matter of law.³⁶ In some instances, the ramifications of implying a term would be so complex that it would simply be inappropriate for a court (as opposed to the legislature) to do so.³⁷ This, as it transpired, was, according to the Full Court, one of those occasions.

2 *Owning an Employee’s Inventions*

The Full Court accordingly turned its attention to the more particular issue of implied terms in the context of inventions made by employees. It reiterated Nettle J’s statement in *Victoria University of Technology v Wilson*³⁸ that:

It is an implied term of employment that any invention or discovery made in the course of the employment of the employee in doing that which he is engaged and instructed to do during the time of his employment, and during working hours, and using the materials of his employers, is the property of the employer and not the employee. Having made a discovery or invention in course of such work, the employee becomes a trustee for the employer of that invention or discovery, and he is therefore as a trustee bound to give the benefit of any such discovery or invention to his employer.³⁹

The key point here is that ‘an employee’s trusteeship of an invention’ for the employer arises only in respect of those inventions that either she is expressly required to make or she makes in the course of the work she is employed to do. Absent those circumstances, there is simply no basis to imply ownership of the inventions in the employer. It is not surprising, therefore, that in these types of cases courts constantly struggle with difficult issues of defining the ‘actual subject matter and purpose of the employee’s engagement itself and with the question: “[w]hat is it that he is employed to do?”⁴⁰ Such difficulties of definition are, as the Full Court pointed out, compounded by various factors including: the latitude that employees might have in deciding how to employ their inventive faculties; the seniority of their position which might saddle them with fiduciary duties and oblige them to hold all inventions they have made for the benefit of their employers; and/or whether their duty to invent has changed over time in line with the changing nature of their employment.⁴¹

36 Ibid 178 [145].

37 Ibid 379 [146].

38 (2004) 60 IPR 392.

39 Ibid 422 [104]. The Full Court in *Gray* (2009) 179 FCR 346, 380 [151] referred to *Sterling Engineering Co Ltd v Patchett* [1955] AC 534 in explaining that the origin of this rule is to be found in the master/servant relationship which deems the master the owner of any product generated from the work that the servant is paid to do.

40 *Gray* (2009) 179 FCR 346, 381 [152].

41 Ibid 381–2 [155]–[157].

A further factor that impacts on the legitimacy of an implied term of ownership is the employee's duty of confidentiality.⁴² Breach of confidence gives an employer some measure of protection against the unauthorised communication and/or use of its secret information by its employee or by a third party. Confidentiality is assessed by weighing up various factors including, importantly in the context of the *Gray* case, how much time and money has been spent in researching or applying the information, the ease with which people could replicate the information, and the novelty of the technique embodied in the information.⁴³ The duty of confidence endures post-employment and so 'can pose a significant obstacle to the mobility of employees engaged in research-related employment having applications in science or technology'.⁴⁴ The Full Court emphasised that where employees were employed to carry out inventive work for their employers, disclosure of confidential information might prove to be a thorny issue, involving as it does disclosure of confidential information to the employee and the generation of confidential information by the employee. Although they would be precluded from disclosing confidential information to third parties, including fellow employees, without their employer's consent, internal disclosures to other members of a research team would be impliedly authorised.

3 *Gray's Employment*

No little importance attached to the context and conditions of Gray's actual employment in the university environment of UWA. The Full Court highlighted general themes that recurred in French J's analysis of Gray's tenure at UWA, and how he interacted with other academic staff members as well as with senior management figures.⁴⁵ Of greatest importance was the fact that Gray conducted research on a collaborative basis within a research team and carried out the research by seeking funding and grants from external bodies.⁴⁶ He did this on his own initiative rather than at the behest of UWA. Research projects proliferated⁴⁷ and often culminated in 'multi-authored journal articles and papers that dealt with research results, clinical trials, etc', as well as 'sole authored pieces by members of the research group'.⁴⁸ Evidence accepted by French J and recorded in some detail by the Full Court demonstrated Gray's research group's 'strong

42 Ibid 382 [159], where the Full Court described this duty like the implied terms about employee inventions, as 'an unhappy mixture of equitable obligation (the duty of confidence and fiduciary obligation) and implied terms (particularly, but not only, the duty of good faith and fidelity)' (references omitted).

43 Ibid 383 [163].

44 Ibid 383–4 [164].

45 Ibid 371–5 [125]–[133].

46 Gray's track record was very impressive. He and members of his team made 41 successful NH & MRC funding applications. He was the driving force in setting up two incorporated bodies to give support to his research program. His attempts to commercialise the inventions commenced in the late 1980s when he approached UWA's Uniscan, followed by unsuccessful attempts to woo commercial partners, before seeking venture capital support in 1994: *Gray* (2009) 179 FCR 346, 373–4 [131]–[132].

47 Contributed to variously by researchers from other institutions and by a moving feast of junior academics whose engagements with the projects depended on the availability of funding: ibid 372–3 [127].

48 Ibid 373 [128].

commitment to the publication and dissemination of research results for the sake of developing new treatments and new approaches to cancer management'.⁴⁹ This dissemination, which started when Gray was employed by the University of Melbourne and which continued after he moved to UWA, took place in public and private fora, at research colloquia and conferences, 'without any concern about the disclosure of the new methodologies'.⁵⁰ The context of Gray's employment was thus highly significant. Indeed, the Full Court went further in expressing its regret that neither it nor the trial judge had been asked to consider Gray's duties to share and disseminate research results as part of his role as a teacher of students. It might have been 'unnecessary' but the Full Court was nonetheless minded to emphasise that it was 'the coalescence of teaching (with its dissemination of knowledge) and research (with its generation of knowledge) that is so characteristic of universities and (save in the case of the university researcher with no teaching responsibilities at all) differentiates the university academic from the researcher in private enterprise'.⁵¹ The emphasis ascribed to Gray's teaching role, as well as the collaborative nature of his research work, were important factors in how the Full Court responded to the implied term argument of UWA and played a pivotal role in the decision ultimately reached.

4 The Trial Judge's Decision

French J refused to imply a term vesting ownership of Gray's inventions in UWA. He viewed as critically important⁵² the difference in the relationship between academic staff and their university employer and the relationship between employees and commercial employers. The former is characterised by the free flow of research, ideas and information as an integral part of the core value of academic freedom. Monotti and Ricketson⁵³ pointed out that in this context, and in the absence of an express term, the incongruity of automatically imposing the same secrecy obligations on academic staff as are generally imposed on employees in other employment contexts is manifest. French J signified his strong agreement with the general tenor of these observations.⁵⁴ He also found that there was no duty imposed on academic staff not to disclose the results of research.⁵⁵ To the contrary, Gray was free to publish the results of his research.⁵⁶ Additionally, staff were free to choose whether, in carrying out their research, they would invent or not.⁵⁷ UWA's claim to ownership of the invention by means of an implied-in-law term was further weakened by the fact that academic staff had to be entrepreneurial in seeking funding from external organisations to fund

49 Ibid.

50 Ibid.

51 Ibid 371–2 [123].

52 *University of Western Australia v Gray (No 20)* (2008) 246 ALR 603, 656 [159].

53 A Monotti and S Ricketson, *Universities and Intellectual Property* (OUP, 2003) 6.66–6.67.

54 *University of Western Australia v Gray (No 20)* (2008) 246 ALR 603, 656 [159].

55 Ibid 656 [160], 930 [1366].

56 Ibid 930 [1366].

57 Ibid 656 [160].

their research and, as part of that process, had to be collaborative in conducting research with independent third parties.⁵⁸ The inexorable conclusion was that there was no basis to imply, as a matter of law, a term entitling UWA to claim ownership of an invention created by its academic staff.⁵⁹

5 The Appeal

On appeal, UWA raised two principal points. The first, that there was ‘no relevant distinction between a University as an employer and any other employer’,⁶⁰ was given short shrift by the Full Court. UWA ‘was created to serve the public purposes served by a “university”’⁶¹ — to offer courses, to provide research facilities and to confer degrees. It might, in common with other universities, have been compelled to pursue commercial activities in the more straitened circumstances of the past two decades but ‘[its] traditional public function as an institution of higher education’ still prevailed and Gray was entirely free to choose his own field of research regardless of whether it ‘advance[d] a commercial purpose of UWA’⁶² or not. Additionally Gray’s status in the university environment was significant. As an academic staff member he was more than simply an employee. He was a member of the ‘special purpose statutory corporation’⁶³ that comprised the University and was bound by its statutes, rules and regulations. To ignore his status as a member was to ignore a distinctive dimension of his relationship with the University. The explicit acknowledgement of the ‘two faceted character’ of Gray’s position as both a member and an employee of UWA underpinned the Full Court’s rejection of the second limb of the argument on appeal, that ‘Dr Gray’s contractual duty to undertake research was, in the circumstances, sufficient to bring it within the class of contract attracting the implied term’.⁶⁴ All academic staff, as members of the University, were free to choose their own research fields and to decide how, when and where they would publish the results of their research. Such ‘freedoms’ sat uneasily with the commonly implied duties imposed on employees, such as obeying all lawful and reasonable instructions issued by the employer or keeping secret all confidential information generated in the course of employment.

The Full Court accepted that there was a considerable divergence of views on the content of these freedoms. It emphasised them to endorse French J’s approach in taking note of Monotti and Ricketson’s concerns about the unhappy mix of implied terms and academic freedom and about the differences between universities and other organisations. In the Full Court’s view, ‘considerations of policy and consequentialist considerations are matters properly to be taken into account in deciding whether or not a term should be implied in law into a class or

58 Ibid 656 [161], 930 [1366].

59 Ibid 657 [164].

60 *Gray* (2009) 179 FCR 346, 387–8 [181].

61 Ibid 388 [183].

62 Ibid 388 [184].

63 Ibid 388 [183].

64 Ibid 387–8 [181].

type of contract'.⁶⁵ Furthermore, Gray's freedom to choose his area of research and to collaborate with others was consonant with the idea of 'academic freedom as a value' but at odds with UWA's argument about the 'principle of employer entitlement that informs the employment obligation as to inventions'.⁶⁶ This was a matter that had properly been taken into account by French J.⁶⁷

The key question to be answered by the Full Court therefore was what place an employee invention term would have and what employment context this would presuppose.⁶⁸ Inevitably, the imposition of an employee invention term, underpinned as it is by the employee's duty of confidentiality, would impact adversely on collaborative research and the exchange of ideas, on the publication of research and on the mobility of academic staff.⁶⁹ Were the term to be a freestanding one, unsupported by a duty of confidentiality, then its rationale would be that the employer was entitled only to the 'inventions' made in the scope of employment rather than to all of the intellectual property generated by the employee.⁷⁰ This would mean that '[t]he employee would have been free to destroy the potential patentability of an invention by progressively putting research results into the public domain'⁷¹ — a result which in the Court's words, 'would have been strange indeed'.⁷²

Examining the circumstances of Gray's employment and the research environment in which he operated in light of the above considerations led the Full Court to conclude, as had French J at trial, that there was no basis to imply the term sought by UWA because Gray 'had not been engaged to use his inventive faculty in an agreed way, or for an agreed purpose, for UWA's benefit'.⁷³ UWA's attempt to circumvent this by arguing that if Gray chose to invent something then that should be taken as doing work he was engaged to do and so entitle the University to ownership of the invention⁷⁴ was roundly dismissed:

Such a deemed, contingent duty to invent requires an untenable implication. It is not what Dr Gray's terms of employment required; there is no 'necessity' for it being implied by law into the employment contracts of university academic staff; and, importantly, it is inconsistent with the researcher's freedom to share and to publish research results.⁷⁵

Gray's freedom to publish the results of his research, unconstrained by a duty of confidence, was an important factor in the Full Court's decision not to

65 Ibid 389 [187].

66 Ibid 389 [188].

67 Ibid.

68 Ibid 389–90 [190].

69 Ibid.

70 Ibid 390 [191].

71 Ibid.

72 Ibid.

73 Ibid 390 [194].

74 Ibid 391 [196].

75 Ibid 391 [197].

make the implication sought.⁷⁶ The fact that Gray and his team had to and did solicit research funding from outside sources⁷⁷ was another telling factor. If the employee invention term depended in part upon the notion of having paid the piper to play the tune, then ‘the suggested implied term would allow UWA to reap where various entities had sown’.⁷⁸ Gray had immense standing as an independent researcher and grants were made to him personally with UWA’s role being only to administer and manage the grant monies.⁷⁹ He had to undertake this entrepreneurial role to carry out the research work that UWA ‘wished to foster, but seemingly could not fund’.⁸⁰ Dismissing UWA’s contention that this latter point was merely evidence of ‘Dr Gray’s post-contractual conduct ... [that could not] be used to negate an implication into a contract’,⁸¹ the Full Court held that it was proper to have regard to post-contractual conduct of Gray as the manifestation of ‘the known context and shared expectations of the parties in relation to raising funds for research at the time of contracting’.⁸² Finally, the Full Court endorsed French J’s view that the necessity for academic staff from UWA to collaborate with other researchers from external institutions in order to secure research funding sounded the death knell for a claim of exclusive ownership by one organisation via an implied term.⁸³

The cumulative effect of the above factors led the Full Court to conclude that the trial judge was correct in his finding that UWA failed to meet the threshold. The contract of employment between UWA and Gray as a member of academic staff was not of such a type or class as to justify the implication of an employee invention term. The more general ‘considerations of policy and consequentialist considerations’ operated, correctly in the Full Court’s view, ‘not only in support of making the implication into a class, *but also to negate the implication*’.⁸⁴ The case could quite easily have been decided on a single ground — that Gray had no duty to invent. But what was most influential at both levels of the Federal Court was ‘the distinctiveness of a university such as UWA and of academic employment in it as considerations relevant to the determination of the “threshold question”’.⁸⁵ In considering the material on UWA’s status as a university and on how Gray performed his employment, French J was, in the Full Court’s view, properly entitled to have regard to the more general issues of policy suggested by that material and this in turn entirely justified his reference to the writings of commentators and consideration of the value of academic freedom.⁸⁶ ‘After all,

76 Ibid 391 [198].

77 Ibid 391–2 [200].

78 Ibid.

79 Ibid.

80 Ibid.

81 Ibid 392 [201].

82 Ibid 392 [202].

83 Ibid 392 [204].

84 Ibid 393 [206] (emphasis in original).

85 Ibid.

86 Ibid 394 [209].

what was being made was a judgment as to the “necessity” of implying a term into a particular class or type of contract’.⁸⁷

III THE TEST OF NECESSITY AS THE BASIS FOR THE IMPLICATION OF TERMS

Unlike the approach adopted in the United States, where terms (whether implied-in-law or in-fact — no distinction is made between the two) are implied ‘for reasons of justice, fairness and policy’,⁸⁸ Anglo-Australian case law lays down criteria which must be satisfied before an implication is made. It also, as previously noted, differentiates between implied-in-fact terms and implied-in-law ones. The requirements for implied-in-fact terms were set out in the oft-quoted advice of the Privy Council in *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council*,⁸⁹ that

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.⁹⁰

The High Court of Australia has applied these criteria in cases where there is ‘a formal contract, complete on its face’,⁹¹ but in *Byrne v Australian Airlines Ltd*⁹² where there was no formal contract the Court adopted the more general test that a term will be implied ‘if, but only if, the implication of the particular term is necessary for the reasonable or effective operation of a contract of that nature in the circumstances of the case’.⁹³

This latter test appears to be very similar to the general test for implying terms in law as set out in *Liverpool City Council v Irwin*,⁹⁴ where it was stated that a term will be read into a contract ‘as the nature of the contract itself implicitly requires, no more, no less: a test, in other words, of necessity’.⁹⁵ This test has been approved and applied in Australia for implying terms in law.⁹⁶

87 Ibid.

88 *Gray* (2009) 179 FCR 346, 379 [147].

89 (1977) 180 CLR 266. This test was affirmed by the High Court of Australia in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1981–82) 149 CLR 337.

90 *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council* (1977) 180 CLR 266, 283 (Lord Simon).

91 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 422 (Brennan CJ, Dawson and Toohey JJ).

92 Ibid.

93 *Hawkins v Clayton* (1987–88) 164 CLR 539, 573 (Deane J); *ibid.* See also McHugh and Gummow JJ’s comments: at 442.

94 [1977] AC 239.

95 Ibid 254 (Lord Wilberforce).

96 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410.

In our view, the similarity in the expression of the two tests, as approved by the High Court, means that despite what the Full Court said in *Gray* about a different test of necessity applying in the context of implied-in-law terms as opposed to implied-in-fact terms,⁹⁷ this turns out to be a distinction without a difference. The key issue is a simple one: what is required to satisfy the necessity test for all implied terms? In our view, the recent advice of the Privy Council in *Attorney-General of Belize v Belize Telecom Ltd*,⁹⁸ delivered by Lord Hoffmann, is particularly instructive in the quest for an answer to this question.

Belize Telecommunications Ltd ('the company') was formed to effect the privatisation of Belize's state-owned monopoly telecommunications services provider, Belize Telecommunications Authority. Although selling off most of its financial interest to private investors, the Belize government sought initially to maintain its control in the enterprise through its shareholding in the company. There were three classes of shares in the company's share capital. These comprised one Special Rights Redeemable Preference Share ('the special share') which was initially issued to the government, class B shares and class C shares. The company's articles provided for the possible appointment and removal of up to eight directors: two by a majority of class B shareholders, up to four by a majority of class C shareholders and the remaining two by the special shareholder. However, under art 90(D)(ii), if the special shareholder also had class C shares amounting to 37.5 per cent or more of the issued share capital it could appoint and remove two of the four class C directors, ('the two special C directors') despite not being a majority shareholder of class C shares.⁹⁹

In 2004 Belize Telcom Ltd ('BT') acquired the special share and a majority of the B and C class shares from the government. As the holder of more than 37.5 per cent of the issued share capital it appointed the two special C directors. To finance the acquisition BT had borrowed monies from the government secured by the shares in the company. When BT defaulted on the loan a year later the government took back a large number of the pledged shares. This left BT with the special share and an amount of C shares that was less than 37.5 per cent of the issued share capital. The result of this event was that there was no person qualified to remove the two special C directors who had been appointed under art (90)(D)(ii). Article 112, which dealt with the circumstances of the office of director being vacated due to bankruptcy, insanity and the like, did not cover this peculiar situation. Did this mean therefore that the directors were unable to be removed — that they would stay in office unless and until they chose to resign, died in office, or fell within the ambit of art 112?¹⁰⁰ Such a result would, it was contended, be plainly 'absurd ... and the articles should be construed as providing by implication that a director appointed by virtue of a specified shareholding vacates his office if there is no longer any holder of such a shareholding'.¹⁰¹

97 *Gray* (2009) 179 FCR 346, 375 [136].

98 [2009] 1 WLR 1988.

99 *Ibid* 1990–1 [5]–[6].

100 *Ibid* 1992 [14].

101 *Ibid*.

On the premise that ‘the implication of a term is an exercise in the construction of the instrument as a whole’¹⁰² it followed, according to Lord Hoffmann, that there is only ever one question for the court, which is whether the implied term ‘would spell out in express words what the instrument, read against the relevant background, would reasonably be understood to mean’.¹⁰³ If each of the officious bystander tests articulated in *Shirlaw v Southern Foundries (1926) Ltd*,¹⁰⁴ the business efficacy test found in *The Moorcock*,¹⁰⁵ and the five-pronged test announced in *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council*¹⁰⁶ were to be given ‘a life of their own’,¹⁰⁷ that would subvert the ‘objectivity which informs the whole process of construction of contracts’¹⁰⁸ into one of ‘barren argument over how the actual parties would have reacted to the proposed amendment’.¹⁰⁹ These tests were, Lord Hoffmann opined, not separate or individual tests; they were no more than different ways in which judges had expressed the core idea that ‘the proposed implied term must spell out what the contract actually means, or in which they have explained why they did not think that it did so’¹¹⁰ because ‘a reasonable man would not have understood that to be what the instrument meant’.¹¹¹

In the *Belize* case itself the relevant background against which the articles of association had to be assessed comprised two principal factors. The first was that the power to appoint and dismiss directors from the Board ‘reflected the interests of the various participants in the company’¹¹² — the political and economic interests of the government through its holding of the special share and C shares and the economic interests of investors who held B and C classes of shares. The second factor was that the government’s powers in the company were ‘graduated according to its economic interest in the company at the relevant time’¹¹³ so that, for example, as holder of the special share as well as holding C shares comprising at least 25 per cent of the issued share capital it could block certain board or shareholder resolutions and if its shareholding of C shares was above 37.5 per cent it could appoint or remove special C class directors. Considered in the light of these factors, their Lordships concluded that the articles could not ‘reasonably mean that the Government Appointed Directors should remain in office after the Special Share has ceased to exist. They must be read as providing by implication that when the special share goes, the Government Appointed Directors go with it’.¹¹⁴

102 Ibid 1993–4 [19].

103 Ibid 1994 [21].

104 [1939] 2 KB 206, 227.

105 (1889) 14 PD 64, 68.

106 (1977) 180 CLR 266.

107 *Belize* [2009] 1 WLR 1988, 1994 [22].

108 Ibid 1884–995 [25].

109 Ibid.

110 Ibid 1995 [27].

111 Ibid.

112 Ibid 1995–6 [28].

113 Ibid.

114 Ibid 1996 [30].

This implication by construction test, so cogently articulated by Lord Hoffmann, has the virtue of being simple and couched in conceptual language that is familiar in any contract lawyer's lexicon. When it is formulated as an 'objective principle of reasonableness', it both draws the test for the implication of terms more closely into line with general principles of contractual interpretation and provides clarity. This ensures greater predictability and certainty in this area of law.¹¹⁵ It steers judges away from the potentially unbounded 'fairness, justice and policy' considerations favoured by courts in the United States and gives them a more principled approach to rely on when pronouncing on the rights and obligations of contracting parties. If this is the test to be adopted for implying terms-in-fact, which was the concern in *Belize* itself, it is, it is suggested, but a short step to recognising its appropriateness for implying terms-in-law as well. In classes of contracts there will also be objective meanings. This is readily apparent indeed from a close reading of the judgment in *Gray*. When the Full Court refused to imply the term sought by the UWA, relying on general 'considerations of policy and consequentialist considerations' to do so,¹¹⁶ it was doing no more than simply assessing Gray's contract of employment with UWA in terms of what any reasonable person in the shoes of either contracting party would have understood that contract to comprise.

IV DISTINGUISHING BETWEEN TERMS IMPLIED-IN-LAW AND TERMS IMPLIED-IN-FACT

This leads us to question whether there is any utility in persisting with the distinction between terms implied-in-law and terms implied-in-fact. An analogy may be instructive here. In the same way that all so-called institutional constructive trusts started off life as remedial constructive trusts,¹¹⁷ so too with implied-in-law terms — save for those terms implied-in-law by virtue of statute, all others started their life as terms implied-in-fact.¹¹⁸ The onus was originally on the party seeking to have the term incorporated into the contract by implication to show that it spelled out what the parties had objectively agreed, as any reasonable person would have understood, given the relevant background. Of course, once the term sought has been implied in a class of contracts and has accordingly acquired the status of an implied-in-law term, then the onus shifts.¹¹⁹ Its implication becomes a given — the onus is now on the party resisting its implication to show that 'a reasonable man would not have understood that to be what the instrument meant'.¹²⁰

115 Chris Peters, 'The Implication of Terms in Fact' (2009) 68 *Cambridge Law Journal* 513, 515.

116 *Gray* (2009) 179 FCR 346, 389 [187].

117 See Jessica Palmer, 'Attempting Clarification of Constructive Trusts' (2010) 24 *New Zealand Universities Law Review* 113, 126.

118 *Gray* (2009) 179 FCR 346, 375 [136].

119 *University of Western Australia v Gray (No 20)* (2008) 246 ALR 603, 930 [1364].

120 *Belize* [2009] 1 WLR 1988, 1995 [27].

The line of analysis undertaken by the Privy Council in *Belize* and the further argument presented in this paper gains some support from the approach of the High Court of Australia in *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd*.¹²¹ A company purchased a number of insurance policies through a broker. In respect of one policy the company paid the premiums due to the broker, but the broker did not pay them on to the insurer before the broker was wound up. The insurer then sought to recover the premiums it alleged had been unpaid directly from the company. The company argued that there were implied terms in its contract of insurance with the insurer to the effect that, first, the insurer could look only to the broker for payment of the premium, and, second, the payment by the assured to the broker was a good discharge of the debt owed to the insurer. These terms were said to be implied into the contract by virtue of trade custom. The High Court in a single judgment rejected the company's argument. In outlining four requirements for the implication of terms by virtue of custom or usage, the Court stated:

It has sometimes been said that the implication of a term into a contract does not depend on the parties' intention, actual or presumed, but on broader considerations ... But these statements are directed to situations in which the courts have been asked to imply terms amounting to rules of law applicable to all contracts of a particular class. The present case is of a different kind in which it may be necessary to speak of presumed intention. In matters of this kind, that phrase means no more than that the general notoriety of the custom makes it reasonable to assume that the parties contracted on the basis of the custom, and that it is therefore reasonable to import such a term into the contract.¹²²

Of course, the consequence that this analysis fails to articulate is this: had the Court upheld the company's argument and implied either or both of the terms sought, on the basis that there was indeed such a custom or usage in connection with insurance contracts, that term or those terms would in effect become implied-in-law into all insurance contracts for the future, *unless* the insurer in question could show that in respect of any particular insurance contract such implication would contravene the express terms of the contract.

A further instructive example is the well-known implied-in-law duty of confidentiality owed by a banker to his customer, deriving its modern recognition from the 1923 decision of a particularly powerful English Court of Appeal in *Tournier v National Provincial and Union Bank of England*.¹²³ All three judges expounded on the limitations and qualifications of the implied contractual duty, but Atkin LJ reflected on the nature of the implication. His Lordship cited¹²⁴ a passage from an earlier judgment of Scrutton LJ (with whom he was sitting in *Tournier* itself) in *Re Comptoir Commercial Anversois and Power*:

121 (1985–86) 160 CLR 226.

122 *Ibid* 237.

123 [1924] 1 KB 461.

124 *Ibid* 483.

[The Court] ought not to imply a term merely because it would be a reasonable term to include if the parties had thought about the matter, or because one party, if he had thought about the matter, would not have made the contract unless the term was included; *it must be such a necessary term that both parties must have intended that it should be a term of the contract*, and have only not expressed it because its necessity was so obvious that it was taken for granted.¹²⁵

Atkin LJ interpolated that ‘the test ... is not merely what the parties, as fair and reasonable men, would presumably have agreed upon, but what the Court considers they must necessarily have agreed upon ...’¹²⁶ This seems not to introduce any new factor beyond the parties’ objectively ascertained intention, which makes the approach of Atkin LJ quite consistent with that taken by Lord Hoffmann over 80 years later. Thus the banker’s duty of confidentiality is a term implied-in-law into the banker–customer contract, and the implication is a matter of construction. Furthermore, as Bankes LJ made clear (and agreed with by both Atkin and Scrutton LJJ), it is open to the customer to waive the duty as he decides. The role of intention could not be any clearer.

Outside of terms implied into contracts by force of statute, all implied terms depend for their existence on a true construction of the contract and the test as applied by Lord Hoffmann in *Belize* is applicable across the board: ‘is that what the [contract], read as a whole against the relevant background, would reasonably be understood to mean?’¹²⁷ The distinction in the context of judicially implied terms usually drawn between terms implied-in-law and terms implied-in-fact is not a distinction of substance but one of process. It does not and should not introduce different notions of necessity, since there is only one, founded upon the true construction of the contract itself. What it does is tell the parties which one of them has the onus of establishing the implied term in the contract between them. It is analogous to some of the presumptions so beloved of equity, such as the presumption of a resulting trust, or the presumption of advancement, or the presumption of undue influence. Another analogy could be drawn with the *contra proferentem* rule. The Full Court in *Gray* was correct not to imply into the contract between Gray and UWA the term sought by UWA, but that was not because what was at issue was a term implied-in-law and there were reasons of policy not to do so, but rather because that was not what the contract, read as a whole against the relevant background, would reasonably be understood to mean.

125 [1920] 1 KB 868, 899–900 (emphasis added).

126 *Tournier v National Provincial and Union Bank of England* [1924] 1 KB 461, 483–4. Essentially the same analysis was presented by Dixon J in *Gullett v Gardner* (1948) 22 ALJ 151 as discussed by Priestley JA in *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 262–3. Priestley JA indeed cited Dixon J’s observations for the proposition that they ‘may also illustrate that the sharp distinction between the two kinds of implication [implied-in-fact and implied-in-law] may, at least in some cases, be more a matter of form than substance’: at 263.

127 *Belize* [2009] 1 WLR 1988, 1994 [21].