

UNIVERSITY OF TAMPERE
Department of Management Studies

**THE PRINCIPLE OF GOOD FAITH IN EUROPEAN
INTERNATIONAL TRADE**

Business Law
Master's Thesis
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1. ABSTRACT

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The processes of integration and harmonization of European contract law are the positive tendencies in the modern development of different national legal systems. The general principles of law should become the unifying elements of the modern European contract law; one of those principles is the principle of good faith. Therefore, the purpose of this Master's Thesis was to research understanding of the principle of good faith in the European and international legislation and legal practices; the focus was made in the contract law and international trade.

The theory part of the research, which performed after orientation to the subject and identification of the theoretical backgrounds, is based on literary research and overview of national legislation and legal practices of European countries. It presents the study of historical development of the principle of good faith, the analysis of understanding of the principle in legal doctrine, and the overview of differences and similarities in the legislative consolidation and the application of the principle of good faith among European countries. Eight European countries were analyzed; the countries were chosen from different legal families, due to specialties in the understanding of the principle of good faith. In the practical part, the principle of good faith was researched in the light of the European and international legal acts, the judgments of the European Court of Human Rights, and preliminary rulings of the European Court of Justice. About 60 cases of European courts and 13 legal acts were analyzed in the study to obtain sufficient amount of information. The judgments were grouped in accordance with the way of application of the principle of good faith. Such grouping helped to detect the conditions of application and the elements of the content of the principle of good faith.

With the collected and analyzed information it was possible to determinate the common core in understanding of the principle of good faith in international trade and contract law, to give comprehensive definition for the principle, to define its elements, grounds and conditions for application. In addition the national specifics in understanding of the principle were identified. This research can be used as a doctrinal base for the regulatory developments in national legal systems and for national legal practices, for example, for the renewals of Civil Code in Russian legal system.

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3. LIST OF ABBREVIATIONS

BGB	Bürgerliches Gesetzbuch (German Civil Code 1900)
EU Treaty	the Treaty on functioning of European Union 2007
ECHR	European Court of Human Rights
ECJ	European Court of Justice
ECR	European Court Reports
EU	European Union
ICC	International Chamber of Commerce
OJ	Official Journal of the European Union
PECL	Principles of European Contract Law
UPICC	The UNIDROIT Principles of International Commercial Contracts 2004
§, Art.	Article

4. INTRODUCTION

4.1. Subject of the study

Since the second half of the 20th century, international trade has been developing world-wide. Therefore, the legal regulation of international trade, particularly in financial, commercial, and service sectors, is becoming more sophisticated. Evidently, this tendency emerges within European countries where the number of legal acts regulating international trade has increased. Every Member State of the European Union applies common provisions which arise from EU statutes, conventions, treaties, directives, and rules developed by the European Court of Justice (Zimmermann & Whittaker 2000, p.8). Without common legal clauses based on the cultural solidarity and unity of legal principles, the political existence of the EU would be impossible. However, a major difference between the Member States is every country's specific understanding of the common provisions (Smits 2005, pp. 9, 11). Primarily, this claim addresses the area of private law.

The main goal of the modern development of united supranational law is harmonization and unification of the rules of substantive law, on which the law of obligations is based and, (Zimmermann & Whittaker 2000, pp.8-12) ultimately, the European Code of Contracts will appear (Smits 2005, pp. 1-2; Zimmermann & Whittaker 2000, p.12; Micklitz 1995, p. 271). The Code should be founded on legal customs, practices and principles, which are developed in the national legal systems. One of those principles is the legal principle of *good faith*, which should become a unifying element of European contract law.

The terms which are used to designate *good faith* vary within the national legal systems of the different European states (Ratio 2000, p. 327). The Roman law name "bona fides" (Zimmermann 2000 & Whittaker, p.16), nowadays, is not mentioned in any legal acts although *this phrase* is often used as a collective term to describe the classical understanding of the doctrine. German law of obligation is based on the term "Treu und Glauben" (§ 242 Bürgerliches Gesetzbuch 1900), which literally mean "fidelity and faith" (Zimmermann 2000 & Whittaker, p.18). In French and Italian statutes, it is defined as "bonne foi" (n.3 of art.1134 French Civil Code 1804; Musy 2000, p.3) and "buona fede"(art. 1366, 1375, 1175, 1337 Italian Civil Code 1942; Musy 2000, p.5), which are very similar to the classical definition. In states with a common law system, the legal terms "good faith situations" and "good faith and fair dealing" are used and relate to honest business practices (Musy 2000, pp.6-7). By

analyzing the different phrases which are defining *bona fides*, it is possible to see the development of understanding of good faith in legal science. For example, in the Civil Code of Netherlands, (1992) the concept of *bona fides* is described by the words “redelijkheid en billijkheid”, which means “reasonableness and fairness” (Translate.eu). Dutch legal scientists view these meanings as consistent with the term good faith (Hartkamp 1992, pp. 3-4).

The principle of good faith for some European legal systems is the core for development of their obligation law, while in other countries it is eliminated or rejected (Zimmermann & Whittaker 2000, p. 1). The reasons for such differences lay in the business practices and history of each countries economical development. For instance, in Germany, business transactions are based on long-term relationships and the disclosure of business information, while in England, the economy is more risk-taking and short-term oriented. (Teubner 1998) That is why some legal scientists consider *bona fides* as “unworkable in practice”, “legal transplant”, and a “legal irritant” for common law systems (Teubner 1998, p. 11).

However, the processes of globalization and harmonization of law require a common understanding of the basic principles of law among the European countries. Besides the differences, which exist in the European states, there is a common core of the concept of *bona fides*. Therefore, provisions concerning the principle of good faith are included in lots of international agreements, such as the Vienna Convention (United Nations Convention on Contracts for the International Sales of Goods) 1980, the UNIDROIT Principles of International Commercial Contracts 2004, and the Principles of European Contract Law 2002. In all these documents, the numbers of provisions concerning good faith and its contents are different. However, in legal practice, these documents are used simultaneously, mutually supplementing each others. To detect and understand the core meaning of the principle, it is necessary to study legal practices of the European courts, namely the European court of Justice and the European court of Human Rights.

4.2. Goal for the research, research problems and research questions

There are several problems concerning the principle of good faith. First of all, there is no definition of “good faith” in any statutes of European countries or international conventions. The major role in defining the concept is played by the national and supranational courts and

the legal scientists. Thus, it is necessary to try to deduct the meaning of the concept. Therefore, **the goal of this research is to provide a definition for the principle of good faith and to detect its elements.** This concept is not always transparent; is the principle of good faith a legal or a moral principle and how are the law and morality interconnected when the principle is applied? **The interrelation between the moral and legal principles of good faith and their differences will be identified.** Secondly, the target of the Masters' Thesis is **to define a role and place for the principle of good faith in European international trade,** because this aspect is not sufficiently researched in the literature. Third, since there is no general understanding of the concept of *bona fides*, it is important **to detect the differences and similarities in understanding of the principle among the European countries and to define a common core.** The common core can be found by researching the legal practices of the European courts. Therefore, the **target of this research is to find out the understanding of the principle of good faith by European courts.** Fourth, it is not evident what the conditions for application of the principle are. **My goal is to deduct these conditions from the cases of European courts.**

To conclude, the **research questions** can be specified as follows:

1. What does the principle of good faith mean? What are the elements of the principle? Is it a legal or moral principle?
2. What kind of role does the principle of good faith play in the international trade?
3. What are the differences among the European countries in the understanding of this concept? What are the similarities?
5. How do European courts (the ECJ and the ECHR) apply and understand the concept of *bona fides*?

4.3. Research-methods, theoretical backgrounds and literature-review

Research-methods

The research was completed by using qualitative methods, meaning that the answers for the research questions are given through case studies, interpretation, and observing “process theory” (Maxwell 2004, p. 249).

For the theoretical part of this thesis, descriptive research methods are used. To analyze the data, narrative and connecting analysis (Maxell 2003, p.255) will be utilized. Since one of the goals of the research is to provide a definition of the theoretical concept of “good faith”, it is important to use inductive analysis to explain the concept. A method of comparison will be used to examine the differences in understanding of good faith in different legal systems. For instance, it is essential to define such differences in common law systems and continental systems of law and also between states’ continental systems of law and in international documents. The legal and moral concept of good faith should be compared as well. The different courts’ judgments are also the subject of comparison. The use of comparative methods will provide the opportunity to find the common core of the concept of good faith, to define the general conditions of applying the principle of good faith, and to detect the differences in understanding and use of the principle.

Theoretical backgrounds for the research

Dworkin’s theory, as presented in his essay ‘The Modul of Rule I’, provides a good basis for the research of legal principles. Dworkin challenged the theories of legal positivism and legal utilitarianism, and proposed his own concept of standards: rules, principles, and policies (Ratio 2002, p.268). A rule, according to Dworkin, may become binding within a group of people if that group, through its behavior, accepted the rule as a standard of conduct (Ratio 2002, p.273). He defines ‘principle’ as whole set of standards other than rules, and the term ‘policy’ is used to refer to the set of goals to be reached. ‘Policy’ governs the improvements in economic, political, and social areas, while ‘principles’ are the requirements of justice or fairness or other moral dimensions. Dworkin identifies arguments of policy, which secure the interests of society, and arguments of principles, which secure some individual or group rights and which, according to Dworkin, are superior. There are two criteria to make a distinction between principles and rules: *logical distinction*, meaning that rule is applicable or

not to the case, while principle can have quantity of exceptions, and the *dimension of weight*, which is only the dimension of the principle. The dimension of weight affects the “validity of principles” (Ratio 2002, pp. 275-278). If principles collide, the judge must weight up the principles involved. So, according to Dworkin, principles may dictate a result in the case, but an applicable rule provide certain result and nothing else can change it. (Ratio 2002, pp. 275-278)

Dworkin also developed his own concept of rights. He states that humans have rights before some authority or court has maintained it. Therefore, when the word of law is vague, the judge must take in account the intention of law. Dworkin supports the idea that there cannot always be a right answer in every possible case, however, in most of the cases there is fair solution. Based on this argument, Dworkin proposed the idea of basic legal theory, which justifies the legal cases in the most accurate way. Dworkin also finds lots of legal clauses vague. For example, fairness can mean different thing for different people and it is not always possible to name the cases where the concept should be applied. Dworkin states that conceptions of fairness may differ from each other; however, the concept of fairness is always the same. Juha Ratio (2000, p.301) further develops Dworkin’s idea of concept and conception and names a problem of translation within the European Union. He recognizes that the understandings of certain concepts may differ from country to country, which may have an impact on the translations of the concept at hand (Ratio 2000, p.301). According to Dworkin, courts should accept the vagueness of some provisions and should revise these principles with fresh moral insight. (Ratio 2002, p.281-283). Juha Ratio acknowledges that Dworkin’s theory of law concerning judicial activism and judicial restraint is very useful while studying the on-going debate of law-making/law-finding function of the ECJ (Ratio 2002, p. 299).

These same problems of translation and understanding within the EU are stated by Klami (Ratio 2000, p.326). For example, Klami argues that the terms *Treu und Glauben*, *god tro*, *vilpitön mieli*, *bona fides*, and good faith differ from each other in Germany, Sweden, Finland, and the United Kingdom as legal concepts (Ratio 2000, p.327).

The characteristics of *principles*, given by Laporta, are also a valuable base of research on the principle of good faith. According to Laporta, principles do not give a concluding reason for the case, they are applied unless rebutted. Principles have dimensions of weight of

importance. Principles are also requirements of optimization, meaning that something must be implemented in the highest level. Lastly, principles have deep connections with values, political targets, and moral issues. (Ratio 2002, p. 287)

Pöyhönen, a Finnish legal scientist, criticized the division of principles and policies proposed by Dworkin. According to Pöyhönen, it is not always possible to separate individual rights and collective goals; that is why rights can derive from policies and Dworkin's theory is inconsistent at the 'level of morality'. (Ratio 2002, p. 290)

Juha Ratio (2002, p. 299), who was influenced by Dworkin's theory, makes a conclusion which seems very valuable for future research. Ratio states that, "...the principles cannot be organized in a hierarchical order which could be applied generally in every case...principles can be categorized in numerous ways depending on the method used" (Ratio 2000, p.290).

It is impossible to study principles of law without taking into consideration the theory of Kaarlo Tuori (2002). This scientist states that modern law does not consist of only regulations and statutes; it includes 'legal culture' and 'deep structure of law'. These deep layers, "...create preconditions for and impose limitations on the material at the surface law"(Tuori 2002, p. 147). Tuori underlines that the surface level of law is turbulent because of new regulations, new court decisions, and the debates of scholars and judges (Tuori 2002, p.155).

'Legal culture' is the memory of the law within the narrow legal community; it continues a connection with the past history of the law. Through legal culture the surface-level of law receives new determinants. The division of surface-level and legal culture can explain difficulties which arise when European regulation is incorporated into domestic legal order. The concept of legal culture was created by representatives of a national societal group, for example, Finnish lawyers. It exists in the minds of individuals as practical knowledge. Legal order is a part of legal culture; it consists of meta-norms, which include doctrine of sources of law, standards by which the contradictions between legal norms are to be solved, and standards which maintain the internal consistency in legal order. *General doctrine* is also included as a part of legal culture. The significance of general doctrine varies within different legal cultures. In the Anglo-American legal system, the concept of general doctrine is met with suspicion. Contrastingly, in Continental European legal culture, general doctrine is a part of the status, for example the German Civil Code *Bürgerliches Gesetzbuch* contains a general part of private law and a general part of its different sub-fields. Also, constitutional

law is connected with principles which constitute law's deep structure. (Tuori 2002, p. 163-171)

General doctrine is comprised of, from one side, distinctive legal concepts and, from the other side, general legal principles. Through the legal concept, social reality is approached in legal practices. Legal concepts resemble social-scientific concepts; however, they have immediate normative implications. (Tuori 2002, p. 174) Also, general doctrine is applied in the field of law in question, where it appears as a general principles of law. Such principles are *pacta sunt servanda*, the principle of equity in private law, principles of equality, proportionality, and objectivity in administrative law. Tuori also distinguishes within legal principles, the elements of legal culture and their discursive expressions at the surface of the law. He states that principles as legal norms are not exactly the same as principles as sources of law. Principles as sources of law are not only found in legislation. For example, they can be a part of the government bills, *travaux préparatoires*. Legal principles expose legal order to the influence of morality. However, not all moral principles are legally relevant. Principles must find support in authoritative legal sources defined by prevailing met-norms, legislation, or in precedents. (Tuori 2002, p.177-181)

Tuori identifies the most stable layer in the law as being the deep structure of law (Tuori 2002, p.192). He states that integration at the level of deep structure represents the globalization of law in a more fundamental sense than the surface-level supranational normative level (Tuori 2002, p. 185). Deep structure is common to all legal cultures representing modern law. The elements of the deep structure of law are fundamental principles, such as human rights as a general normative idea (Tuori 2002, p.192).

Tuori's theory, in the study, will be used to identify where the principle of good faith originates in different legal cultures. Does the principle exist only in the surface of the law or also in the legal culture and legal order? What is the difference in the understanding of this principle in different European countries? Is the principle of good faith a general legal principle or an element of the other principles or the rule of law? Also, Tuori's theory will be applied to find out if the principle of good faith is a moral or a legal principle. His theoretical idea about the deep structure of law (Tuori 2002, p. 183-191) can also be very useful for discovering a common core of the principle of good faith.

Literature-review

The monograph *The Principle of Legal Certainty in EC Law* by Juha Ratio (2000) provides a good base for the theoretical background of this research. In the monograph, different theories are described. Also, the book identifies the different issues concerning preliminary ruling of the ECJ.

A book by Kaarlo Tuori (2002), *Critical Legal Positivism*, also provides a theoretical base for this research. Tuori discusses the structure of law, which helps to categorize the principle of good faith and find the place of the principle within the different levels of law.

There are several researches concerning good faith, the principle of good faith, and other aspects of the topic. The book by Reinhard Zimmermann & Simon Whittaker *Good Faith in European Contract Law* (2000) is especially interesting; in this book, the origin, the development of the concept “bona fides”, and the differences between the national systems of European countries are described. Articles by Teubner Gunther (1998), Irene Kull (2002), and Alberto M. Musy (2000) discuss such aspects, respectively, as a negative influence of establishment of the general principle of good faith in the countries with common law system, the establishment of the principle of good faith as a constitutional value, and common elements of the principle in different European countries. Moreover, publications by Jan M. Smiths (2005) and Stella Vettori (2007) describe different dimensions of *bona fides*. Also, some comparative analyses concerning the topic are done by Konrad Zweigert & Hein Kötz in their book *Introduction to Comparative Law* (1998). The influence of European law is researched in the book *The European way* by Tuomas Ojanen (1998) and in the book *The European Court and national courts - doctrine and jurisprudence: legal change in its social context* by Anne-Marie Slaughter & Alec Stone Sweet & J. H. H. Weiler (1998). The morality of law and its ethical aspects are discussed in books written by Kent Greenwalt (1987), Fernando Teson (2005), Michael Perry (1990), Philip Soper (2002) and Lon Fuller (1969). Moral issues in business are researched by Johanna Laurila (1995). The principles of European law discussed in books by Antonio Estella de Noriega, Takis Tridimas (2006), Jeremy Bentham (2000), Esa Paasivirta & Kirsti Rissanen (1995), Michael Bayles (1987) and Juha Ratio (2002). The significance and influence of European courts are described in books by Antoine Masson & Kevin O'Connor (2007) and Michael Goldhaber (2007).

However, the influence of the European courts (the European Court of Justice and the European Court of Human Rights) and their understanding of the concept of good faith have never been researched as a main subject in literature and scientific articles. Thus, the target of this research is to study court cases of the ECJ and the ECHR where the principle of good faith was applied and to deduce the definition of the principle, conditions of application, and understanding of the meaning of “bona fides”. It is also important to compare the legal practices of the ECJ and the ECHR with national legislation and to detect the differences and reasons for it.

5. DEVELOPMENT OF THE PRINCIPLE OF GOOD FAITH IN LEGAL DOCTRINE AND IN NATIONAL LEGAL SYSTEMS

5.1. Historical development of the principle of good faith

In order to understand different areas of law, it is not enough to simply know modern legislation. The way in which law has developed in the past, in order to arrive at its present position, is very important. By studying the historical perspective of law, it is possible to understand how it is likely to develop. (Taylor 1995, p. 99) Therefore, this chapter will present a historical survey about the development of the principle of good faith.

The notion of good faith, or *bona fides*, originated from Roman law. There was a clause known as *exception doli* and it was applied in procedural law. It gave the judge an equitable discretion to decide each case in accordance with what appeared to be fair and reasonable. Moreover, *bona fides* was one of the most fertile agents in the development of Roman contract law. For instance, in the contracts of sales, the buyer was granted a right to claim his damages in cases of eviction. Also, good faith allowed error (mistake) and duress to be taken into account in determining what kind of protection could be granted. *Bona fides* was involved in such institutions in Roman law as liability for the latent defects, the rules relating to the implied warranty of peaceable possession, and annulment of contracts due to mistake. In the course of time, the concept of *bona fides* was absorbed by a broader notion of equity. In the Middle Ages, “equity” remained in the forefront of legal discussions as an opposition to the concept of “strict” law. Good faith also dominated relations between merchants and became a fundamental principle of medieval and early modern law. It was said that, “...good faith is the prime mover and life-giving spirit of commerce” (Zimmermann & Whittaker p.18). *Bona fides* contributed considerably to the sort of flexibility, convenience, and informality within the international community of merchants. (Zimmermann & Whittaker 2000, p. 16-18)

Scientists (Blegvad 1995, p. 349, Zimmermann & Whittaker 2000, p.16-17) state that in previous times, basic trust was very important in personal relations. Mutual trust was regarded as a basic condition for a deal. Business was further anchored in a person’s, or a party’s, commitment to the deals, which were mostly conducted in face-to-face situations. Business relations between people have become more distanced, psychologically as well as physically. In modern societies, we often interact with unknown people instead of relatives or

acquaintances. The conclusion of contracts is regulated by law. This development of modern legal systems has taken a long time. However, trust has continued to be an essential core value despite the existence of well functioning legal rules. (Blegvad 1995, p. 346) People with empirical socio-legal interests argue that trust is a very necessary aspect in business deals. They also agree with the fact that trust, to a certain extent, is functioning under “the shadow of the law”. (Blegvad 1995, p. 349)

There is an opinion that in the multinational contract law project of the development of the European Code of Contracts, the notion of “fairness” could serve as the common object of a restructuring of the national traditions of contract law thinking (Joerges 1995, p. 323), and that the principle of good faith will become one of the harmonizing elements of European contract law (Zimmermann & Whittaker 2000).

5.2. Principle of good faith and ethical norms

Many authors write about the morality of law (Fuller 1964; Passivirta & Rissanen 1995; Teson 2005). The topic seems especially important when the principle of good faith is discussed. In this chapter, moral rules that are important in society will be identified, as well as the coherence between these norms and law and the place of the principle of good faith within the system of ethical and legal norms.

It is obvious that all social groups, such as small communities, professions, societies and states, have common customs or habits which regulate the behavior of their members. Bad and good patterns of behavior are associated with positive and negative emotions and attitudes, which enhance cohesion and strength of the group. The morality prevailing in the social group consists of influential and often unwritten principles. They are clarified in the systems of values and norms formulated by religious or philosophical doctrines. Ethics theory attempts to analyze and justify such moral principles. Ethics, according to Aristotle, should provide the virtues that a good person should have. Justice can be described as a fundamental mental disposition of the virtuous person. (Niiniluoto 1995, p. 11) The basic formal ingredient of justice is the rule of equity: people in the same or similar situations have to be treated equally (Niiniluoto 1995, p. 19).

It is common knowledge that it must be known what is “perfectly good”, before the “bad” can be recognized (Fuller 1964, p.32). However, it is impossible to define “perfectly good”. Thus, based upon the moral principles and common sense, the members of social groups have an ability to judge whether a situation is just or not; to have a so-called sense of justice. This sense of justice changes over time as moral values develop in new circumstances. (Niiniluoto 1995, p. 11)

Unjust action causes moral disapproval, however, it can be only a minor punishment for a dishonest person. Legislation can be understood as a more formal tool for defining rights and duties; in other words, behavior is regulated by judicial sanctions. In some discursive theories of law (Perelman and Habermas), the validity of the legal norm in society is defined as the acceptability of that norm. Aulis Aarnio argues that law should be supported by the majority, “...in the rationally reasoning legal community” (Niiniluoto 1995, p. 12). On the contrary, doctrines of legal realism and positivism define a legal order as the content of those enacted statutes which are followed in the community. (Niiniluoto 1995, p. 11-12) “The Law certainly makes Society, but no one must forget that Society also makes Law” (Masson & O’Connor 2007, p.15). Graver argues that a certain level of social justice is necessary for the legitimacy of the social order, and thus, constitutes a necessary condition for the market economy (Graver 1995, p. 206). Lon Fuller has the same opinion and, therefore, he named one chapter of his book “the morality that makes law possible” (Fuller 1964, p. 33-95).

Some scientists (Graver 1995, p. 197) define the European Union as a project of justice in three ways: justice in terms of some distributive principle (distributive justice), justice as a properly functioning market (freedom of economic activities), and justice as equality (international justice). In terms of justice, rationalization is a very important concept. Both of these ethical concepts should supplement each other. (Joerges 1995, p. 320)

Teson (2005, p.8) states that the international order, in general, should benefit from the contributions of moral-political philosophy and political science, in addition to standard doctrinal analysis (Teson 2005, p.8).

Britt-Mari Blegvad argues that trust has become a focal concept in sociology and sociologists of law have combined an interest in the role of trust with an interest in how informal, conventional, social, and economic norms co-function with legal norms in regulating, among

other things, business relations. These informal norms embody conceptions of fairness and justice. (Blegvad 1995, p. 341)

There is an opinion (Reifner 1995, p. 386) that justice is something which cannot be restricted to the given law, but defines the role and requirements of law against a more general moral background in which law should be, as in German legal philosophy, designed to protect the weak.

The principle of good faith is, without doubt, an ethical principle based on standards of justice, rationality, and trust. Good faith, or in Latin *bona fides*, is defined as, "...the mental and moral state of honesty, conviction as to the truth or falsehood of a proposition or body of opinion, or as to the rectitude or depravity of a line of conduct" (Catholic Encyclopedia).

To define the place of the principle of good faith in the system of ethical norms, the theory of Lon Fuller (1964, p.5-10) seems very suitable. He distinguishes between the morality of aspiration and the morality of duty. The morality of aspiration is the morality of *good life*, of excellence, and of the fullest realization of human powers. Whereas the morality of aspiration starts at the top of human achievement, the morality of duty starts at the bottom. It lays down the basic rules without which an ordered society is impossible. The morality of duty prescribes what is necessary for social living. (Fuller 1964, p.5-10) Applying the theory of Fuller, it is possible to say that the principle of good faith belongs to the morality of duty. Without good faith, the existence of rational society would be impossible and the principle of equal treatment would be destroyed. Therefore, the concept of good faith is very important in law, especially equitable matters (Catholic Encyclopedia).

If the principle of good faith is established in the legal statutes, it becomes a legal principle. Scientists (Niiniluoto 1995, p. 12) state that it is natural that the legal order should reflect the sense of justice in society. Hence, the principle of good faith being an ethical principle is transmitted to legislation by establishing it in the legal statutes.

After analyzing concepts and opinions presented in the legal literature above, about different aspects of morality and law, it is possible to draw the following conclusions:

- Every social group has its morality, which is based on habits and traditions.

- Justice, trust, and rationality are basic moral values, which are essential for all human beings.
- It is impossible to define what is “perfectly good”. Therefore, social and legal judgments are often guided by moral principles and common sense.
- Ethical and moral norms change over time and are always developing in new circumstances.
- Law and moral values are interrelated with each other. Law is a formal tool to define rights and duties.
- It is natural that legal order should be based on standards of justice and rationality.
- The principle of good faith is an ethical principle; it is closely related to such moral values as justice, trust, rationality, and honesty.
- According to Fuller’s theory, good faith can be considered as a subject of the morality of duty.
- The principle of good faith was established in the legislation of different countries. Therefore, it is possible to say that the principle of good faith is an ethical and a legal principle at the same time.

5.3. Understanding of the principle in legal doctrine

There are many opinions about elements and characteristics of ‘good faith’ and ‘the principle of good faith’ in different legal dictionaries and legal literature.

The law dictionary, *www.Law.com*, defines good faith as, “...an honest intent to act without taking an unfair advantage over another person or to fulfill a promise to act, even when some legal technicality is not fulfilled. The term is applied to all kinds of transactions” (Law.com Law Dictionary).

Michel D. Bayles (1987, p.188) writes about a “duty of good faith”. He states that the duty of good faith consists of different obligations, for instance, the duties of loyalty and honesty.

The violation of these obligations can result in the rescission of the contract or a basis for damages. He also states that it is easier to consider “bad faith”. Bad faith can be detected by analyzing the normative basis of contract law. Bad faith can be found in negotiation without serious intent to contract and taking advantage of others in driving a “hard bargain”. Moreover, it appears in the pursuance of only substantial performance and the abuse of powers to determine contractual compliance. Bad faith can be detected in making up disputes and taking advantage of another to obtain a favorable agreement and in remedial actions, such as refusing performance without reason or abusing the power to terminate a contract. (Bayles 1987, p.188-189)

Bayles also gives the definition for the principle of good faith. He states, “...contract law should require conduct necessary for the minimal trust rational people need to interact with a reasonable prospect of being mutually beneficial” (Bayles 1987, p.188). Honesty is a basic condition for minimal trust, but not the only one. The duty of good faith should be imposed not only on the performance or enforcement of the contract, but also on the processes of contract negotiation and formation. The author emphasizes such aspects of good faith as voluntariness (transferability of property), reasonable opportunity to choose to contract, the duty not to misrepresent, the duty of disclosure, and the duty not to use duress or undue influence. (Bayles 1987, p. 188-190)

The principle of good faith is interconnected with the other principles of contract law. Bayles (1987, p. 149) considers “reasonable expectations” as a principle of contract law. He states, “...in a contractual setting, only those reasonable expectations of which the other party was or should have been aware are to be protected” (Bayles 1987, p.149). By analyzing Bayles’s words, it is possible to conclude that good faith is included in the term “reasonable expectations”. Moreover, good faith is a part of the principle of reliance, the principle of modifications, the principle of mistake, and the principle of illegal contracts. Bayles also writes, “the principle of reliance: a commitment should be enforceable to the extent necessary to prevent loss due to foreseeable reliance” (Bayles 1987, p. 159). He continues that, “...good faith modifications of contracts regardless of consideration, past benefit, or reliance should be enforceable” (Bayles 1987, p. 164). Further, “...the principle of mistake: a contract should not be enforceable against a party who has made an innocent and substantial mistake of fact if either (a) that party has not assumed the risk of the mistake or (b) the other party knew or should have known of the mistake” (Bayles 1987, p.181). The principle of “illegal contracts”

(Bayles 1987, p.186) requires that contracts which are contrary to a law, regulation, or judicially recognized public policy important for the collective good should be modified. If it is impossible, the parties of such contracts should be restored to their positions prior to the contract or losses should be divided (Bayles 1987, p.186). Likewise, good faith is interrelated with such terms as “reasonable opportunity”, “reasonable alternatives”, and “rational person” (Bayles 1987, p.178).

J.C. Smith (2002, p. 183) underlines the connections between the requirements of reasonableness, fairness, and good faith. Smith also writes about illegality in contract law. Bad faith is involved where the contract is unlawful, the purpose of the parties (or one party) is contrary to public policy, where the contract is lawfully made but carried out in an unlawful manner, and where the contract is so devised as to enable one party to perpetrate a fraud. Smith also states that public policy changes over time, so that what was considered as an action in bad faith in the past now can be considered a lawful action. (Smith 2002, p. 256-262)

Richard D. Taylor writes about the “liability for negligence”. The term involves the principle of good faith. The person is liable if he has failed to take a reasonable care. The author analyses the Unfair Contract Act 1997, the Act of England, Wales, Northern Ireland, and Scotland, which establishes that civil liability can be avoided or imposed by means of contract terms (The UK Statute Law Database). The Act states that some exclusions of liability are only effective if they satisfy “the test of reasonableness”. Therefore, the exclusion of liability should not result from the inequality of bargaining power. Taylor underlines that the terms of the contract shall have been fair and reasonable when the contract was made and states, “...the question is merely whether the particular term was reasonable one to include in this contract, not whether the term would be reasonable in any other circumstances” (Taylor 1995, p.116). (Taylor 1995, p. 107-117)

Moreover, “misrepresentation” includes the dimensions of bad and good faith. For example, silence or non-disclosure does not normally give rise to liability; however, there are a number of exceptions that are results of the duties of good faith. For instance, a person who purchases goods by cheque represents by implication – even if nothing is said – that the cheque is a valid order for the amount stated on it. Taylor underlines that only facts can be true or false. However, there can be exceptions. The speaker must be aware of reasonable grounds for his

opinion and he must not be aware of facts which clearly invalidate the opinion. A statement as to one's intention clearly is capable of being true or false in the sense that one either has that intention or does not. A willful misrepresentation of law constitutes misrepresentation since it is a misrepresentation of fact of what is the speaker's belief as to the law. Good faith and bad faith are taken into account when there is a dispute on whether a party is responsible for a mistake. Therefore, if a party knew about the mistake or could have been expected to discover the mistake, it is the condition which makes the contract void. (Taylor 1995, pp. 126-207)

The principle of good faith is involved in the topics of illegality and inequality in contract law. Taylor states that the issue of reasonableness will tend to be raised in terms of fairness, where there is an apparent disparity between the parties in terms of their bargaining power and in terms of the "legitimate interest" being protected in the other cases. Public interest only rarely arises directly since neither party is likely to challenge the contract if it is reasonable as between them. Inequality in contract law includes duress, undue influence, and unfair bargains. Before, in common law, duress was limited, requiring threats of death or physical violence. Now, the courts recognize a wider concept of duress known as "economic duress". For instance, the supplier requires 10 per cent higher price in order not to break the contract. Unconscionable bargains include exploiting the weakness of the other party. As Taylor writes, "...the terms must be unfair or the consideration grossly inadequate" and, "...coupled with undue influences or pressure" (Taylor 1995, p. 207-230). This is a distinction between substantive unfairness and procedural impropriety. (Taylor 1995, p. 207-230)

Micklitz (Micklitz 1995, p.284) considers the principle of legitimate expectations as a general principle of justice in secondary community law. He underlines the connection between the principle and the concept of 'misleading' and good faith. He also presents an example where the principle of legitimate expectations means the same as the principle of good faith: "...whereas the requirement of good faith may be satisfied by the seller or supplier where he deals fairly and equitably with the other party whose legitimate interests he has to take into account" (Micklitz 1995, p.290). Good faith, read in conjunction with 'legitimate expectations', points beyond consumer choice in, "...the direction to a general fairness test" (Micklitz 1995, p.290).

There is an opinion (Usher 1995, p.358) that the concepts of secrecy and privacy, especially professional privacy, are interrelated with the principle of good faith. This means that no confidential information received in the course of professional duties may be divulged to any person or authority whatsoever except in summary or collective form so that individual institutions cannot be identified, or without prejudice to cases covered by criminal law. On the other hand, the principle of good faith is connected with the duty to give information. For example, transactions in property derived from criminal activity are prohibited. Credit and financial institutions must require the identification of a customer when entering into business relationships. (Usher 1995, p.358)

The concept of “the general good” (Usher 1995, p.358) is also considered as a related concept to the principle of good faith. “The general good” refers to the limitation of individual economic benefits in the interest of consumers, health, and environment (Usher 1995, p.358).

Popova (2006, p.7-9) defines the principle of good faith as an avowed legal principle with sovereign legal power, which is applied in public and private law. The principle establishes rights and duties between contracting parties and third persons. In private law, the principle of good faith requires that fraud, misrepresentation, and the threatening of a party or third person are eliminated while exercising the rights and performing the contract. All actions contrary to ethical and moral norms are contrary to the principle of good faith. The author also recognizes two elements of the principle of good faith: objective and subjective. The objective element is the requirements of good faith, which are established in the legal acts. The subjective element is the internal understanding of the duty to behave according to the standards of fairness, honesty, rationality, fidelity, and loyalty by the person. (Попова 2006, p. 7-9) Subjective and objective elements of good faith were also recognized by Zimmermann (Zimmermann 2000).

Sinyavskaya (2007, p. 12) underlines a connection between the legal term “guilt” and the performance of obligations in good faith. The writer proposes to define what is “guilt” based on the standards of good faith, rationality, and reasonable care. (Синявская 2007, p.12)

Tiunov (1979), in his monograph *Principle of adherence of international obligations*, considers the structure of adherence of international obligations. He defines three elements of the structure: the obligation to perform the contract, the duty of good faith in performance, and the performance

of all valid contracts. He also writes about the connection between a principle of reciprocity and the principle of good faith. (Тиуннов 1979)

Kalamkaryan (2001) writes about the connection between the performance of obligations in good faith and the principle of estoppel. *Estoppel* is a legal doctrine where a party is barred from claiming or denying an argument on an equitable ground. There are many types of estoppels. Most estoppels prohibit a party from being harmed as a result of another's deeds, statements, or promises, when later actions or statements contradict or undermine what was originally stated, promised, or implied. (Law dictionary) Kalamkaryan states that the legal base of the estoppels is the principle of good faith (Каламжарян 2001, p. 127).

After analyzing the above presented legal doctrine, the following conclusions can be drawn:

- The principle of good faith is a generally recognized legal principle. The principle is very comprehensive; it includes lots of related concepts and duties.
- Good faith can be explained by words such as honesty, trust, fairness, loyalty, fidelity, reasonableness, and rationality.
- The duty of good faith is interrelated with such concepts as voluntariness, the duty not to misrepresent, the duty to disclosure or to keep secrecy, and the duty not to use duress or undue influence.
- The easiest way to define good faith is, "...not to act in bad faith" (Bayles 1987, p.189).
- The principle of good faith is interrelated with the principles of reasonable and legitimate expectations, reliance, modifications, mistakes, and the principle of illegal contracts.
- The concept of "general good" (Usher 1995, p.358) includes the dimensions of "good faith".
- Good faith in contract law should be estimated at the points of agreement in every single contract because every case is unique and the definition of good faith will be different in different contracts.

- There are two elements of the principle of good faith: subjective and objective. The objective element is the requirements of good faith which are established in legislation. The subjective element is the person's internal understanding of the duty to behave according to the standards of fairness, honesty, rationality, fidelity, and loyalty.
- Based on the standards of good faith, rationality, and reasonable care, disputes in contract law should be settled.
- The duty to act in good faith is an element of international obligations and the international principle of reciprocity.
- The principle of good faith is the legal base of estoppels.

5.4. The principle of good faith in national legal systems

The Helsinki Seminar introductory document states that, "...behind the principle of harmonization, reciprocity and subsidiarity one can identify a line of thought according to which the EU takes care of the freedom of economic activity, whereas the role of Member States is to protect the general interest" (Daintith 1995, p.147). Further, "Within such an approach it would be a responsibility of States to take care of justice in the common market" (Daintith 1995, p.147). Therefore, it is important to know the differences between the European states in the understanding of the principles of justice and good faith. Micklitz's opinion (Micklitz 1995, p.261) is that European private law is only in the beginning of the process of development and private law in different countries is still diversified.

However, the internationalization of "fairness" within the EU space was clearly an important initial objective of EU treaties in a whole series of legal contexts (Daintith 1995, p.147).

Scientists (Daintith 1995, p.153; Collins 2003, p. 40) agree that national and regional variations within Europe in ideas about justice are worthy of investigation as a contribution towards the understanding of the operation of European Union law, and it is necessary to discuss the cultural differences in private law within the EU. Therefore, in this chapter, the diversity in the understanding and application of the principle of good faith, and closely

related principles such as principles of justice and rationality, will be analyzed. Law and legal practices of European countries will be researched; moreover, Russian law will be discussed due to coming changes in legislation that are intended to harmonize Russian and European law. The differences and the similarities in the understanding of the concept, and the tendencies towards its internationalization, will be identified.

5.4.1. Understanding of the principle in German law

Social justice in private law has a strong national bias and focuses on contract law (Micklitz 1995, p.278). This is especially true when the principle of good faith in German law is taken into consideration.

In Germany, *bona fides* appears as the indigenous notion of *Treu und Glauben* - literally translated as “fidelity and faith”. This phrase was found in a number of medieval sources and it was used in the context of commercial relations as a synonym for *bona fides* (Zimmermann & Whittaker 2000, p.18). *Treu und Glauben* found its place in the German Civil Code of 1900 in the famous § 242 which states, “...the debtor is bound to perform according to the requirements of good faith, ordinary usage being taken into consideration” (BGB 1900, § 242). This clause relates specifically to the manner in which the obligation is to be performed. § 242 BGB has thus, by way of interpretation, been transformed into one of the famous “general clauses” by means of which Germany’s “case law revolution” was affected (Musy 2000, p.4). However, § 242 BGB is not the only place where the BGB refers to *Treu und Glauben*. § 157 BGB states that, “...contracts shall be interpreted according to the requirements of good faith, ordinary usage being taken into consideration” (BGB 1900 § 157).

§ 242 BGB became a bone of contention in the big methodological disputes of the first part of the 20th century; it involved such topics as doctrine of positivism, free law movement, and jurisprudence of interests. On the one hand, *Treu und Glauben* was considered a clause with negative effect, which destroys legal culture; on the other, as “queen of rules”. (Zimmermann 2000 & Whittaker, p. 20)

After long case-law and doctrine development, the law of good faith was used in order to devise a remedy for code gaps, such as the protection of a recipient from a partial or incorrect performance. It replaced a “general tort of negligence”, which does not exist in German civil

law; law of good faith expanded tort liability to protect some pre-contractual, contractual, or post-contractual situations. (Musy 2000, p.4)

Before, § 242 BGB was applied to deal with *culpa in contrahendo*. *Culpa in contrahendo* is a Latin term meaning "obligations in negotiation". It is an important concept in the contract law of Germany and in many other countries. The German scientist Rudolf von Jhering is credited with the discovery of the *culpa in contrahendo* doctrine. *Culpa in contrahendo* recognizes a duty to negotiate with care and not to lead a negotiating partner to act to his detriment before a firm contract is concluded. Originally, the courts saw a gap in the legal system of the German Civil Code and filled it with the development of *culpa in contrahendo* under § 242 BGB. Since the modernization of the Law of Obligations in 2001, the legal doctrine is provided by statute. §311 BGB lists a number of steps by which an obligation to pay damages may be created. This §311(2) should be used in connection with §§280(1) and 241(2) of the BGB 1900. (Bass 2009, pp. 218-223)

It is possible to divide the law of good faith in the German legal system into three functions. The first function includes the expansion and establishment of contractual duties, which includes the secondary duties of performance, duties of information, of protection, and cooperation. The second function of good faith is the limitation of contractual rights. It deals with the doctrine of individual and institutional abuse of rights, such as unfair acquisition of rights, failure to comply with the duties, lack of legitimate interest, proportionality, and contradictory behavior. The third function of good faith is transformation of contract, which expands the judicial power to rewrite a contract in the light of subsequent events: imbalance of equivalence, frustration of contractual purpose, and fundamental social changes. (Teubner 1998, p.20)

There is an opinion (Teubner 1998, p.25) that the application of law of good faith in Germany presents a "living law", a part of legal culture. It can be proved by the following examples. First, German corporate governance and corporate finance tend to favor long-term financing of firms. It is supported in private law by good faith obligations and the general duty of loyalty. A wide system of disclosure of information has been developed in the relationships between banks and companies. Second, labor unions play an important role in industrial relations; hence, there are equally extensive legal duties between managers and employees. Third, inter-company relations are very long-term oriented. Therefore, under the good faith

clause, the court has imposed duties of cooperation, which are directed toward the common purpose of the contract. If a new situation arises, the judges take the freedom to rewrite the contractual terms. Fourth, there is the business associations' coordination of the market which takes certain interests into account, particularly consumer interests. Fifth, businesses negotiate technical business standards with the government and the courts reconstruct good faith standards to counteract excessive economic transaction. (Teubner 1998, p.25-26)

To conclude, the principle of good faith in German law has a very long historical development - in the law, in court-cases, and in legal doctrine. The legal doctrine is very detailed and plays a significant role. The law of good faith can be considered a "living law" and a part of legal culture because of the tradition of business and government relations in Germany.

5.4.2. *The principle of good faith in the Italian law*

The Italian Civil Code (1942) was established much later than the German BGB. Thus, Italian scholars were fully aware of German case law regarding paragraph 242 of the BGB. The Italian Code provides protection of "good faith" in the contractual relationships in the following articles: Art.1366 "Contract must be interpreted in good faith", Art.1375 "Contract must be executed in good faith", and Art.1175 "Debtor and creditor must behave according to good faith and fair dealing rules". Additionally, Article 1337 provides that, "...parties must behave in good faith during the pre-contractual bargaining and contract drafting" (Italian Civil Code 1942). On the one hand, the Italian doctrine has not been able to draw up a clear systematic picture of good faith standard situations for judges. On the other hand, the Italian doctrine, until the late seventies, was strongly influenced by the German doctrine, which was in contrast with Italian judges who were still influenced by French doctrine and courts. This cultural confusion is now making a difficult problem of conflicting theories about *good faith* and *culpa in contrahendo*. Until the beginning of the seventies, the dominant position of the Supreme Court of Cassation held that good faith provisions did not offer a ground for legal action. In the late seventies, after long disputes in legal doctrine, case law changed to recognize the *buona fede* principle as an autonomous basis for a cause of action. (Musy 2000, pp.5-6)

There are different opinions among Italian scholars about the usage made by courts of the principle of good faith. Some scientists think that the principle could be used for

redistributive purposes; some are worried about the tendency to use it as a general equitable principle, a solution that might vest too broad discretionary power in the judges' hands. (Musy 2000, p.6)

5.4.3. Good faith in French law

In the civil law system of Western Europe, the minimalist view to the scope of good faith is represented by the French courts, which have not relied on the *bonne foi* to the same extent that their German counterparts did (Musy 2000, p.2).

Art.1134 of the French Civil Code (1804) states that, "...agreements lawfully entered into take the place of the law for those who have made them" (French Civil Code 1804). This seems to be the main concern of French contract law. This principle of freedom of the contract can be understood as a contrary element of the principle of good faith. However, in French obligation law there are provisions about good faith. The n.3 of art.1134 (French Civil Code 1804) states that, "...agreements must be performed in good faith". Art.1135 (French Civil Code 1804) adds that, "...agreements are binding not only as to what is therein expressed, but also as to all the consequences, which equity, usage, or statute give to the obligation according to its nature". The Obligation Section of the French Civil Code does not include other explicit provisions about the principle of good faith.

French scholars, such as F. Terre, R. Simler, and Y. Laquette (1996, p. 347) expanded the number of situations where the good faith principle is applicable. First of all, in the formation of a contract, the parties must deal in good faith. This means the principle of freedom of contract is limited by the duty of good faith. French jurisprudence looks for a very substantial deviation from pre-contractual reliance in order to establish a basis for liability in tort or deceit (Musy 2000, p.3). Hence, Art.1382 (French Civil Code 1804) states that, "...any act whatever of man, which causes damage to another, obliges the one by whose fault it occurred, to compensate it". Moreover, Art.1110 (French Civil Code 1804) establishes that, "...error is ground for annulment of an agreement only where it rests on the very substance of the thing which is the object thereof. It is not a ground for annulment where it only rests on the person with whom one has the intention of contracting unless regard to/for that person was the main cause of agreement". Art.1116 (French Civil Code 1804) adds that, "...deception is a ground for annulment of a contract where the schemes used by one of the

parties are such that it is obvious that, without them, the other party would not have entered into the contract”.

Second, in the performance of contract, there are at least two main applications of the good faith principle: the duty of loyalty and the duty of cooperation. The duty of loyalty includes two categories. First, the exact goal foreseen by the agreement must be achieved between the parties apart from the good faith evaluation. Second, any behavior imposing difficulties on the performance must be avoided; the parties have to act with due care. (Musy 2000, p.3)

The duty of cooperation is divided into two different applications too: the utmost good faith contract and the duty to disclose (Musy 2000, p.3).

The French *bonne foi*, even if strengthened by the doctrinal efforts, is still weakened by an insufficient application within the courts. The main difference between French doctrine and legal practices compared to German ones is the absence of a clear distinction between subjective and objective good faith – the German *Guter Glaube* and *Treu und Glauben*, particularly in the context of cooperation cases. (Musy 2000, p.3)

5.4.4. Good faith in the Netherlands Civil Code

The concept of good faith permeates all branches of Dutch law of obligations, contract law, and other branches of law as well. Art.6:1 p.14 (Civil Code of Netherlands 1992) provides that both parties to an obligation should behave in their relationship according to what is reasonable and equitable. Art.6:248 p.1 (Civil Code of Netherlands 1992) provides that contracts not only have the effects expressly agreed upon, but also those, which, according to the nature of the contract, result from the law, usage, or the requirements of reasonableness and equity. The principle of *bona fides* or good faith is expressed by the words "reasonableness and equity". (Hartkamp 1992 p. 6-7)

The principle has three dimensions. First, all contracts must be interpreted according to good faith. Second, good faith has a "supplementing function". In this case, the rights and duties are not provided by law, they arise between the parties in the contract. Third, it has a "restrictive" function, expressed in Art.6:248 p.2 (Civil Code of Netherlands 1992). It means that a rule which is binding the parties does not apply if it contradicts the criteria of reasonableness and equity. Therefore, the principle of good faith may be one of the reasons why the provisions of the contract will be not applied. For example, the courts deny a debtor

the right to rely on an exemption clause, which in the circumstances of the case turned out to be unreasonably unconscionable towards the creditor. (Hartkamp 1992 p. 7-8) Art.6:233 (Civil Code of Netherlands 1992) provides that a stipulation in general conditions may be annulled, either through an informal declaration by a party to the contract addressed to the other party or by judgment, if, taking into consideration all the circumstances of the case, it is unreasonably onerous to the other party. (Hartkamp 1992 p. 8)

It is important to note that the "restrictive" function of good faith is not limited to the provisions of the contract. The rule applies to all obligations upon the parties as a result of the contract. It concerns to all statutory rules: mandatory and supplementary. Therefore, the Dutch courts may not apply some provisions of mandatory rule of law. It is possible to say that all rules created by the parties or by statute have been brought under the revision of the courts to control whether their application in a particular case would lead to an unjust result. (Hartkamp 1992 p. 8-9)

The problem of a restrictive function of *bona fides* is especially important in the cases of void contracts. Like other civil law systems, Dutch law provides for the discharge of debtors in cases of impossibility of performance. "Unforeseen circumstances" may also create numerous difficulties in the performance of the contract, increase the amount of the corresponding obligations, or make the goal the parties had in mind unachievable. Art.6:258 (Civil Code of Netherlands 1992) establishes that the court, at the demand of one of the parties, may modify the effects of a contract or set it aside in whole or in part on the basis of unforeseen circumstances. These circumstances must be of such a nature that the parties, according to criteria of reasonableness and equity, may not expect that the contract be maintained in an unmodified form. It is essential that the term "unforeseen circumstances" should not be taken in its literal sense. The test does not relate to, "...what parties have foreseen or could foresee, but asks whether the contract makes sufficient provision for the supervening event". (Hartkamp 1992 p. 9-10)

Articles 6:248 and 258 (Civil Code of Netherlands 1992), which were discussed above, apply directly only to contract. Art.6:2 (Civil Code of Netherlands 1992) applies to all obligations. The code lacks a provision of a general character, which is applicable to all civil law relationships. However, these statutory provisions affect other branches of law either directly or *per analogiam*. For instance, Art.6:216 (Civil Code of Netherlands 1992) states that the

provisions on contracts apply *mutatis mutandis* to other multilateral patrimonial juridical acts, Art.3:166 para.3 (Civil Code of Netherlands 1992) states that Art.6:2 applies *mutatis mutandis* to the juridical relations between the partners, and Art.2:8 (Civil Code of Netherlands 1992) provides a comparable rule for the relations for legal persons, for example, corporations, associations, etc. (Hartkamp 1992 p. 10)

The Supreme Court has gradually widened the scope of the provision on good faith. For example, the Supreme Court has stated that parties, when negotiating a contract, must act according to criteria of reasonableness and equity, which impose on each of them the duty to take into account the other's reasonable interests. According to recent decisions, this general duty may imply that a party lacks the freedom to break off negotiations; in this case, the court may grant an injunction to continue or to resume them. Also, when negotiations have been broken off, the party which breaks the negotiation is obligated to pay damages to the other party. These damages may even amount to the loss of profits, which the plaintiff would have made from the contract if it had been concluded. (Hartkamp 1992 p. 10-11)

5.4.5. The principle of good faith in Estonian law

Estonian law is very progressive in its development of the principle of good faith. While exercising civil rights and performing civil obligations, the obligation to act in good faith, as well as the general clause on good morals, is considered as the most important private law provisions through which constitutional values appear in private law (Kull 2002, p. 142).

In Estonian law, the principle of good faith is established as a constitutional principle. This means that people in social interactions must behave with goodwill, fairly, and justly towards each other. The principle of estoppel and the principle of equity are considered as derivatives of the good faith principle. Moreover, the principle of justice established as a "...basic value of Estonian statehood". (Kull 2002, p.142)

Besides this, the principle of good faith is a general principle of Estonian civil law. Section 108 of the Estonian Civil Code (1994) sets out the general obligation of the person to act in good faith when exercising civil rights and performing civil obligations and it is forbidden to exercise the rights only in for the purpose of causing damage to the other person. The Estonian law of obligations includes provisions establishing the principle of good faith. It is

stated that obligees and obligors shall act in good faith in their relationships between each other (p.6 (1) of Law of Obligation Act of Estonia 2001).

Kull (Kull 2002, p.143) underlines that a contract, the content of which is contrary to the good morals, must be considered as null and void. Such a contract will not receive protection by the courts. The main goal is to reach a fair settlement of a particular case. (Kull 2002, p.143)

5.4.6. The principle of good faith in Finland

The Nordic school of thought is grounded in the doctrine of social welfarism. Social need is the basis for new material values such as contractual balance, security, autonomy, freedom, privacy, remedies, responsibility, and access to justice. It is also the basis for procedural values such as reflexivity in terms of organization, procedure, and competences. The theory of social need places an emphasis on the individual and legal rules should be person-related and guarantee effective protection (Micklitz 1995, p.278-279). Zweigert and Hein Kötz (1998, p.276-278) stated that Nordic countries must, without a doubt, be admitted to form a special legal family, alongside the Romanistic and the German families, by reason of their close interrelationship and their common "stylistic" hallmarks. This statement seems very important because Nordic countries have numerous special features. These features include a lack of modern codes in private law, concrete and practical thinking, and maximum protection of justice and fairness (Eftestøl-Wilhelmsson 2005). In this chapter, Finnish law will be analyzed.

There are many general principles in Finnish contract law. Disputes arising between contracting parties are settled on the basis of general principles, commercial law, or consumer protection law, as well as EU law. The Nordic tradition has been strongly influenced by legal realism. Therefore, Finns will literally follow all EU directives, while a more flexible attitude in southern Europe is more willing to ignore some of them. (Niiniluoto 1995, p.12) As to the general principles, Juha Pöyhönen states that they are, "...the filter through which the system of basic rights influences the law of obligations". (Pöyhönen 2002, p. 61) Among the general principles of Finnish law of obligations are the freedom of action, the protection of good faith (*vilpitön mieli*), the protection of weaker parties, fairness, reciprocity, and reinforcement of appropriate acting ethics. (Pöyhönen 2002, p. 61)

In Finnish legal doctrine, the protection of good faith is defined as, "...juridical protection given to expectations formed by participants in an activity as well as by other parties" (Pöyhönen 2002, p. 61-62).

As a general rule, negotiation offers have no binding effect if they do not lead to the contract. However, the doctrine *culpa in contrahendo* applies when there have been negotiations for a contract, but, because one party was acting in bad faith, no contract was made. For example, one of the parties began negotiation without intention to conclude a contract. This type of responsibility is exceptional. (Saarnilehto 1987, pp. 50-52)

Failure to fulfill general prerequisites of the conclusion of contracts, disturbances linked to the formation of the transaction, and non-compliance with obligatory requirements can result in nullity and invalidity of legal transaction. Primarily, nullity can be based on strong claims which may be, for example, coercion by force (the threatening of life or health), or minority of the other party. Strong claims must be taken into account in the decision-making of any authorities *ex officio* without the need for a parties' claim and, thus, the whole contract becomes invalid. Weak claims are, for instance, duress (the threatening of reputation or defamation of character), blackmail, and fraud. As opposite to strong claims, weak claims affect only certain persons and require a certain kind of claim. A weak claim is always neglected by the court when the object of the contract is in the possession of a third party by means of good faith (Pöyhönen 2002, p. 88-89). These conditions of the contract are established in Sections 28-32, Chapter 3 of the Legal Transactions Act (228/1929).

Also, a contract can be declared null because of the conditions provided by Section 33 (Legal Transactions Act 228/1929). "A transaction that would otherwise be binding shall not be enforceable if it was entered into under circumstances that would make it incompatible with honor and good faith for anyone knowing of those circumstances to invoke the transaction and the person to whom the transaction was directed must be presumed to have known of the circumstances" (Section 33 Legal Transactions Act 228/1929). Section 33 presents the general principle of good faith, which is basically the same as the German *Treu und Glauben*.

In Finnish law, the principle *pacta sunt servanda*, which means "contracts must be respected", is restricted by Section 36 (Legal Transactions Act 228/1929). Section 36 states that a contract can be changed to make it more reasonable by leaving it without effect partly or totally. When assessing unreasonability, the whole juridical act has to be taken under

consideration: the whole content, the positions of parties, conditions at the moment, conditions during conclusion of the contract, and all related matters (Section 33, Legal Transactions Act 228/1929). It is possible to say that freedom of contract is restricted by good faith and reasonability and the purpose of the provision on adjustment is to restore a balance in the contract that has been disrupted. However, the adjustment is an exception to the rule of binding force of contracts. (Pöyhönen 2002, p. 88-89)

Finnish law also provides protection for the good faith purchaser. A pre-condition for the protection is possession of the object in good faith. However, in Finnish law there is an important exception compared to other countries: if the owner of the object has lost possession of the object due to crime (robbery, theft, annexation or moral coercion), the object has to be impounded without financial compensation and there is no protection of good faith. (Rule of implementation of criminal law § 11)

To conclude, Finnish law presents high standards for the protection of justice and the principle of good faith is established as a general principle. The freedom of contract is restricted by the requirements of reasonability and good faith.

5.4.7. The principle of good faith in common law countries

The most minimalist approach to the principle of good faith is represented by the common law of England (Musy 2000, p.2). Scientists (Musy 2000, p.6, Zimmermann & Whittaker 2000, p. 39, Teubner 1998, p.11-32) agree that English law does not recognize a general obligation to negotiate nor to act in good faith.

However, the principle of good faith was established in English merchant law until its disappearance in the 18th century. During the period of 1870-1980, English law began to emphasize some pre-contractual duties between the parties and to develop a new doctrine concerning the principle of good faith. The obligations of good faith were added to a number of contractual relations, for instance, in insurance and company law. Fiduciary relationships, in general, provide several instances of duties that in the civil law world would be related to the good faith principle. The rule of equity is still sound and alive in the English law of remedies; it offers protection against the most difficult situations. For example, the equitable remedy of Promissory Estoppel can offer protection against promise revocation or unjust

withdrawal from negotiations. Family and professional-client relations (special relation or good faith relation) require a duty of good faith and a full disclosure. (Musy 2000, p.7)

The lack of a general obligation of good faith can be described as an illustration of the English attitude to see the law as an independent domain and a world distinct from business and politics. Parties to a contract are free to act as they wish if they do not act in breach of the terms of the contract (Zimmermann 2000 & Whittaker, p.40). English judges do not like to wield power to determine whether the parties have acted in good faith or not. However, often, English courts offer protection of good faith obligations, but they prefer to do it without referring to it as a general principle, which can create a problem regarding the predictability of the legal outcomes of the cases. (Musy 2000, p.7)

Jane Stapleton points out that even if English lawyers do not name it good faith, they believe in the need for legal doctrines that would protect the obligations which arise from such situations as a person being dishonest, a person conducting himself contrary to his word, a person exploiting a position of dominance, or abusing power over a person who is vulnerable relative to him. (Stapleton 1999, p.27)

However, Teubner considers the principle of good faith to be “legal transplant” or “legal irritants”, which is, “...unworkable in practice” and, “...inherently inconsistent with the position of the negotiating parties” (Teubner 1998, p.11-32). He criticizes the provisions of good faith of the Principle of European Contract Law, which, in his opinion, cannot be implemented in English law and should be rejected. Teubner bases his position on the traditions and habits of business relationships in common law countries. In Germany, for instance, the principle of good faith presents a “living law”. In the common law countries, where the financial system is risk-taking, governmental regulation prevails upon non-governmental, labor unions are weak, competition is intense and, therefore, cooperation between the companies is low; the principle of good faith does not have any “fruitful soil” for development and does not belong to legal culture. (Teubner 1998, p.11-32)

To conclude, there is no general obligation of good faith imposed on the parties of a contract in modern English law. However, the courts offer protection of the good faith duties without referring to the general principles. There are different opinions about the general principle of good faith among the legal scientists of the common law system. Some authors consider the

principle of good faith a “legal irritant”; others find a need for legal doctrine to protect the good faith obligations.

5.4.8. The principle of good faith in Russian law

The doctrine of legal positivism had a very strong influence on Russian law in the past and, therefore, such categories as justice and rationality were under-valued by the courts and legislators in the decision-making and law-making processes. However, nowadays, the situation is changing. The general principles begin to influence the court judgments and they find its place in the legislation (Попова 2006, p.3).

In Russian legislation, the principle of good faith appears in public and private law. The provisions concerning good faith were established in the Civil Code, Taxation Code, Family Code, Labor Code, and some other legal acts. The private law area is mainly regulated by the Civil Code. There are numerous provisions in the code concerning good faith — p.2 Art.6, p.3 Art.10, p.3 Art.157, 169, 173, 174, 179, p.1. Arts.401, 404 and 1193 of the Civil Code — and good faith purchasers (Art.301-303). However, in Russian civil legislation, the principle of good faith is not established as a general principle of civil law.

According to Popova (2006, p.10), the objective element of the principle of good faith is established in p.2 Art.6. It states that, if it is not possible to use an analogy of law, the rights and duties of the parties should be defined in accordance with the general principles, the scope of the civil legislation, and the requirements of good faith, rationality and justice. This provision defines guidelines for the court if there are gaps in the legislation.

Other provisions of the Civil Code establish the subjective element of the principle of good faith (Popova 2006, p.11), meaning internal understanding of the duty to behave according to the standards of fairness, honesty, rationality, and loyalty. The subjective element appears as a legal presumption of good faith in p.3 Art.10 of the Civil Code. Besides these legal norms, the requirements of good faith are established in the law of obligations. For instance, if there are precedent conditions in the transaction, the parties should act in good faith and should not influence these conditions. Also, if the transaction is contrary to the fundamental principles of the legal system of Russia and morality, it is null. By analyzing Art.173, 174 (Civil Code of the Russian Federation, Part 1 1994), it is possible to conclude that the legislator defines bad faith as an awareness of the party that his/her actions are unlawful. Moreover, the actions

such as fraud, duress and some others are considered contrary to the requirements of good faith (Art.179, Civil Code of Russian Federation, Part 1 1994). In all these cases, the transaction can be declared null and void. From Art.401 it is possible to deduce that good faith is connected with such concepts as “due care” and ”prudence”, while bad faith is associated with deliberate and careless infliction of damage or non-act to decrease the damage. Furthermore, the legislator often uses the term “reasonable time”, which includes dimensions of the principle of good faith too.

The doctrine of *culpa in contrahendo* is not used in Russian law. Russian legal scientists (Гнищевич 2008, p.123) underline that there are no general conditions for pre-contractual liabilities.

To conclude, the principle of good faith is recognized in Russian law and legal doctrine. However, the principle is not established in Art.1 of the Civil Code of the Russian Federation “Fundamental principles of civil law”. This means that there is no general principle of good faith.

At the moment, there are proposals for regulatory developments to establish the principle of good faith as a general principle of Russian civil law.

5.5. Summary of theory part

After analyzing historical backgrounds of the development of the principle of good faith, comparing the principle of good faith and ethical norms, researching legal doctrine on the principle of good faith, and analyzing national legislations in European countries, it is possible to draw the following conclusions.

- The principle of good faith has a very long development. It appeared in Roman law and became one of the core concepts of the different branches of law. It dominated relations between merchants and became a fundamental principle of medieval and early modern law. Nowadays, despite well-developed legal rules, trust remains a very necessary aspect in business deals.
- In the multinational contract law project of the development of the European Code of Contracts, the notion of “fairness” could serve as the common object of a reconstruction of national traditions of contract law thinking (Joerges 1995, p. 323) and the principle of good faith will become one of the harmonizing elements of European contract law (Zimmermann & Whittaker 2000).
- Every social group has its morality, which is based on habits and traditions.
- Justice, trust, and rationality are basic moral values which are essential to all human beings.
- It is impossible to define what is perfectly good; therefore, social and legal judgments are often guided by moral principles and common sense.
- Ethical and moral norms change during the time and develop in new circumstances.
- Law and moral values are interrelated with each other. Law is a formal tool to define rights and duties.
- It is natural that legal order should be based on the standards of justice and rationality.

- The principle of good faith is an ethical principle; it is closely related to such moral values as justice, trust, rationality, honesty, fairness, loyalty, fidelity, reasonableness, and rationality.
- According to Fuller's theory, good faith can be considered a subject of the morality of duty.
- The principle of good faith was established in the legislation of the different countries. Therefore, it is possible to say that the principle of good faith is at the same time an ethical and a legal principle.
- The legal principle of good faith is a generally recognized legal principle. The principle is very comprehensive; it includes numerous related concepts and duties.
- The principle of good faith and the principle of justice are interrelated principles. In some cases, the principle of good faith is based on the principle of justice. In other cases, the principle of justice and the principle of good faith are intrinsically the same principles.
- The duty of good faith is interrelated with such concepts as voluntariness, the duty not to misrepresent, the duty of disclosure or to keep secrecy, and the duty not to use duress or undue influence.
- The easiest way to define good faith is to "not to act in bad faith" (Bayles 1987, p.189).
- The principle of good faith is interrelated with the principles of reasonable and legitimate expectations, reliance, modifications, mistakes, and the principle of illegal contracts.
- The concept of "general good" (Usher 1995, p.358) includes the dimensions of "good faith".
- *Good faith* in contract law should be estimated at the point of agreement and in every particular contract.
- There are two elements of the principle of good faith: subjective and objective. The objective element is the requirements of good faith, which are established in legal

acts. The subjective element is the internal understanding of the duty to behave according to the standards of fairness, honesty, rationality, fidelity, and loyalty by the person.

- There is a proposition to define what is “guilt” based on the standards of good faith, rationality, and reasonable care.
- The duty to act in good faith is the element of the structure of adherence of the international obligations.
- The legal base of the estoppels is the principle of good faith.
- Germany made a big contribution in the development of the principle of good faith in European law. In German law, *bona fides* appears as the notion of *Treu und Glauben*. It was established in the German Civil Code of 1900 in § 242. The clause has been transformed into one of the famous “general clauses”. It was used to fill code gaps, such as protection of the recipient from a partial or incorrect performance of duties. The German scientist Rudolf von Jhering is credited with the discovery of the doctrine of *culpa in contrahendo*. *Culpa in contrahendo* recognizes a duty to negotiate with care and not to lead a negotiating partner to act to his detriment before a firm contract is concluded.
- The Italian Code provides protection of good faith in the contractual relationships in the several articles. The principle of good faith is established as a general principle in contract law, the law of obligations, and in the pre-contractual relations. Italian legal scientists think that the principle could be used for redistributive purposes; some are worried that it broadens discretionary power of judges.
- In the civil law system of Western Europe, the minimalist view to the principle of good faith is represented by the French courts. However, in the French law of obligations, the principle of good faith is established as a general principle. It is applied in a number of situations: in the formation of contract the parties must deal in good faith, in the performance of contract the principle appeared as the duty of loyalty and the duty of cooperation. The principle of good faith in French law is still weakened by an insufficient application within the courts.
- The concept of good faith permeates all branches of the Dutch law of obligations. The principle of good faith is expressed by the words “equitable and reasonable”. The

principle has three dimensions: contracts must be interpreted according to good faith, “good faith” has a "supplementing" function, and it has a "restrictive" function. The Dutch code lacks a provision of a general character applicable to all civil law relationships. However, the existing statutory provisions affect other branches of law, either directly or *per analogiam*.

- Estonian law is very progressive in the development of the principle of good faith. The principle of good faith is established as a constitutional principle. It is a general principle of Estonian civil law and the law of obligations includes the provisions establishing the principle good faith.
- The Nordic countries have numerous special features, such as lack of modern codes in private law, concrete and practical thinking, and maximum protection of justice and fairness. Finnish law presents high standards for the protection of justice. The Finnish Contracts Act, Section 33, presents a general principle of good faith, which is basically the same as the German *Treu und Glauben*. Freedom of contract is restricted by reasonability and good faith.
- The most minimalist approach to the principle of good faith is represented by the common law of England. English law does not recognize a general duty to negotiate nor to perform in good faith. However, the courts offer protection of the good faith duties without referring to the general principles. There are different opinions about the general principle of good faith among legal scientists about the common law system. Some authors consider the principle of good faith a “legal irritant”; others find a need for the legal doctrine to protect good faith duties.
- The doctrine of legal positivism had a very strong influence on Russian law in the past; therefore, such categories as justice and rationality were not a basis for decision-making and law-making processes. However, nowadays, the situation is changing. The general principles begin to influence the courts’ judgments and find the place in the legislation. In Russian legislation, the principle of good faith appears in public and private law. However, the principle is not established as a general principle of law. The doctrine of *culpa in contrahendo* is not used in Russian law. At the moment, there are proposals for regulatory developments to establish the principle of good faith as a general principle of Russian civil law.

6. PRINCIPLE OF GOOD FAITH IN THE EUROPEAN LEGAL ACTS

6.1. Review of the European legal acts containing provisions about good faith

The principle of good faith can be considered as a general principle of law. Therefore, it is important to understand what the sources of the general principles are. The scientist Neuwahl considers the general principles in the law of the European Union; he states that general constitutional principles can be derived from the EU Treaty or from the system of the Treaty. Moreover, the general principles can be found in secondary EU law, national legal systems, and international law. The general principles can also flow directly from a developing practice of the EU institutions. (Neuwahl 1995, p.45-52) Article 263 deals with judicial review and specifies the grounds upon which an annulment can be based. The second paragraph of the article includes the words "... infringement of the Treaty or of any rule of law relating to their application ..." (Art.263, EU Treaty 2007). Therefore, the phrase "any rule of law" must necessarily refer to something other than the Treaty itself. This article has been used by the ECJ as a basis for the principle that an act of the EU may be quashed for the infringement of a general principle of law. Article 340 (second paragraph) is concerned with non-contractual liability, or tort, and expressly provides that the liability of EU is based on the "...general principles common to the laws of the Member States" (Art.340, EU Treaty 2007). (Mifsud-Bonnici 1996)

To analyze the principle of good faith, the Directive on Unfair Contract Terms (Council Directive 93/13/EEC of 5 April 1993) must be considered as it introduces "...a notion of good faith in order to prevent significant imbalances in the rights and obligations of consumers on the one hand and sellers and suppliers on the other hand. This general requirement is supplemented by a list of examples of terms that may be regarded as unfair" (Directive on Unfair Contract Terms 1993).

The principle of good faith is established in Article 3 of the Directive, which states that "...a contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer" (Art.3, Council Directive 93/13/EEC of 5 April 1993).

The Directive does not give a definition for the “requirement of good faith”; however, as it was mentioned above, it provides the examples of terms which can be understood as acting in bad faith. So, for instance, the Directive puts “the label of unfairness” on terms which require a consumer who fails to fulfill his obligations to pay a disproportionately high sum in compensation (annex 1e) (Wilhelmsson 1995, p.333). Moreover, the annex (1q) to the Directive contains terms excluding or hindering the consumers’ right to take legal action or exercise any other legal remedy are to be regarded as unfair. Examples of such unfair terms can be unacceptable forum clauses or arbitration clauses. Also, binding the consumer to terms with which he had no possibility to become familiar with before the conclusion of the contract, enabling the seller or supplier to change unilaterally the terms of contract or characteristics of the product, or have an exclusive right to interpret any terms of the contract without a valid reason are all considered as contrary to the requirement of good faith. In the opinion of Wilhelmsson, the Directive fulfils the consumers’ legitimate expectations in the market. (Wilhelmsson 1995, p.333)

The Directive on Commercial Agents establishes mutual duty of a commercial agent and a principal to act according the principle of good faith. Thus, a commercial agent should make proper efforts to negotiate, communicate to his principle all necessary information available to him, and comply with reasonable instructions given by his principal. On principal’s part, there are the duties to provide his commercial agent with the necessary documentation relating to the goods concerned, to obtain for an agent the information necessary for the performance of the agency contract, and to inform the commercial agent within a reasonable period of his acceptance, refusal, or non-execution of a commercial transaction which the commercial agent has procured for the principal. (Arts.3-4, Council Directive 86/653/EEC of 18 December 1986, OJ L 382, 1986, p.17-21)

The Money Laundering Directive (Council Directive 91/308/EEC of 10 June 1991, OJ L 166, 1991, p.0077-0083) is intended, essentially, to prohibit transactions in property derived from criminal activity or transactions intended to conceal or disguise its illicit origins. Under Art.3 of that Directive, credit and financial institutions must require identification of customers when entering into business relationships, in particular when opening accounts or offering safe custody facilities, and in the context of any other single transactions or linked transactions involving a sum of €15,000 or more. Under Art.6, credit and financial institutions and their directors and employees must, on their own initiative, inform the

authorities responsible for combating money laundering of any fact which might be an indication of money laundering, and must at the request of those authorities supply them with all necessary information. This information must be given to the responsible authorities in the Member State whose territory the institution forwarding the information is situated. In any event, by virtue of Art.9, disclosure in good faith to the responsible authorities by an employee or director of a credit or financial institution shall not constitute a breach of any restriction on disclosure of information imposed by contract or by any legislation, regulatory, or administrative provision, and shall not involve the institutions or its directors or employees in liability of any kind. (Usher 1995, p.361)

The Consumer Credit Directive (Council Directive 87/102/EEC of 22 December 1986, OJ L 042, 1987, p.0048-0053) also includes provisions concerning the principle of good faith. From the text of the Directive, the rules, which are based on good faith and justice, can be deduced. Such rules are the prohibition of extortionate credit and price discrimination, disclosure of credit cost information, possibilities for the credit adjustments, early repayments, and consumer bankruptcy. (Reifner 1995, p.393)

The Unfair Commercial Practice Directive (Directive 2005/29/EC of 11 May 2005, OJ L 149, 2005, p.22-31) addresses the commercial practices directly related to influencing consumers' transactional decisions, including unfair advertising and marketing practices. The general principle of good faith is established in Art.2 of the Directive. It is stated that a "professional diligence" is the standard of special skill and care which businesses may reasonably be expected to exercise towards consumers. It must be commensurate with honest market practice and/or the general principle of good faith in the trader's field of activity (p.h, Art.2). The commercial practices can be considered as unfair if they are contrary to the requirements of professional diligence (p.2a, Art.5), and so they are contrary to the principle of good faith. The unfair business-to-consumer commercial practices can be divided to misleading commercial practices and aggressive commercial practices. The Directive provides the list with example of such behavior (annex 1), which can be understood as behavior in bad faith. For instance, stating that a product can legally be sold when it cannot, that the trader is about to cease trading or move premises when he is not, falsely claiming that a product able to cure illnesses, or that product will be only available for a very limited time, and some other actions can be considered as misleading commercial practices. Examples of aggressive commercial practices include the creation of the impression that the consumer cannot leave the premises

until a contract is formed, the false impression that the consumer has already won or will win when in fact there is no prize, the implication that the trader's livelihood will be in danger if the consumer does not buy the product, and others practices. The target of the Directive is to protect the consumer from the decisions which he would not make if the commercial practices would be carried out in good faith.

It is possible to conclude that European legislation contains provisions concerning the principle of good faith. There is no definition of good faith; however, the legal acts provide the list of examples of the actions in bad faith.

6.2. Review of the international legal acts establishing the principle of good faith

There are different points of view about the nature of the international general principles. Without a doubt, the international general principles can be found in the national laws (Wopera 2008, p. 29). Some scientists, Verdross and *Völkerrecht* (Тункин 2000, p.171), think that international general principles arise from a common legal consciousness. Other scientists (Лукашук 1997, p.105; Тункин 2000, p.179) state that international general principles appear in the national legal systems and, through the international treaties and international practices, become general principles of international law.

The principle of good faith is recognized as a general principle of international law and the evidence for this statement can be found in international legal acts.

The Vienna Convention on the Law of Treaties of 1969, in the preamble, states that the parties are, "...noting that the principles of free consent and of good faith and the *pacta sunt servanda* rule are universally recognized". Also, Art.26 establishes that, "...every treaty in force is binding upon the parties to it and must be performed by them in good faith". The general rule of interpretation (Art.31) requires that treaties are, "...interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose". Moreover, the principle of good faith is established in the Charter of United Nations (1945) and Declaration on principles of international law concerning friendly relations and cooperation among states (1970), where it is stated that Member States should fulfill the obligations in good faith in accordance with the Charter, international principles, and international agreements. It is possible to say that the principle of

good faith is established as a general principle in international public law and it governs all international relations.

Further, the United Nations Convention on Contracts for the International Sales of Goods 1980, the UNIDROIT Principles of International Commercial Contracts 2004, and the Principles of European Contract Law 2002 are analyzed because these international acts can be understood as very important sources of international contract law.

6.2.1. The principle of good faith in the United Nations Convention on Contracts for the International Sales of Goods 1980

The Vienna Convention (United Nations Convention on Contracts for the International Sales of Goods) of 1980 is a treaty proposing a uniform international sales law, which includes a comprehensive code of legal rules governing the formation of contracts for the international sale of goods, the obligations of the buyer and seller, remedies for breach of contract, and other aspects of the contract (UNCITRAL, United Nations Convention on Contracts for the International Sales of Goods 1980).

In the general provisions (Art.7) the principle of good faith is established as a general principle of the Convention. The article states that, "...in the interpretation of the Convention, regard is to be had... to promote...the observance of good faith in international trade" (Explanatory note by the UNCITRAL Secretariat on the United Nations conventions for the international sales of goods). In particular, when a question concerning a matter governed by the Convention is not expressly settled in it, the question is to be settled in conformity with the general principles on which the Convention is based (Explanatory note by the UNCITRAL Secretariat on the United Nations conventions for the international sales of goods).

The expressions "reasonable person", "reasonable time", "unreasonable inconvenience", and "unreasonable expenses" are widely used in the Convention, for instance, in the p.2,3 Art.8, p.2 Art.18, Art.34, Art.37, Art.39, and other articles. The concept of "due care" is also applied. For example, p.2 Art.35 states that the goods should be, "...contained or packaged in the manner usual for such goods or, where there is no such manner, in a manner adequate to preserve and protect the goods" (United Nations Convention on Contracts for the International Sales of Goods 1980). Moreover, the Convention establishes the duty to disclosure. Such duty appears in the Art.40 where the seller is liable for the lack of

conformity if it, "...relates to facts of which he knew or could not have been unaware and which he did not disclose to the buyer" (United Nations Convention on Contracts for the International Sales of Goods 1980).

6.2.2. Principle of good faith in the UNIDROIT Principles of International Commercial Contracts 2004

The UNIDROIT Principles of International Commercial Contracts of 2004 is a set of rules of contract law for use by merchants and business people in cross border transactions. Since their first publication in 1994, the Principles have proved to be a serious alternative to national contract laws in international disputes decided by arbitral tribunals, such as those administered by the International Chamber of Commerce (ICC). At the same time, they have been accepted as a model for reforming the laws on international contracts by countries such as Russia, China, Estonia, and Lithuania. (Kleinheisterkamp & Vogenauer 2009)

In 2004, the Governing Council of UNIDROIT adopted the new edition of the UNIDROIT Principles of International Commercial Contracts. As compared to the first edition published in 1994, the second edition contains 5 additional chapters as well as an expanded Preamble and new provisions on Inconsistent Behavior and on Release by Agreement. Additionally, wherever appropriate, the 1994 edition of the Principles has been adapted to meet the needs of electronic contracting. (UNIDROIT, UNIDROIT Principles of International Commercial Contracts 2004)

The UNIDROIT Principles, "...attempt to ensure fairness in international commercial relations by expressly stating the general duty of the parties to act in accordance with good faith and fair dealing and, in a number of specific instances, imposing standards of reasonable behavior" (Introduction to the 1994 edition, UNIDROIT, p.XV).

One of the mandatory provisions of the principles is Art.1.7 on good faith and fair dealing. (Art.1.5, Comment, UNIDROIT, p.14). It is possible to say that Art.1.7 establishes one of the purposes of the principles. Such purpose is, "...to promote the observance of good faith and fair dealing in contractual relations" (Art.1.6, Comment, UNIDROIT, p.16). Art.17 "Good faith and fair dealing" states that, "...each party must act in accordance with good faith and fair dealing in international trade" and, "...the parties may not exclude or limit this duty" (Art. 1.7, UNIDROIT, p.18).

“Good faith and fair dealing” is a fundamental idea of the Principles, because there are many provisions in the different chapters which constitute a direct or indirect application of the principle of good faith and fair dealing, for instance, Art.1.8, Arts.1.9(2); 2.1.4(2)(b), 2.1.15, 2.1.16, 2.1.18 and 2.1.20; 2.2.4(2), 2.2.5(2), 2.2.7 and 2.2.10; 3.5, 3.8 and 3.10; 4.1(2), 4.2(2), 4.6 and 4.8; 5.1.2 and 5.1.3; 5.2.5; 6.1.3, 6.1.5, 6.1.16(2) and 6.1.17(1); 6.2.3(3)(4); 7.1.2, 7.1.6 and 7.1.7; 7.2.2(b)(c); 7.4.8 and 7.4.13; 9.1.3, 9.1.4 and 9.1.10(1). These articles will be analyzed below. Para.1 of the Art.1.7 is a general term which states that each party must act in accordance with good faith and fair dealing and, therefore, it is clear that even in the lack of special provisions in the Principles the parties’ behavior in the contractual relationships always must conform to good faith and fair dealing, including the negotiation process (Art.1.7, Comment, UNIDROIT, p.18).

In the Comment of the Principles, it is underlined that the behavior contrary to the principle of good faith and fair dealing in some legal systems is known as “abuse of rights”. Such behavior occurs, for instance, when a party exercises a right only to damage the other party, or for a purpose other than the one for which it had a right, or when the exercise of a right contrary to the originally intended result. Here is an example of such behavior. For instance, *Party A* rents premises from *Party B* and opens a restaurant. During the summer months, *Party A* sets up a few tables out of doors on the owner's property. *Party B* has increasing difficulties finding tenants for apartments in the same building because the customers of the restaurant keep noise late at night. *Party B* would be abusing its rights or acting against the principle of good faith if, instead of requesting *Party A* not to serve out of doors late at night, it required *Party A* not to serve out of doors at all. (Art.1.7, Comment, UNIDROIT, p.19)

Moreover, in the Comments, it is stated that provisions concerning good faith and fair dealing are applied in international trade, but the special conditions of international trade must be taken into account. Therefore, only some domestic standards may be applied to the extent that they are shown to be generally accepted among the various legal systems. For instance, according to the domestic legislation of several countries, the purchaser of high-technology equipment loses the right to rely on any defect in the goods if it does not give notice to the seller specifying the nature of the defect without undue delay after it has discovered or ought to have discovered the defect. If *Party A* operates in a country where this type of equipment is so far almost unknown, *Party A* does not lose its right to rely on the defect because *Party B*,

being aware of *Party A*'s lack of technical knowledge, could not reasonably have expected *Party A* properly to identify the nature of the defect. (Art.1.7, Comment, UNIDROIT, p.20)

The mandatory nature of the principle of good faith and fair dealing appears in such way that parties may not contractually exclude or limit this principle. However, parties can provide in their contract a duty to observe more strict standards of behavior. (Art.1.7, Comment, UNIDROIT, p.21)

Art.1.8 "Inconsistent Behavior" is an application of the principle of good faith (Art.1.8, Comment, UNIDROIT, p.21). It states that, "...a party cannot act inconsistently with an understanding it has caused the other party to have and upon which that other party reasonably has acted in reliance to its detriment" (Art.1.8, UNIDROIT, p.21). For instance, *Party B* falsely understood that contract can be performed in a particular way. *Party B* proceeds with the performance. *Party A* does not tell anything about the mistake despite the fact that *Party A* and *Party B* meet regularly. *Party A* will be precluded from arguing that performance did not comply with the contract. (Art.1.8, Comment, UNIDROIT, p.22). In other words, if *Party A* would insist that there was a mistake in the performance, his behavior would be contrary to the principle of good faith. Therefore, it is possible to say that the principle of good faith requires performance of unwritten obligations too.

Such category as reasonableness underlined in the Arts.1.9(2); 2.1.4(2)(b), 2.1.18.

The German doctrine *culpa in contrahendo* appears in Art.2.1.15 "Negotiations in bad faith". Parties during the negotiation are normally not liable for failure to reach the agreement. If the parties break the negotiation in bad faith, or begin and continue negotiation without purpose to reach the agreement, one party is liable for losses caused to the other party (Art.2.1.15, UNIDROIT, p.59). Also, at some point of negotiation, a party is not allowed to break the negotiation without justification. Such point depends on circumstances of the case and the extent to which the other party had reason to rely on the positive outcome of negotiation. (Art.2.1.15, Comment, UNIDROIT, p.61)

Likewise, a party which is involved in the negotiation has a duty not to disclosure or use in bad faith the information which was given to it in confidential (Art.2.1.16, UNIDROIT, p.61).

The Principles establish provisions on “surprising terms”; these terms are considered a surprise in that they would not be reasonably expected by the party (Art.2.1.20, UNIDROIT, p.67). The estimation whether the term is “surprising” or not is based on the trade sector and the way in which the parties conducted their negotiation (Art.2.1.20, Comment, UNIDROIT, p.68).

The Principles also established the duties of the agent and the principal to act in good faith (Arts.2.2.4 (2), 2.2.5 (2), 2.2.7, UNIDROIT, p.81).

The principle of good faith is also included in Art.3.5 “Relevant mistake”. It states that a contract is not valid if, “...the other party made the same mistake, or caused the mistake, or knew or ought to have known of the mistake and it was contrary to reasonable commercial standards of fair dealing to leave the mistaken party in error” (Art.3.5, UNIDROIT, p. 98). In order to avoid the contract, the mistaken party must also show that the other party was under a duty to inform it of its error (Art.3.5, UNIDROIT, p.101).

The UNIDROIT Principles prohibit fraud and gross disparity. Fraud could appear as fraudulent representation, including language or practices, or fraudulent non-disclosure of circumstances, which should be disclosed (Art.3.8, UNIDROIT, p.102). Gross disparity is based on the fact the other party has taken unfair advantage of the first party’s dependence, economic distress or urgent needs, or its improvidence, ignorance, inexperience, or lack of bargaining skill (Art.3.10, UNIDROIT, p.106).

The principle of good faith is involved in the interpretation of the contract, statement, and other conduct when the common intention of the parties cannot be established. In such case, “... the contract shall be interpreted according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances” (Arts.4.1, 4.2 UNIDROIT, p.118). Art.4.6 states that the vague terms, which are provided by one party, is interpreted against that party (Art.4.6, UNIDROIT, p.125). Also, if there is some term missing in the contract, the appropriate term shall be supplied, which is satisfying, among others requirements of good faith and fair dealing and reasonableness (Art.4.8, UNIDROIT, p. 127).

Art.5.1.2 describes sources of implied obligation in the contract. These obligations should be based, among others, on the nature and purpose of the contract, or maybe consequence of the

principle good faith, fair dealing, and reasonableness in the contractual relationships. (Art.5.1.2, Comment, UNIDROIT, p.129-130)

Art.5.1.3 establishes the duty of co-operation, if it is reasonably expected for the performance of the obligations. A contract is not merely a meeting point for conflicting interests but must also, to a certain extent, be viewed as a common project in which each party must cooperate. This view is clearly related to the principle of good faith and fair dealing (Art.1.7) which permeates the law of contract. The duty of co-operation must of course be confined within certain limits, so as not to upset the allocation of duties in the performance of the contract. (Art.5.1.3, Comment, UNIDROIT, p.131)

The principle of good faith is taken into account in estimation of possibilities of partial performance and earlier performance. There may be situations where the obligee's legitimate interest in receiving full performance is not definite and where temporary acceptance of partial performance will not cause any major harm to the obligee. The same situation can be involved with earlier performance, which under certain circumstances can cause no harm for the receiver. If the party tendering partial or earlier performance proves this to be the case, the obligee cannot then refuse such partial performance, and there is no non-performance in such cases. This may be seen as a consequence of the general principle of good faith and fair dealing. (Arts.6.1.3, 6.1.5, UNIDROIT, pp.153-157)

The Principles established the rule that each party must bear any increase of expenses occasioned by a change in its place of business. It is possible that a party's move may cause other inconvenience for the other party. Therefore, the obligation to act in good faith (Art.1.7) and the duty to cooperate (Art.5.1.3) will often impose on the moving party an obligation to inform the other party in reasonable time so as to enable the latter to make such preparations as may be necessary. (Art.6.1.16 (2), Comment, UNIDROIT, p.159)

In the case of hardship of the party, a renegotiation may be requested. Such request for renegotiations by the disadvantaged party and the conduct of both parties during the renegotiation process are subject to the general principle of good faith and to the duty of cooperation. Therefore, the party requesting a renegotiation must honestly believe that a case of hardship actually exists and may not use this situation only as a tactical maneuver. Moreover, both parties must conduct renegotiations in a constructive manner, in particular by refraining from any form of obstruction and by providing all the necessary information. If the

agreement was not reached the parties may resort to the court. The contract will be terminated or adapted by the court only when this is reasonable. (Art.6.2.3, Comment, UNIDROIT, pp.188-191)

The principle of good faith is a base for the exclusion of liability for non-performance if non-performance was caused by the other's party's act or omission, some event to which the other party bears the risk, or force majeure (Arts.7.1.2, 7.1.7 UNIDROIT, p.194, pp.206-207). On the other hand, it is prohibited to include clauses which excludes one party's liability for non-performance or which permits significantly different performance. This prohibition arises from the principle of good faith and fair dealing. The reason for the inclusion of a specific provision on exemption clauses is that they are particularly common in international contract practice and tend to give rise to much controversy between the parties. Such rule gives the court a broad discretionary power based on the principle of fairness, therefore, the court may ignore clauses which are grossly unfair. (Art.7.1.6, Comment, UNIDROIT, p.203)

The performance of non-monetary obligation occurs in exceptional cases, particularly when there has been a significant change of circumstances after the conclusion of a contract; performance, although still possible, may have become so challenging that it would be contrary to the general principle of good faith and fair dealing. This rule is established in Art.7.2.2. (Comment, UNIDROIT, pp.209-210)

The duty of an aggrieved party to mitigate harm is established in Art.7.4.8. The purpose of this article is to avoid the party passively waiting to be compensated for harm which it could have avoided or reduced. Any harm which the aggrieved party could have avoided by taking reasonable steps will not be compensated. The steps to be taken by the party may be directed either to limiting the extent of the harm above all when there is a risk of it lasting for a long time if such steps are not taken, or to avoiding any increase in the initial harm. (Art.7.4.8, Comment, UNIDROIT, p.244)

The principle of good faith prevents the possibility of abuse of the right for agreed payment for non-performance (Art.7.4.13, UNIDROIT, pp.251-252). This article permits the reduction of the agreed sum if it is grossly excessive, "...in relation to the harm resulting from the non-performance and to the other circumstances". The parties may not exclude the possibility of reduction. The agreed sum may only be reduced, but not entirely, to award damages corresponding to the exact amount of the harm. It is important that the amount of payment

must be “grossly excessive”, so that it would clearly appear to be so to any reasonable person. (Art.7.4.13, Comment, UNIDROIT, p.251-252)

Moreover, the principle of good faith is applied in the relations between the assignor, the assignee, and the obligor in the assignment of rights. Therefore, it is established that a right to non-monetary performance and a right to the partial payment of a monetary sum maybe assigned only if it the assignment does not contain the obligation significantly bigger burdensome. (Arts.9.1.3, 9.1.4, UNIDROIT, pp.269-270)

Only after the obligor receives a notice, the assignment becomes effective towards the obligor so that he is liable to pay to the assignee. The purpose is to place the burden of informing on the parties of agreement - the assignor and the assignee. However, it does not necessarily exclude that in certain circumstances the obligor will be liable for damages if they acted in bad faith when it paid the assignor. (Art.9.1.10, Comment, UNIDROIT, p.279)

After analyzing the above presented provisions, it is possible to conclude that the principle of good faith, being established as a general principle, permeates many rules of the Principles of International Commercial Contracts. Such rules concern the formation of contracts, authority of agents, validity and interpretation of contracts, the rights of third party, performance and non-performance, and assignment of rights.

6.2.3. The Principles of European Contract Law 2002 and the principle of good faith

The Principles of European Contract Law of 2002 represent a project on the way to a common understanding of European Private Law. The Principles were compiled by the Commission on European Contract Law, also known as the “Lando-Commission”. The Principles are comprised of three parts. Part I and II concern the formation of contracts, validity, performance, and remedies for non-performance. Part I of these principles was released in 1995; part II was completed in 1996 and published in 2000. Part III focuses upon general contract law questions, such as prescription, set-off, plurality of debtors, illegality, unconscionability, conditions, and capitalization interest. (Max Planck Institute for Comparative and International Private Law, Principles of European Contract Law 2002)

One of the purposes of the Principles of the European Contract Law is, “... to promote good faith and fair dealing, certainty in contractual relationships, and uniformity of application”

(Art.1:106). All issues which are not resolved in the Principles should be settled according to the ideas established in the Principles (Art.1:106). Art1:102 states the main principle of contract law — freedom of contract; however, this freedom is limited by the requirements of good faith and fair dealing (Art.1:102).

The general obligations established in Art.1:201, entitled “Good Faith and Fair Dealing”, requires that, “...each party must act in accordance with good faith and fair dealing”. Moreover, the article states that such duty is mandatory because it is not possible to exclude or limit it. As a consequence of the general obligation to act in good faith, the Principles establish the duty to co-operate in order to reach the goal of the contract (Art.1:202). The concept of reasonableness interrelated with the principle of good faith appears in Article 1:302. The action is reasonable if the person acting in good faith in the same situation would do the same action (Art.1:302).

The Principle prevents the contracting parties from the harm that can be done by a third person involved in making a contract, or entrusted with performance by a party, or performed with their permission. If such person acts intentionally harmful, or with gross negligence contrary to the principle of good faith, the person will be liable for his behavior, the imputed knowledge, or foresight. (Art.1:305)

Similar to the Principles of International Commercial Contracts (UNIDROIT), the Principles of European Contract Law establish liability for negotiations, which originates from the German doctrine *culpa in contrahendo*. Article 2:301 (2) entitled “Negotiations Contrary to Good Faith”, states that, “...a party who has negotiated or broken off negotiations contrary to good faith and fair dealing is liable for the losses caused to the other party”. It continues with the explanation that it is obviously contrary to the principle of good faith to start the negotiation without intention to reach the agreement. (Art.2:301)

Article 4:103 established rules about mistakes as to facts or law which are similar to the Principles of International Commercial Contracts (UNIDROIT). A party may avoid the contract for such mistake if the mistake was caused by wrong information given by the other party, or the other party knew or ought to have known of the mistake and did not inform the mistaken party. Such actions are considered as contrary to the principle of good faith; therefore, the contract will be invalid. (Art.4:103)

Article 4:107 prohibits fraudulent representation and establishes the duty to disclose the necessary information. To decide which information it is necessary to disclose according to the requirements of good faith and fair dealing, aspects such as special expertise of the party, costs of relevant information, possibility to acquire information, and importance of information should be estimated (Art.4:103).

The contract can be avoided also for the reason if one party has excessive benefit or unfair advantage (Art.4:109). For instance, if a party was dependent on or had a relationship of trust with the other party, was in difficult economical situation or had an urgent needs, or, "...was improvident, ignorant, inexperienced or lacking in bargaining skill" (Art.4:109). If the other party knew or was supposed to know the situation and used it for their own benefit to get an unfair advantage, the court will consider the situation as contrary to the requirement of good faith and may adapt the contract or the contract can be void (Art.4:109). Moreover, if some terms of the contract were not individually negotiated and these terms cause significant imbalance of rights and obligations of the parties, they can be avoided. Such "unfair terms" are contrary to the requirements of good faith. (Art.4:110)

Article 4:118 underlines that remedies for provisions on fraud, threats, unfair benefits, and unfair contract terms are mandatory. The parties cannot exclude or restrict them. Remedies for mistake and incorrect performance can be excluded only if it is not contrary to the principle of good faith. (Art.4:118)

During the interpretation of the contract, the principle of good faith and fair dealing, among other aspects, shall be taken in account (Art.5:102). The implied obligations, which arise in the contract, should be grounded on the principle of good faith too (Art.6:102).

Change of circumstances may cause significant difficulties in performance of the contract; therefore, the parties may renegotiate the contract. However, if parties are not able to reach an agreement, the court can terminate or adapt the contract. If one party refused to negotiate, broke the negotiation, and was acting in bad faith, it will be liable for damages. (Art.6:111)

The Principles of European Contract Law establishes that relations between the assignor and the assignee are the subject of the requirements of good faith. Therefore, the assignor must disclose to the assignee all necessary information, for instance, about the rights which the debtor might have against the assignor. Moreover, the claim can be modified without consent

of the assignee only if, "... it is made in good faith and is of a nature to which the assignee could not reasonably object". (Art.11:204)

Parties must act in accordance to the principle of good faith if a contractual obligation is made conditional upon the occurrence of an uncertain future event. If a party prevented the event, by the actions which are contrary to duties of good faith and fair dealing or co-operation, the condition is deemed to be fulfilled.

The Principles of European Contract Law widely uses the concept of good faith and fair dealing. The principle of good faith was established as a general principle and is repeated in the articles where it is particularly important. Most of the situations when the principle of good faith is applied are the same as in the Principles of International Commercial Contracts (UNIDROIT). However, the Principle of European Contract Law more often underlines the requirements of good faith and not just deemed it.

After presenting and analyzing the European and international legislation where the principle of good faith is established, it is possible to draw the following conclusions:

- The provisions containing requirements of the principle of good faith exist in European and international legislation, and regulate, in detail, the way of application of the principle of good faith and its content. However, in the legal acts of the EU and international legislation, there is no definition of the principle of good faith.
- The Directive on Unfair Contract Terms uses the terms "good faith" or "requirements of good faith" but does not define them. However, it provides a list of a number of situations which are contrary to the principle of good faith. In the Directive, good faith is closely interrelated with the concept of fairness.
- The Directive on Commercial Agent establishes mutual duties of good faith between a commercial agent and a principal. Such duties include the duty to inform, the duty of due care, and the duty to disclosure.
- The Money Laundering Directive states that good faith requires disclosure of information by credit and financial institutions to the authorities in the case of any fact which might be an indication of money laundering.

- The principle of disclosure as an element of the principle of good faith is also established in the Consumer Credit Directive.
- The Unfair Commercial Practice Directive states that professional diligence must be commensurate with the general principle of good faith. Commercial practices are unfair if they are contrary to the requirements of the professional diligence and the general principle of good faith. The behavior of bad faith in the field of commercial practices can be divided into misleading commercial practices and aggressive commercial practices.
- In international legislation, the principle of good faith is established in public and private law and penetrates through all international relations. After analyzing international legislation, it is possible to state that the principle of good faith is an independent universally recognized legal rule, which guides all relations between states, institutions, legal and natural persons. As for international trade, the Vienna Convention of 1980, UNIDROIT Principles of 2004, and the Principles of European Contract Law establish the general principle of good faith in their provisions. The Vienna Convention presents a more abstractive rule about the principle, compared to the UNIDROIT Principles and PECL, which regulate in details the application and the content of the principle of good faith. To summarize, in international trade, the principle of good faith is applicable to relations between the contracting parties starting from the negotiation stage and ending in the stage of contract performance. There are certain requirements of good faith and a certain way of behavior which should be followed by the parties Such requirements are:
 - to enter negotiation and to continue it with the purpose to conclude a contract;
 - prohibition to disclose confidential information, which was received during negotiation;
 - compliance with compulsory provisions of national legislation;
 - prohibition to use dependant, fiduciary position of the party or other conditions, which can lead to unfair profit;

- honest behavior with the contracting party, requiring disclosure of all necessary information and prohibiting information hiding
- disclosure of information about the possible damages;
- cooperation during performance of obligations;
- prohibition to profit from the own unlawful actions;
- performance of all obligations in the contract, including unwritten obligations;
- possibility of earlier and partial performance, if it does not make any harm obligee;
- renegotiation of the contract and cooperation in minimizing damages.

Further development and unified approaches to the application of the principle of good faith can be observed in the legal practices of the European courts, which will be analyzed next.

7. UNDERSTANDING OF THE PRINCIPLE OF GOOD FAITH BY THE EUROPEAN COURT OF HUMAN RIGHTS AND THE EUROPEAN COURT OF JUSTICE.

7.1. Importance of the ECHR and the ECJ for the European countries

European integration has moved forward at such a great speed that the structure of democracy in the national states has been changed significantly. Under the influence of European regulations and case law, the functions of legislative, executive, and judicial power have been expanded and redefined. The new “constitutional order” caused by European integration also has consequences for the rule of law. The Court of Justice stood at the cradle of the development of the European legal order by establishing supremacy of EU law, direct effect, and acknowledgement of autonomous EU powers. It has also provided the necessary legal protection and acknowledgement of the principles of EU law. (Vervaele 1995, p. 171)

The importance of the courts judgments is underlined by lots of other scientists (Taylor 1995, p.9-11; Estella 2002, p.137-139). For example, Richard D. Taylor states, that, “...cases are still the most important source of the law of contract” (Taylor 1995, p.9). The purpose of reading cases is not merely to learn the rule or principle which the case is an authority for, but to gain an insight into how the courts arrive at those principles and rules and how the judges interpret facts and apply legal principles to those facts. The cases have a real insight into how the principles can be applied to the factual situations. (Taylor 1995, p.9)

The European Court of Human Rights is the court set up in Strasbourg in 1959 to examine alleged violations and ensure that States comply with their obligations under the Convention on Human Rights of 1953. During the past half-century the Court has made more than 10,000 judgments. Its decisions are obligatory for the States and have bound governments to amend legislation and administrative practice in many fields. As it is stated in the ECHR website, “...the Court’s case-law, the European Convention on Human Rights has become a dynamic and powerful instrument in the response to new challenges and the ongoing promotion of the rule of law and democracy in Europe”. (The Registry of the ECHR, The European Court of Human Rights, Some Facts and Figures)

The European Court of Justice of the European Union, which was established in 1952 and has its seat in Luxembourg, consists of three courts: the Court of Justice, the Court of First

Instance (created in 1988) and the Civil Service Tribunal (created in 2004). The mission of the court is to ensure that, "...the law is observed...in the interpretation and application" of the Treaties (CURIA, General Presentation). It includes the reviews of the legality of the acts of the institutions of the European Union, ensuring that the Member States comply with their obligations under EU law, interpretation of the EU law at the request of the national courts, and tribunals. This mission is the so-called preliminary ruling of the ECJ. (CURIA, General Presentation)

The European Court of Justice deals with political and economic matters, directly or indirectly. It helps to create social or organic solidarity, including the creation of a political, cultural, legal, and economic community. (Snyder 1995, p. 96-97)

Tuomas Ojanen (1998) makes an example from the speech of English judge in 1977, which stated that in the EU, everybody should do as the European Court does and international conventions should interpret it in the same spirit and by same methods as the judges of other countries do, "...so as obtain a uniform result" (Ojanen 1998, p.9).

Tuomas Ojanen explains that the European way has two dimensions; two "lanes". One lane consists of the set of norms, concepts, doctrines, etc. that account for the interpretation and application of EU law whenever the national courts decide to do it themselves; they can determine issues of EU law without consulting the Court of Justice. Another lane includes norms specifying duties of national courts under so called reference procedure. Under this procedure, national courts are entitled, and, on some occasions, obliged to refer questions as to the meaning of EU law to the Court of Justice (Ojanen 1998, p.11). A reference procedure has been conceived as, "...an index both of judicial co-operation between the Court of Justice and the national courts of the Member States" (Ojanen 1998, p.11-12) and the integration of the EU law into national law (Ojanen 1998, p.11-12).

Other scientists (Neuwahl 1995, p.63) present questions about the role of the ECJ, such as whether the Court of Justice, when making judgment, may be induced to forming a view of attitudes prevailing in the living society and it would depend on national courts to take charge of the aspects of constitutional adjudication. Neuwahl states that the Court of Justice has already played an indispensable part in the process of constitutionalization of the EU by granting and protecting the fundamental principles by progressively interpreting the Treaty. On the other hand, however, the Court of Justice does not perform to everybody's

expectations as a constitutional court. This criticism arises because there is a debate among scientists within the EU about the choice between maintaining the highest standards of rights and social justice protection, and the average one in function of the constitutional traditions of the Member States. (Neuwahl 1995, p.63-64)

However, it is true that in a remarkably short period of time, about 50 years, the ECJ has without doubt become one of the most significant judicial institutions in the world. It is an attractive venue for interest groups to publicly confront Member States because of its high level of recognition amongst European citizens. Also, the prospect of favorable decisions contributing to European-wide change as opposed to narrow focus of domestic litigation is very important. There is an opinion that the governments of the larger Member States should also appreciate the ECJ's wide competency. (Masson & O'Connor 2007, p.245)

7.2. Application of the principle of good faith by the ECHR

Case-law of the European Court of Human Rights compromises law and ethics (Микели де Сальвиа 2004, p.15). The ECHR applies the concept of good faith even though there are no provisions establishing the general principle of good faith in the Convention for the Protection of Human Rights and Fundamental Freedoms. The judgments where the concept of good faith is applied will be analyzed below. The judgments will be grouped according to the similarities in the way of the application of the principle of good faith.

The ECHR underlines in its decisions that good faith should be based on facts. This statement can be proved by the following cases.

In the case *Europapress Holding d.o.o—Croatia*, the dispute arose between a newspaper publisher and the Minister of Finance. The magazine published the article “Minister S. pointed a handgun at journalist E.V”. Article 10 of the Convention on Human Rights establishes the freedom of expression; however, the ECHR argues that journalists require acting in good faith in order to provide accurate and reliable information. The fact that the minister pointed the hand gun was described in the article as undoubtedly true. However, the journalist could not prove this fact. Eye-witnesses had testified that at no time was the gun was pointed at E.V. Therefore, there were no facts confirming that the newspaper publisher was acting in good faith in providing the information in the article. The conclusion made by

the court was that the Art.10 of the Convention was not violated. (*Europapress Holding d.o.o—Croatia*, 25333/06, Judgment 22.10.2009)

The same decision was made in the case *Brunet-Lecomte and others – France*, where the magazine published the interview of the former manager of a bank, in which he reported large-scale money laundering by the bank and black-market money from tax evasion and criminal activities of the bank. Such statements were not proven by any facts and in the comments of the interview there were no moderation of the statements. Therefore, the ECHR saw lack of good faith of the publisher of the magazine. (*Brunet-Lecomte and others – France*, 42117/04, Judgment 5.2.2009) Furthermore, in the case *Mihaiu-Romania* the ECHR detected that a journalist wrote the article in bad faith, without appropriate factual basis (*Mihaiu-Romania*, 42512/02, Judgment 4.11.2008).

In the case *Wojtas-Kaletka—Poland*, the applicant, in comments to the press in her trade-union capacity and in an open letter, criticized the decision of a public television company to stop broadcasting two classical music programs. The journalist was reprimanded and a higher regional court found in the applicant's behavior that there was a breach of her duty of loyalty towards her employer. However, the ECHR stated that, "... the applicant's good faith was not in dispute" (*Wojtas-Kaletka—Poland*, 20463/02, Judgment 16.07.2009), because the journalist's comments had had a sufficient factual basis; no personal accusations had been made and the tone had been measured. Therefore, the ECHR found violation of Art.10 of the Convention "Freedom of expression". (*Wojtas-Kaletka—Poland*, 20463/02, Judgment 16.07.2009)

A similar decision was made in the case *Sorguc-Turkey*, where a university professor criticized the system of appointment and promotion of academics in the university. The professor made an example of a candidate without mentioning his name, who did not have the academic qualifications required for the post of assistant professor. The national court ordered the professor to pay damages for the assistant. However, the ECHR underlined that the professor's statement was based on facts and he had voiced it in good faith. Hence, the ECHR found violation of academic freedom and, especially, freedom to express opinion about the institution or system in which they worked. (*Sorguc-Turkey*, 17089/03, Judgment 23.06.2009) In the case of *Juppala – Finland*, a violation of the freedom of expression has been indicated by the ECHR too, because the applicant was acting in good faith and told the

truth about her suspicions - that her grandchild was bitten by his parent even though the fact was not confirmed in the future investigation (*Juppala – Finland*, 18620/03, Judgment 2.12.2008). The same decision was done in the case, *Lombardo and others – Malta* (*Lombardo and others – Malta*, 7333/06, Judgment 24.4.2007), *Tonsbergs Blad AS and Haukom - Norway* (*Tonsbergs Blad AS and Haukom - Norway*, 510/04, Judgment 1.3.2007), *Mamere – France* (*Mamere – France*, 12697/03, Judgment 7.11.2006), and other cases.

The ECHR applies the principle of good faith to secure balance of interests, fairness, and protection of possession.

In the case *Moskal-Poland*, the applicant was granted an early-retirement pension, which was, “...valid indefinitely” (*Moskal-Poland*, 10373/05, Judgement 15.9.2009). Based on that grant, the applicant resigned from her full-time job. However, after 10 months the pension was discontinued because the Social Security Board made a decision that the pension was awarded by mistake. The applicant has applied for the early-retirement pension in good faith and did not break the applicable law. On the other hand, the authorities are allowed to correct their mistakes and it would be unfair to other individuals contributing to the social-security fund, especially those who have been denied a benefit because they did not meet statutory requirements. The ECHR has taken into account that the applicant acted in good faith, that the early-retirement pension was the sole source of income of the applicant and there are difficulties in securing new employment. Therefore, the court has made a decision that a fair balance between the demands of the general interest of the public and the requirements of the protection of the individual’s fundamental rights was disturbed and the burden placed on the applicant had been excessive. The ECHR found a violation of Art.1 of Protocol No.1, which protects possession. (*Moskal-Poland*, 10373/05, Judgement 15.9.2009)

In the case *Sud Fondi SRL and Others*, three applicant companies were the owners of the land where they constructed buildings and the local authority had granted a planning permission. However, in a judgment, a criminal court held that the buildings had been built illegally. It ordered the confiscation of all the land and buildings and their transfer to the municipality. The ECHR found in the case a violation of rights for possession. First of all, the Court noted, that it is important to take into account that the applicant companies had acted in good faith and without negligence because they were granted permission from municipality. Further, the

authorities had no right for the confiscation. Hence, the ECHR stated a violation of Art.1 of Protocol No. 1. (*Sud Fondi SRL and Others – Italy*, 75909/01, Judgment 20.1.2009)

The principle of good faith appeared as a base of the decision also in the case *Köktepe – Turkey*, where the applicant acquired the land in good faith and the government violated enjoyment of peaceful possession by annullment the applicant's title to the land (*Köktepe – Turkey*, 35785/03, Judgment 22.7.2008). A similar decision was made in the case *Kalinova – Bulgaria*; based on the principle of good faith the ECHR found a violation of the Convention in deprivation of property without compensation (*Kalinova – Bulgaria*, 45116/98, Judgment 8.11.2007).

The ECHR often applies the concepts of fairness and justice which are, as it is concluded above, interrelated with the principle of good faith (See, for example, cases *Gasparini - Italy and Belgium*, 10750/03, Judgment, 12.05.2009, *Panovits – Cyprus*, 4268/04, Judgment 11.12.2008, *Yaremenko – Ukraine*, 32092/02, Judgment 12.6.2008, and many other cases). The ECHR often bases the decisions on such statements as, "...not complied with the requirement of fairness" (*Maksimov – Azerbaijan/Azerbaïdjan*, 38228/05, Judgment 8.10.2009) or, "...the requirements of fairness were met" (*Gasparini - Italy and Belgium*, 10750/03, Judgment 12.5.2009), or, "...errors such as those...would seriously affect the fairness, integrity and public reputation of judicial proceedings" (*Lenskaya – Russia*, 28730/03, Judgment 29.1.2009), "...the proceedings had been unfair" (*Gorou - Greece*, 12686/03, Judgment 14.6.2007), or, "...limitation on their right... disproportionate in relation to the aim of guaranteeing legal certainty and the proper administration of justice" (*Stagno – Belgium*, 1062/07, Judgment 7.7.2009). Compliance with the concepts of fairness and justice play a primary role in the cases of the ECHR.

It is also possible to detect from the ECHR case-law that the principle of good faith is correlated with the concepts of reasonableness (see, for example, *Svetlana Orlova – Russia*, 4487/04, Judgment 30.7.2009), lawfulness (see, for example, *Kolevi – Bulgaria/Bulgarie*, 1108/02, Judgment, 05.11.2009), and due performance of obligations (see, for example, *Menesheva – Russia*, 59261/00, Judgment 9.3.2006).

Moreover, the ECHR underlines that it is necessary to take into account national features of the law and estimate compliance with the principles of fairness, justice, and good faith based

on national-specifics (Микели де Сальвиа 2004, pp. 33-34) (See, for example, *Khamidov – Russia*, 72118/01, Judgment 15.11.2007.).

Regarding contract law, the ECHR applies provisions of the Vienna Convention of 1969, especially Art.31.1. The ECHR repeats that a treaty should be interpreted in good faith (see, for example, cases *Mamatkulov and Askarov—Turkey*, 46827/99, 46951/99, Judgment 04.02.2005, *Bosphorus Hava Yollari Turizm ve Ticaret Anonim Sirketi—Ireland*, 45036/98, Judgment 30.06.2005, *Tarariyeva—Russia*, 4353/03, Judgment 14.12.2006).

The ECHR often bases judgments on the principle of justice, fairness, reasonableness, lawfulness, and the principle of good faith. The analysis of the ECHR's case-law confirms that there is no general rule about the principle of good faith. In every case, the application is different and many facts have to be taken into account, for example, national law requirements. The ECHR applies the principle of good faith mainly in public law, however, such application has an impact on the private law area, for instance, protection of possession, and the securing of the balance of public and private interests. Often, the ECHR defines good faith as due performances of obligations; such a definition is applicable in public and in private law areas. The main conclusion of the analysis of the case-law of the ECHR is that good faith of the parties should be proven by facts; such facts are different in every case. Therefore, it is possible to say that legal presumption of good faith, which established in the legislation of some countries, should be always supported by facts and such facts should be examined by the court.

7.3. The principle of good faith in the preliminary ruling of the ECJ

The European Court of Justice (ECJ) has developed a doctrine that rules of EU law may be derived from the general principles of law in addition to treaties and EU legislation. This has been seen by some as a means by which the ECJ has effectively justified its stepping into the law-making process of the EU. In this sense, the ECJ has had quite a creative role; it has identified those principles, and with the aid of a number of EU Treaty articles, it has invoked these general principles as the legal foundation of a number of its judgments. By applying general principles of law, the Court of Justice can resolve ambiguities, fill gaps in, or even strike down EU law. Even without pronouncement by the Court of Justice, the detection of

general principles can give an indication of how EU “constitutional” law ought to be interpreted at any given moment in time. (Neuwahl 1995, p.45)

The ECJ applies the principle of good faith in public law and private law areas. In public law, the principle of good faith is deduced from the principle of justice.

There are several examples of the application of the principle of good faith, named as principle of justice, in public law. First of all, it is because of Court Justice’s case law, Article 5 of the EU Treaty of 2007, which states that, “...the Member States shall coordinate their economic policies within the Union” and, “...the Council shall adopt measures, in particular broad guidelines for these policies (Art.5 EU Treaty 2007), has developed into a key principle of justice (Vervaele 1995, p.179). The ECJ states that, “...it requires the Member States to take all measures necessary to guarantee the application and effectiveness of Community law” (Case 68/88, *European Community v. Greece*, [1989], ECR 2965). Therefore, it continues, “...whilst the choice of penalties remains within discretion of Member States, they must ensure in particular that infringements of Community law are penalized under conditions, both procedural and substantive, which are analogous to those applicable to infringements of national law of similar nature and importance and which, in any event, make the penalty effective, proportionate and dissuasive” (Case 68/88, *European Community v. Greece*, [1989], ECR 2965).

A second key principle of justice in the implementation of EU law, which has been developed by the Court of Justice, is the *effet utile* principle. It can be deduced indirectly from Article 5 of the EU Treaty. The principle means that for the effectiveness of the EU law, also in case of execution and enforcement, the EU and national administrative bodies act in such a way that the EU regulations may achieve positive effect. (Vervaele 1995, p. 183) The *effet utile* principle is applied in the *Van Gend & Loos* case (Case 26/62, *Van Gend & Loos*, [1963], ECR 0003), *Von Colson and Kamann v. Land Nordrhein Westfalen* case (Case C-14/83, *Von Colson and Kamann v. Land Nordrhein Westfalen*, [1984], ECR 1909) and *Foto-Frost* (Case 314/89, *Foto-Frost v. Hauptzollamt Lubeck-Ost*, [1987], ECR 4199), *Factortame* (Case C-213/89, *the Queen v. Secretary of State for Transport, ex parte Factortame Ltd and others*, [1990], ECR I-2433), *Emmott* (Case C-208/90, *Theresa Emmott v. Minister for Social Welfare and Attorney General*, [1992], ECR 2613), *Francovich* (Joint Cases C-6 and 9:90, *Adrea Francovich and Danila Bonifaci and others v. Italy*, [1991], ECR 5357), *Zuckerfabrik*

(Joined cases C-143/88 and C-92/89, *Zuckerfabrik Suderdithmarschen and Soest*, [1991], ECR I-534) cases.

The ECJ establishes the principle of good faith as a general principle in solving disputes between European institutions and states that, "...relations between the Member States and the Community institutions are governed by reciprocal duties to cooperate in good faith" (Case T-341/07, *Jose Maria Sison v Council of the European Union*, [2009], <<http://curia.europa.eu>>; see, also, Case C-339/00, *Ireland v Commission*, [2003], ECR I-11757).

Moreover, as the ECHR, the ECJ often refers to Article 31 of the Vienna Conventions of 23 May 1969 and underlines that, "...a treaty must be interpreted in good faith, in accordance with the ordinary meaning to be given to its terms in their context and in the light of its object and purpose" (Case C-118/07, *Commission of the European Communities v Republic of Finland*, [2009], <<http://curia.europa.eu>>). The same referencing can be found in Case C-268/99, *Jany and Others*, [2001], ECR I-8615; Case C-344/04, *IATA and ELFAA*, [2006], ECR I-403, and others.

The ECJ applies the general principle of good faith in many areas of law, for instance, taxation (Case C-566/07, *Staatssecretaris van Financiën v Stadeco BV*, [2009], <<http://curia.europa.eu>>), labour law (Case C-3/08, *Ketty Leyman v Institut national d'assurance maladie-invalidité (INAMI)*, [2009], <<http://curia.europa.eu>>), environmental law (Case C-362/06, *Markku Sahlstedt and Others v Commission of the European Communities*, [2009], <<http://curia.europa.eu>>), and other branches of law.

Regarding international trade and contract law, there are many interesting cases where the ECJ applies the principle of good faith.

The early decision of December 14th, 1976, *Galeries Segoura SPRL v Société Rahim Bonakdarian* (Case 25/76, *Galeries Segoura SPRL v Société Rahim Bonakdarian*, [1976], ECR 01851), where the dispute arose about Art.17 of the Brussels Convention, seems very remarkable. Parties of the case concluded a contract orally about purchasing carpets. The vendor performed his side of the agreement in consideration of a part-payment made by the purchaser. When handling over the batch of carpets, the vendor delivered to the purchaser a document named as "Confirmation of order and invoice", which stated that the sale and

delivery had taken place and the conditions of it are established on reverse side of the document. These conditions on the reverse side contained, among others, a provision stating that all disputes were to be decided exclusively by the Hamburg court. The document had not been confirmed by the purchaser of carpets. After the purchaser received a formal notice to pay the balance of the purchase price, the vendor began legal action and a Hamburg court ordered the purchaser to pay the balance with interest. The ECJ decided that the condition about the Hamburg court is not binding over the purchaser because, in accordance with the principle of good faith, such general conditions on the reverse side could be compulsory for the purchaser only if he would give a written agreement with the conditions, or if a continuing trading relation between parties would be such nature that it would be clear that the parties are aware about general conditions and agreed to be governed by them. However, this was not applicable for the parties' relations. (Case 25/76, *Galeries Segoura SPRL v Société Rahim Bonakdarian*, [1976], ECR 01851)

This case seems to be interesting not only because the ECJ based the decision on the principle of good faith, but also because the ECJ gave an example of the situation which would comply with the requirement of good faith (a written agreement, a continuing trading relation between parties). Such modeling gives a good explanation of how the ECJ defines the principle of good faith.

Another interesting case described by Zimmermann, in his book *Good Faith in European Contract Law*, is *Cecil v Barchester Chemicals Ltd*, also known as "courgettes perishing" (Zimmermann 2000, p. 170). In the case, Cecil, a gardener, was buying fertilizers from Barchester Chemicals Ltd for her courgettes. The fertilizers contained a large amount of salt and the plants perished when the fertilizer was put on them. It is obvious that if Cecil had given enough water for the courgettes, this would not have happened. However, the ECJ decided that, in this case, the principle of good faith was violated because the producer of the fertilizers must explain on the package that plants need rich irrigation. In this case, bad faith of the producer can be defined as providing incomplete information. (Zimmermann 2000, p. 170)

Lots of questions about good faith and its application arise in the area concerning intellectual property, especially trademarks. For instance, the judgment of the ECJ and the opinion of the Advocate General Sharpston about the case *Chocoladefabriken Lindt & Sprüngli AG v Franz Hauswirth GmbH* are about application of the principle of good faith in the process of trade

mark registration (Case C-529/07, *Chocoladefabriken Lindt & Sprüngli AG v Franz Hauswirth GmbH*, [2009], <<http://curia.europa.eu>>). For the first time, the Court was asked for guidance on the concept of bad faith within the meaning of the EU trade mark legislation. The applicant is a chocolate manufacture, Lindt, which has produced and marketed Easter chocolate bunnies since the early 1950s. Lindt registered the form and presentation of the chocolate bunnies as an EU trade mark. The defendant, Franz Hauswirth GmbH, has produced his own bunnies since 1962. There are lots of similarities in the outlook of the bunnies and, yet, some little differences. However, chocolate bunnies were produced for many decades and, since the appearance of machine wrapping, the shapes of those bunnies became increasingly similar. The ECJ was asked for a preliminary ruling about if the Lindt producer was acting in bad faith when it applied for a trade mark registration. (Case C-529/07, *Chocoladefabriken Lindt & Sprüngli AG v Franz Hauswirth GmbH*, [2009], Opinion of advocate general Sharpston <<http://curia.europa.eu>>)

The Advocate General Sharpston tried to give a definition of bad faith in the scope of European legislation. He believed that bad faith is a concept that not lawyers, but philosophers and theologians had been researching without even achieving mastery of its definition. Sharpston stated that the presence, or absence, of bad faith must be inferred from all the relevant objective circumstances. He models the situations which could be clearly defined as actions in bad or good faith. The advocate general concludes that bad faith is a subjective state – an intention incompatible with accepted standards of honest or ethical conduct – which is ascertainable from objective evidence, and which must be assessed case by case. Therefore, an intention to prevent competitors from continuing to use unregistered signs which they have hitherto been entitled to use and to defend against competition from other such signs is indicative of bad faith. (Case C-529/07, *Chocoladefabriken Lindt & Sprüngli AG v Franz Hauswirth GmbH*, [2009], Opinion of advocate general Sharpston <<http://curia.europa.eu>>)

The ECJ agreed with the opinion of the Advocate General and concluded that the national court must take into consideration all relevant factors specific to the particular case which pertained at the time of filing the application for registration of the signed EU trade mark. Specifically, the national court has to take into account such facts that the applicant knows or must know that a third party is using a similar sign or product in one of the Member States, which can possibly be confused with the sign in registration. Also, the court must take into

account the applicant's intent to prevent that third party from continuing to use such sign or product, and the degree of legal protection which the third party's sign has. (Case C-529/07, *Chocoladefabriken Lindt & Sprüngli AG v Franz Hauswirth GmbH*, [2009], <<http://curia.europa.eu>>)

As described above, the ECJ states that good and bad faith should be based on facts. A similar conclusion was made by the ECHR. The ECJ adds that all relevant factors have to be estimated at the time when the issue action was done; the ECJ and advocate general again used modeling of the situations to illustrate which actions can be defined as actions in good or bad faith. Sharpston defines bad faith as a subjective state; bad faith is an intention contrary to social standards of honest or ethical conduct that can be detected from objective evidences. Thus, as legal doctrine, the ECJ recognizes objective and subjective elements of the principle of good faith.

In other cases concerning trademarks and unfair competition, the principle of good faith also played an important role. See, for example, the case of *F.lli Graffione SNC v Ditta Fransa*, where it is stated that a prohibition to use a trade mark is possible in order to protect consumers against the misleading effect of a particular trade mark (Case 313/94, *F.lli Graffione SNC v Ditta Fransa*, [1996], ECR I-06039). Another example is the case of *Consorzio per la tutela del formaggio Gorgonzola v Käserei Champignon Hofmeister GmbH & Co. KG and Eduard Bracharz GmbH*, where the ECJ underlines the importance of the registration of the trademark in good faith and states that good faith, as a concept, must be interpreted in light of all legislation, national and international, applicable at the time when the application for registration of the trade mark was lodged. (Case-87/97, *Consorzio per la tutela del formaggio Gorgonzola v Käserei Champignon Hofmeister GmbH & Co. KG and Eduard Bracharz*, [1999], ECR I-01301)

Some judgments of the ECJ concern the doctrine of *culpa in contrahendo*.

The opinion of Advocate General Geelhoed, delivered on the 31st of January, 2002, about Case C-334/00 *Fonderie Officine Meccaniche Tacconi Spa v Heinrich Wagner Sinto Maschinenfabrik GmbH*, gives an explanation about the pre-contractual liabilities and liability to negotiate a contract in good faith. He states that, as a consequence of freedom of contract, a person is free to choose when, with whom, about what matters he wants to enter into negotiation, and the point to which he wishes to continue negotiation. However, the

freedom to stop negotiation is not absolute. Geelhoed makes a reference to the UNIDROIT principles and explanatory note, which establish a liability for losses if a party breaks negotiations in bad faith and state that the negotiation can reach a point after which it is not possible to break off without justification. Such a point depends on the extent to which the other party relies on the positive outcome and a number of issues to which the parties have already agreed. Geelhoed names three stages in negotiation. During the first stage, parties may break off negotiation without any liabilities. During the second stage, the expectations which have been created can cause harm, therefore, it is not possible to break off negotiation suddenly; it can be considered as a delict or quasi-delict and compensation for the expenses incurred can be ordered. In the third stage, there is still no contract, but it can be inferred from the circumstances that an obligation has been assumed between the parties, for instance, one of the parties has already begun performing the contract. In this case, positive contractual interest can be claimed. (Case C-334/00 *Fonderie Officine Meccaniche Tacconi Spa v Heinrich Wagner Sinto Maschinenfabrik GmbH*, Opinion of advocate general Geelhoed, [2002], <<http://curia.europa.eu>>)

In the judgment of the 17th of September, 2002, on the case *Fonderie Officine Meccaniche Tacconi Spa v Heinrich Wagner Sinto Maschinenfabrik GmbH*, the ECJ agreed with the opinion of Advocate General Geelhoed and established that, "...on the occasion of negotiations with a view to the formation of a contract and by a possible breach of rules of law, in particular the rule which requires the parties to act in good faith in such negotiations, an action founded on the pre-contractual liability of the defendant is a matter relating to tort, delict or quasi-delict" (Case C-334/00, *Fonderie Officine Meccaniche Tacconi Spa v Heinrich Wagner Sinto Maschinenfabrik GmbH*, [2002], ECR I-11757).

The ECJ underlines the importance of negotiation in good faith also in the case *TeliaSonera Finland Oyj v iMEZ Ab*, where it states that, "...a national regulatory authority may require an undertaking which does not have significant market power but which controls access to end-users to negotiate in good faith with another undertaking" (Case C-192/08, *TeliaSonera Finland Oyj v iMEZ Ab*, [2009], <<http://curia.europa.eu>>).

All of the above presented information confirms that the ECJ supports the liability to negotiate contracts in good faith. The ECJ identifies different stages in negotiation and

establishes that breach of negotiation without justification can be considered as tort, delict, or quasi-delict.

The ECJ often lets the national court decide what is fair and what is unfair; it recognizes the importance of national law and national specifics. For instance, in the case of *Pannon GSM Zrt. v Erzsébet Sustikné Győrfi*, Mrs Sustikné Győrfi entered into a subscription contract with Pannon. The contract was concluded on the basis of a form supplied by Pannon which stipulated that, by signing the contract, the consumer acknowledged the applicable terms and conditions, including the general contractual conditions forming an integral part of the contract and accepted their content. The dispute arose about the jurisdiction, which was established in these general conditions. The place of the proceedings was inconvenient for the consumer due to the lack of transportation. The ECJ was asked to give a preliminary ruling about the possibility to consider such provisions as unfair. (Case C-243/08, *Pannon GSM Zrt. v Erzsébet Sustikné Győrfi*, [2009], <<http://curia.europa.eu>>)

The ECJ stated the importance of the protection of consumer and explained that the system of protection is based on the idea that the consumer is in a weak position vis-à-vis the seller or supplier, in regards to both his bargaining power and his level of knowledge. Therefore, the consumer agrees to terms drawn up in advance by the seller or supplier without being able to influence the content of those terms. Thus, an unfair contract term is not binding on the consumer and it is not necessary, in that regard, for that consumer to have successfully contested the validity of such a term beforehand. The ECJ also states that in referring to concepts of good faith and significant imbalance between the rights and obligations of the parties, European legislation merely defines, in a general way, the factors that render unfair a contractual term that has not been individually negotiated. The Directive on unfair contract terms contains only an indicative and non-exhaustive list of terms which may be regarded as unfair. Therefore, the Court concluded that it is for the national court to assess whether a contractual term may be considered as unfair. It continued that the national court has to take into account the fact that a term contained in a contract concluded between a consumer and a seller/supplier, without being individually negotiated and which establishes exclusive jurisdiction on the court in the territorial jurisdiction of the seller/supplier, may be considered to be unfair. (Case C-243/08, *Pannon GSM Zrt. v Erzsébet Sustikné Győrfi*, [2009], <<http://curia.europa.eu>>)

The same decision was made on the case *Freiburger Kommunalbauten*, where the Court stated that, "...it is for the national court to decide whether a contractual term ...satisfies the requirements for it to be regarded as unfair" (Case C-237/02 *Freiburger Kommunalbauten* [2004], ECR I-3403).

The Court's judgments also concern unfair advertising. The Court has developed the concept of "responsible consumer" in order to strike down national rules that pretend to protect the consumer but, in reality, serve protectionist devices. (Micklitz 1995, p. 273) For instance, the ECJ has focused on misleading advertising, which has raised considerable concern mainly in the Federal Republic of Germany. In the case of *Procureur de la Republique v X* (Case C-373/90, *Procureur de la Republique v X*, [1992], ECR I-00131), parallel importers have advertised the lower price of their cars without mentioning that the technical equipment was less complete than in ordinary cars bought through the official chain of authorized dealers. The Court of Justice found no misleading effect but the German Bundesgerichtshof took the opposite view. (Micklitz 1995, p. 287) This concept of misleading pricing appeared also in the case *Schutzverband gegen das Unwesen in der Wirtschaft v. Yves Rocher* (Case C-126/91, *Schutzverband gegen das Unwesen in der Wirtschaft v. Yves Rocher*, [1993], ECR I-02361) and *Verein gegen Unwesen in Handel und Gewerbe Köln e.V. v Mars GmbH* (Case-470/93, *Verein gegen Unwesen in Handel und Gewerbe Köln e.V. v Mars GmbH*, [1995], ECR I-01923). Although the Court does not decide on the merit of the case, it develops abstract rules; and in unfair advertising, the rule is that only the responsible consumer needs protection. Micklitz states that this is the power of objective rationality. The Court, in limiting the Member States' freedom to shape consumer protection and social welfarism, imposes a duty on the Member States to take only the necessary measures. Objective rationality and good faith requires protection where it is needed. (Micklitz 1995, p. 274-287)

After analyzing all the cases presented above, it is possible to state that the ECJ invoked the general principles of law as a legal foundation of a number of its judgments and applied the general principles to resolve ambiguities and fill in gaps. The principle of good faith is one of the general principles which is applied by the court in public and private law areas. In public law, the principle of good faith is the element of the principle of justice. The ECJ established that EU law should be exercised by Member States in the most effective and just way; the penalties should be proportionate and dissuasive. As it stated by the ECJ, all relations between European institutions and Member States should be governed by the duty to

cooperate in good faith and the treaties should be interpreted in good faith. The ECJ applies the principle of good faith in all areas of law, such as taxation, labour law, environmental law, intellectual property, and others. Often, the ECJ applies the principle of good faith to solve the disputes arising in international trade and contract law. Firstly, when the Court is making the decision based on the principle of good faith, it assesses the current situation and the opinions of parties about it; in other words, it assesses all relevant facts. Secondly, it analyzes objective factors, such as usual business practices, usage of trade, and duration of business relations. Moreover, the ECJ takes into account national specifics and specifics of the particular contractual relations. After an analysis, the ECJ defines to which degree the principle of good faith was violated by modeling situations that are contrary to the requirements of good faith, or the ideal situation, which satisfies all requirements of the principle of good faith. Based on the degree to which the principle of good faith was violated, the ECJ defines liabilities and penalties. The ECJ detects exact provisions of the contract, which are contrary to the principle of good faith or unfair. The ECJ establishes the duty to negotiate in good faith and identifies different stages of negotiation. Depending on the stage where the negotiation was broken, the ECJ assesses the degree of violation of the principle of good faith. However, the ECJ underlines that the principle of good faith requires protection only where it is necessary; therefore, it developed the rule that only the responsible consumer needs protection.

As in the legal doctrine described in the first part of this research, the ECJ recognizes objective and subjective elements of the principle of good faith and states that bad faith is a subjective intention that is incompatible with social standards of honest or ethical conduct, which can be detected from objective evidences.

To conclude, the ECJ recognizes the importance of the principle of good faith in contractual relations and in international trade. The principle of good faith in contract law is deduced from the general principle of good faith and the principle of justice, which governs all relations between the Member States, European institutions, legal bodies, and individuals.

8. CONCLUSIONS

After collecting and analyzing information from different sources, such as doctrine, legislation, and legal practices concerning the principle of good faith, it is possible to draw the following conclusions.

The general principles of law are the most fundamental guidelines, the transcendent elements of natural law, which govern regulation over all types of legal relations and appear as the primary source of law. Long historical development of the principles foregoes the establishment of the general principles in the law. It began from the formation of the subjective position of the individual on behavior in society; such position arose from ethical and moral norms. Such social norms became a rule of behavior, a regular practice, and, in other words, a law of nature. This law of nature is a “deep structure of law” according to Tuori’s theory, which was discussed in the first part of this research. Through an analysis made by legal scientists and a long duration of the application of the rule, such norms find their place in the legal acts of different legal systems. They can be directly established in the law and can be deduced from other legal norms. Moreover, these principles can exist as regular business practices and the violation of them can be liable to punishment. The general principles can also exist in the courts’ legal practices and be a base for court judgments. The final stage of the development of such a rule is the transformation of it to the general principle of international law by establishing it in supranational agreements and treaties.

Based on the process of development of the general principles, it is possible to deduce specific features of the principles. The general principles, which exist as common practices, are very stable. They never violate human rights because they appear as a natural law. The application of the general principles does not depend on a sanction of the state since the norm is essential for human beings. Moreover, the general principles are protected by law and by ethical conduct of behavior, so that, if the principle is violated, there will be not only legal punishment but also moral disapproval.

The importance of the general principles is recognized at national, European, and international levels. They can be found in a number of international treaties and the EU Treaty underlines the significance of the general principles as they are developed and applied by the ECHR and the ECJ.

The principle of good faith is one of the general principles and a universally recognized legal norm that regulates legal relations in public and in private law areas. It also determines the rights and duties of parties. The principle of good faith appears as a moral principle of mutual trust, honesty, and fairness — basic rules without which the order of society would be impossible. By being transmitted to legislation, the moral principle of good faith became a legal principle and exists nowadays in both dimensions. The principle of good faith is closely interrelated with the principle of justice in the legal doctrine, courts' judgments, and legislation. The principle of good faith can be an element of the principle of justice, or in some cases, the principle of justice and principle of good faith are intrinsically the same principles. The concepts of rationality and reasonableness are also tightly connected with the principle of good faith, therefore, the concept of “reasonable consumer” and “rational person”, which acts in good faith, have been developed, as well as other concepts such as “reasonable time”, “reasonable expectations”, and “reasonable care”.

In private law relationships, the principle of good faith establishes that negotiation, formation, and performance of the contract shall not violate the rights and duties of other parties and third persons. Legal provisions, which prohibit fraud, dishonesty, misrepresentation, duress, usage of dependant position or hardship, unilateral rejection of performance, disclosure of confidential information are based on the principle of good faith. The violation of law, regulation, public policy, and ethical norms are also prohibited by the principle of good faith. Good faith of the parties should be estimated in every particular contract and at the point of agreement because every case is unique and the content of good faith will be always different.

It is possible to define two elements of the principle of good faith: subjective and objective. The subjective element is internal requirements, which can be deducted from the legal norm. Subjective elements are directly related to the actions of the individual, which must comply with such categories as truthfulness, honesty, respect for the rights, and loyalty to contract obligations. Moreover, the individual should have an understanding of the consequences of their own actions, the commensurability of own interests with the interests of other parties and third persons, and eliminate the damages to the others. The subjective element shows that an individual has a psychological position and internal understanding of the liability to behave in a certain way. Subjective elements of good faith should be detected from facts and evidences of the each case. The objective element of the principle of good faith is the

requirements, which are established in certain legal norms and sometimes in moral and ethical norms. The roots of the objective elements are in the concepts of rationality and social justice. Therefore, if the contract contains provisions which are contrary to such norm, they will be invalid.

The principle of good faith has a long historical development and evolution. Beginning from Roman law to the present moment, the principle of good faith has been continuously improved in its legal application in different legal systems. Now, the principle of good faith appears as *Treu und Glauben* in German law, where, after long historical development, the principle has a very wide scope of application; it covers pre-contractual, contractual, and post-contractual situations, and is used as a remedy for the gaps in legislation. In Germany, the famous doctrine of *culpa in contrahendo* was developed which recognizes the duty of good faith in a negotiation process. *Bonne foi* was established in French law, and now it is applied to the pre-contractual situations, performance of the contract, and is considered as an element of the duty of cooperation. *Buona fede* appeared in Italian law and presents an autonomous basis for a legal action. Also, *vilpitön mieli* was established in Finnish law, *добросовестность* in Russian law, and the concept of “reasonableness and fairness” appeared in Dutch law. The principle of good faith was declared as a constitutional principle in Estonian law and the requirement to act in good faith is considered as most important within private law rulings through which constitutional values exist in the law of obligations. The concept of “good faith and fair dealing” exists in common law countries and courts offer protection of the good faith duties; however, there is no general obligation to act in good faith.

In the present time, the principle of good faith has an important place in national legal systems and particularly in contract law. The formation of the content of the principle was influenced by different factors, such as moral and ethical values, national specifics, and religious convictions. Therefore, there are differences and similarities in the understanding and application of the principle of good faith at the present time. The common approaches to the content and application of the principle of good faith are the following. First, the principle of good faith is recognized in all European countries which were considered in the research. Secondly, wide judicial discretion forms the legal practices concerning the principle because the principle of good faith is such a norm, which cannot be applied without appropriate explanations and specifications. Legal norms only establish the general way of appropriate

behavior and courts give assessment for all circumstances of the particular case by estimating the degree of violation of legal norms. Third, courts can use different methods and punishments depending on the degree of violation of the principle of good faith. For instance, the obstacle to perform the contract can be eliminated, the contract can be modified totally, or in parts, the contract can be annulled.

The biggest differences in the approaches to the principles of good faith arise because national courts apply national legal norms, which have differences in the scope of application of the principle of good faith, the content of the principle of good faith, its elements, and its requirements. Moreover, in some legal systems, for example Russia, the principle of good faith is not established as a general principle of law, principle of contract law, or law of obligations. In common law countries, the application of the principles is also an issue and the principle is considered by some legal scientists as a “legal transplant”, which is not natural for the English law.

At the present time, the principle of good faith is a universally accepted legal norm in international law and in the law of the European Union. It is established in many international treaties, such as the Charter of United Nations, the Declaration on Principles of International Law concerning Friendly Relations and Cooperation among States of 1970, the Vienna Convention on the Law of Treaties of 1969, and others. Good faith is a core value of all international relations between public and private parties, including relations between states, institutions, legal persons, and individuals. In public law, the principle of good faith is a base for the performance of international obligations and treaties, and closely interconnected with the principle of estoppels and the principle of reciprocity. The principle of good faith also requires that all treaties should be interpreted in good faith.

In the law of the European Union, the principle of good faith is established in a number of Directives, such as the Directive on Unfair Contract Terms of 1993, the Directive on Commercial Agents of 1986, the Money Laundering Directive of 1991, the Consumer Credit Directive of 1987, and the Unfair Commercial Practice Directive of 2005. The Directives state that behavior in good faith includes the duty to inform, to disclose information, the duty of due care, and the duty of professional diligence. The Directive on Unfair Contract Terms and Unfair Commercial Practice Directive contains, in the annexes, the lists of situations that can be considered as actions in bad faith or are unfair actions.

In conjunction with globalization processes, there is tendency of unification and codification of international contract law and legal practices. The Vienna Convention of 1980 and the UNIDROIT Principles of 2004 present international general rules about contract and sales law. In European law, contract law is codified in the Principles of European Contract Law of 2002. The Vienna Convention of 1980, the UNIDROIT Principles, and the Principles of European Contract Law establish the principle of good faith as a general principle and provide protection of good faith in all stages of contractual relations. The Vienna Convention determined an abstract rule of good faith, while the UNIDROIT Principles and PECL regulate the use of the principle and its subject in details. In legal practices, all three legal acts can be used simultaneously, mutually supplementing each other.

In the UNIDROIT Principles, the principle of good faith is established as a mandatory provision. The requirements of good faith include liability for breaking the negotiation without justification, due performance of written and unwritten obligations, cooperation, the duty not to disclose confidential information, and the duty to inform about errors. The principle of good faith prohibits the inclusion of unexpected clauses in standard terms, fraudulent representation, and non-disclosure. It requires the elimination of gross disparity, possibility of partial and earlier performance if it does not cause any harm for the party, possibility of renegotiation, and the duty to mitigate harm.

In the Principles of European Contract Law of 2002, the principle of good faith is also established as a mandatory duty and appears in many provisions. The requirements of good faith are similar to the UNIDROIT Principles; the parties should follow reasonable standards of honest behavior towards each other and have an obligation to comply with the requirements of good faith when exercising contractual rights and fulfilling contractual duties. In addition, a party has to present evidence of appropriate behavior, if for example, there were changes in a situation or unexpected events occur. Moreover, the PECL establishes that the principle of good faith prohibits intentional harm, gross negligence, gain of profit from own unlawful actions, and all kind of threats.

However, despite the existence of the principle of good faith in many clauses in legislation, in any of European or international legal acts, the definition for the principle of good faith was not given; the content of the principle is explained in the provisions prohibiting or requiring some actions and examples of behavior in good and bad faith.

As it was mentioned above, the ECHR and the ECJ have an important role in developing the general principles. The courts use the general principles to fill gaps in the legislation and to make a decision in ambiguous and difficult cases. As it is defined by Dworkin, there is fair solution for most of the cases (Ratio 2000, p.31). Therefore, the principles of justice, fairness, and reasonableness are the key principles in legal practices of the ECHR, and the principle of good faith often appears as an element of those principles. The ECHR, in its judgments, made very important conclusions. First of all, the ECHR determined that good faith should always be based on facts which can be found in the circumstances of a case and examined by the court. Second, the ECHR emphasized the importance of national features to estimate compliance with the general principles and, among others, the principle of good faith. Third, the court defined good faith as due performance of obligations. The ECHR applied the principle of good faith in different situations, such as the protection of possession, securing of balance of interests, interpretation of treaties, and others.

The ECJ has a priority position to define the content and the application of the principle of good faith in disputes arising in European countries. By analyzing the judgments, it is possible to conclude that the ECJ recognizes the principle of good faith as a general principle of law of the European Union and general principle of European contract law. Compared to treaty provisions and national legislation, the ECJ has some specific points regarding the principle of good faith. Just like the ECHR, the Court deduced the principle of good faith from the principle of justice, which requires a fair application of EU law, proportionate penalties, and achievement of positive effect of application of European legislation. The ECJ applied the principle of good faith in different areas of law, among others, labour law, taxation, environmental law, and intellectual property law. A number of preliminary rulings of the ECJ, where the principle of good faith was applied, concerns international trade. The ECJ determined that, in accordance with the requirements of good faith, conditions about jurisdiction should be individually negotiated, and the producer should provide accurate and complete information about the product. Moreover, the ECJ establishes that a trade mark should have no misleading effect, certain stages within negotiations should not be broken without justified reasons, and that weak parties should be protected. Also, the ECJ underlines the importance of business practices, duration of business relations, and national specifics in application of the principle of good faith and fairness. To define the circumstances in which a case must comply with the requirements of good faith, the ECJ analyses all relevant facts and

uses modeling of ideal situations, or situations which are contrary to good faith. However, in its judgments, the ECJ states that the principle of good faith should be protected only where it is needed and based on the standards of rationality.

The definition of the principle of good faith in international trade which reflects the common core of understanding of the principle can be given as follows. The principle of good faith is generally recognized and universally binding within legal provision regulating relations between all legal and natural persons in public and private law areas. It is closely interrelated with ethical norms, norms of morality, and such categories as justice, reasonableness, and equity. In private law and international trade, the principle of good faith prohibits negotiation without purpose to conclude a contract, fraud, duress, misrepresentation, use of undue influence and hardship, disclosure of confidential information, dishonest business practices, and violation of compulsory provisions of legislation and moral principles. The behavior of good faith must have such features as truthfulness, due care, cooperativeness, performance of written and unwritten obligations, the duty to inform about the error, mitigation of harm, respect to other's rights, and loyalty to the own duties. Good faith should be always provable by objective facts.

The presented research is one of the steps in the process of the integration and harmonization of European contract law. It is approved by legal scientists and researchers that the principle of good faith should be one of the unifying elements of European contract law and the law of international trade. This work supports the process of rapprochement between European and Russian law. Therefore, the research can be used as a base for the propositions of future regulatory developments in Russia. First of all, there should be changes in the Russian Civil Code, particularly, in Article 1 where the principle of good faith should be established as a general principle of civil law. Second, the principle of good faith should be applied in legal practices of Russian courts when there is no legal norm, which protects fairness and justice in the particular case. Fourth, the legal presumption of good faith should be always provable by objective facts. Third, Russian legal doctrine should support the application of the principle of good faith by developing an appropriate scientific base for evaluation.

This research presents a sufficient study about understanding the principle of good faith in the European countries: in the legal doctrine, national legislation, and the judgments of the European Court of Human Rights and the European Court of Justice. Due to the limited size

of the research and the lack of knowledge in many European languages, the decisions of the national courts concerning the principle of good faith were studied only from secondary sources. The analysis could be widened by including the detailed consideration of legal practices of national courts of all the other European countries.

Moreover, there are many topics for further research of the principle of good faith and other general principles. For instance, it would be interesting to study the influence of the practices of European courts concerning the principle of good faith and other general principles to national legislation and national courts judgments. Also, it would be beneficial to study changes in national legislation concerning the principle of good faith and the influence of such changes, especially interesting would be the alteration and adaptation of the principle of good faith in common law countries, and in Russian law, due to the regulatory developments. Lastly, other general principles can be researched in light of the judgments of the ECJ and the ECHR, for instance, the principle of reciprocity, the principle of estoppels, and others.