

GOOD-FAITH IN CONTRACTS

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Abstract: *This article will outline only the new aspects in the matter, namely the legal regulation of the negotiation stage in reaching an agreement, as well as the inherent consequences deriving from such regulation, namely the need of observing good faith in negotiations and the obligation of covering the damage caused by sudden breaking off of negotiations. At the same time, the article gives some terminological explanations for the concept of good faith, which is widely used both in substantive law and in procedural law.*

Key words: *good faith, negotiations, breaking negotiations.*

1. Introductory reflections

1.1. The concept of good faith

One of the basic principles for any approach on the effects of contracts is the principle of good faith, which is very natural and reasonable, but also very complicated, due to the problems of application regarding compliance or non-compliance with it. In fact, we must say right from the start that, although it has been regulated for more than 160 years by our laws and although it had been an essential principle of the relationships among merchants before the Old Civil Code was adopted, although all international commercial relations are based on it, unfortunately, its putting into practice is sometimes rather hypothetical.

Both parties and legal courts ignore it, even though both know it well, observe its content – only theoretically – but many times refuse to refer to it more concretely

when it comes to failure of fulfilling obligations.

Good faith has been defined in different manners over the years, both in doctrine and in case law. However, we note the definition given by the Explanatory Dictionary of the Romanian language (DEX), as, in our opinion, it is quite clear and represents the basis for all the definitions that have been formulated so far: good faith (synonymous, according to DEX, to honesty and sincerity) represents one's belief that one acts based on a right and in compliance with the law or with what is right.

Fortunately, our new civil code adds to it the attitude of a natural or legal person exercising their rights and fulfilling their obligations in accordance with public order and good manners.

1.2. Current legal regulation

The principle of contract good faith is

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regulated expressly and unequivocally by the provisions of the New Civil Code, which actually repeat, more rigorously though (and by adding new elements), the old regulations of the Civil Code of 1864.

To strengthen its importance, the current civil code uses the same formulation elements (in addition to the principle expressly defined before any approach to obligations) every time when the question arises regarding the manner in which obligations are fulfilled and, furthermore, where applicable, deals with any equivocal matter based on the good faith of obligation fulfillment.

The main rule in defining the principle under discussion herein is very categorical, the legal regulation being asserted as an imperative (as opposed to superlative) legal norm: „The parties shall act in good faith both in negotiating and in concluding the contract, and during the entire period of its performance. They cannot replace or restrict this obligation” (art. 1.170 the New Civil Code, which recurs to and develops the provisions of art. 970 of the Old Civil Code).

Therefore, it is certain that, according to the new legal provisions (apparently inspired by art. 1.375 C.C.Q.), good faith must exist in three distinct moments: upon negotiating the contract, upon concluding (signing) the contract and, lastly, during the performance of the contract. In any of these stages the parties' obligation of acting in good faith cannot be overseen.

On the other hand, good-faith is also regulated by the New Civil Procedure Code, as the procedural legal norm establishes the judges' right of taking into consideration the disputing parties good faith, among others [1].

1.3. Necessary terminological definitions

The definitions required herein refer to the need of a correct understanding of some concepts related to the broader meaning of ”good faith”, which is used in law. Exhaustively, in private law this means the principle of good faith, the principle of protecting right acquisition in good faith, contract good faith and the exercise of procedural right in good faith. These concepts are distinct, but naturally, they are related.

Therefore, above all, it is important to clarify the concept of good faith as a general law principle (good faith in general), a concept that is mentioned even in the first preliminary heading of the New Civil Code, the principle being regulated for any general rights and obligations irrespective of whether or not they arise from a contractual relationship. For this purpose, it is to be noted that any natural or legal person shall exercise their rights and fulfill their obligations in good faith, observing public order and good manners (art. 14 New Civil Code).

Furthermore, no right can be exercised for the purpose of injuring or damaging another party or in an excessive or unreasonable manner, in contradiction with good faith (art. 15 New Civil Code regulating expressly abusive exercise of rights). As in the old regulation, the good faith is presumed until the contrary is proven – *bona fides presumitur*. This is a significant presumption, because the individual intending to and interested in claiming bad faith towards another individual shall prove such attitude unequivocally; in other words, it is not the party to whom bad faith was claimed that shall prove their innocence, but the party claiming the lack of good faith that shall prove the guilt. This rule is similar to the

in dubio pro reo rule of criminal law, but we note that in criminal law the good faith presumption applies (at least theoretically) fully, which is not the same in civil law, where such principle has significant peculiarities. Thus, in terms of tort liability (which is not dealt with here) the good faith presumption applies very rigorously. On the other hand, in contract law, although the good faith principle applies, to be more specific the obligation of the contracting parties to exercise their rights and fulfill their obligations in good faith, the legal good faith presumption does not apply; the civil code establishes another presumption, namely the presumption of guilt (fault) for the party failing to fulfill their duty.

As part of the basic principle of observing good faith in general, two components are to be retained in substantive law, namely:

- the principle of protecting good faith in acquiring rights, which is the subject matter of rights in rem [2] ;
- the principle of contract good faith, which is the subject matter of the theory on duties, under discussion herein.

Finally, as shown above, good faith also applies in procedural law and it is the subject matter of such law and it refers to the exercise of procedural rights in good faith.

What interests us here is the contract good faith, while the other aspects of good faith will be dealt with later.

2. Content of contract good faith

2.1. Loyalty, cooperation, confidentiality

The good faith as a basic principle guiding (or that should guide) any individual when entering into a contract consists of three essential elements: duty of

loyalty, duty of cooperation and the duty of confidentiality.

The duty of loyalty (which is not regulated by law, but which is invariably mentioned in foreign case law) requires that the contracting parties show honestly and sincerely their intention or goal in concluding the contract or their goal in proposing the negotiation of the contract; such obligation requires, at the same time, that the contracting parties fulfill their duties fairly, with no hidden intentions, that is without intending to cause damage to the other party.

The French judicial practice has sanctioned the breach of such obligation in insurance contracts (where the insured must answer honestly the questions asked by the insurer upon the conclusion of the insurance policy [3], and the insurer must be loyal, namely such insurer may not wait or cause the statute of limitations for the right of the insured to claim the payment of insurance benefits [4]), in loan contracts (where banks' lack of good faith has been found, namely the postponement of the deadline of enforcement on the debtor for the purpose of debts accrual [5]), in work contracts (where employers are considered to violate their duty of loyalty when, for example, they breach a mobility clause or when they hire an individual from outside the company on a position for which an employee was specialising [6]), in guarantee or suretyship contracts (where creditors failing to inform their warrantors about the debtors' difficulties so that the former can act for the purpose of alleviating their duties are deemed to have acted in bad faith [7]), mandates[8] or in purchase contracts (where the seller shall not deceive the customer using vague and confusing advertisements [9]).

The duty of cooperation (which is not regulated by the New Civil Code, but

which is mentioned by the Principles of European Contract Law) requires that the parties actually cooperate in view of a good contract performance, namely they shall do their best that their duties under contract be fulfilled to their value or extent. For this purpose, the text of art. 1:202: PECL, called "Duty to Co-operate" is relevant: "Each party owes to the other a duty to co-operate in order to give full effect to the contract. According to the French case law, breach of this duty has been found in work contracts (meaning that the employer has the obligation of having the salary adjusted to the employee's progress [10]) or in bank contracts (where, for instance, a bank is believed to have failed in fulfilling its duties of cooperation if such bank has not used all legal means to avoid the fraudulent use of a bank card [11]).

Finally, the duty of confidentiality, the third element of contract good faith (especially good faith in negotiations) is expressly stipulated by art. 1.184 of the New Civil Code. According to this duty, the parties shall keep confidentiality over the information and shall not use for their own purposes the confidential information they have become aware of during negotiations. It is important to remember that the duty of confidentiality is implied even if the negotiations do not lead to the conclusion of a contract. Breach of the duty of confidentiality causes the liability of the party at fault, and such liability may be quantified, according to PECL Principles, as the actual losses incurred and the benefits acquired by the other party [12].

2.2. Good faith in negotiations

If we have been aware for a long time of the good faith that should exist when

concluding a contract and during its performance (due to the old regulation included in the former civil code, as well as due to the reports of international private law), a brand new element is the duty of observing good-faith during the negotiation of the contract. It is a novelty mainly because the stage of contract negotiation itself in the history of an agreement is completely unheard of in our domestic laws, but also because *expressis verbis*, the law deals with good faith during negotiations. Art. 1.183 of the New Civil Code is very eloquent in this case, it regulates expressly the stage of negotiation as a stage in itself when entering into a contract, starting with the good faith of such negotiations.

Consequently, the good faith in negotiations is an essential principle, so the parties cannot agree upon its limitation or removal. In the French case law, the legal courts have gone farther and frequently ordered that the good faith in performing a contract and, more specifically, the good faith in negotiations, requires the parties to observe another duty, namely the duty of renegotiating the contract when applicable [13].

In terms of sanctions, as a rule, we note that the commencing of negotiations or their termination contrary to good faith shall be sanctioned by having the party pay damages, generally accounting for the expenses incurred for negotiation and any other losses consequential to the other party's declination of similar offers. However, it is important to notice that the law takes for granted the parties' presumed right of breaking off negotiations without being held liable for their failure [14].

What is the difference from the former regulation? In the old civil code, the negotiations could be terminated without delay and at any time; as long as the

contract had not been concluded, either party could change their mind, even if the parties were in an advanced stage of the negotiation, which, many times, would be reached after a long time and with significant costs. Obviously, by virtue of the new civil code, such situation is no longer possible without the duty of paying damages.

Certainly, the problem here, before any other discussion, is to define the cases of termination of negotiations in order to be able to determine beyond any doubt the situations where the breaking off was made in bad faith (and, in such case, it is noted that the law refers to termination circumstances that go against good faith and are not in bad faith, a slight difference, which, we believe, bears consequences, as it is easier to prove the violation of good faith rules than to prove bad faith, in other words, one does not have to prove the worst or most serious intention [15]).

Then, one may ask this question: has one party terminated negotiations because they have found better business or because they have realized that the business under negotiations was no longer profitable? Or the party may have terminated negotiations because their partner was no longer trustworthy or because such partner did not bring satisfactory guarantees? These are the questions that may be asked in such a case and, most importantly, it remains to be determined whether any of these situations is present when breaking off negotiations contrary to good faith.

Fortunately, it shall be noted that the underlying principle is that the parties cannot be held liable for the failure of negotiations. On the other hand, the law mentions only one circumstance in which the negotiations are deemed to have been terminated contrary to good faith, namely the behaviour of the party initiating or

continuing negotiations with no intention of concluding the contract [16]. The other circumstances are to be defined by judges.

Notes

1. Art. 22 Par. 7 NCPC. For more details about good faith and, especially, the good faith in civil procedural law, please consult, A. Ciurea - „Despre teoria *estoppel* sau noi instrumente de filtrare a acțiunilor în justiție” (*On estoppel theory and new filtering instruments of legal action*). In: *Revista română de drept privat* nr.4/2012, Universul Juridic publishing house, page 53.
2. In simulation of marriage contract (art. 331 NCC), in the case of the drawing up of legal documents by a spouse without the consent of the other spouse (art. 345), in non-natural estate accession (art. 581-594), in acquisitive prescription (art. 930-934) and in good faith possession of movable assets (art. 935-940), etc.
3. Civ. 1, 28 mars 2000, Bull. Civ. I, no 101, R, page 406, D 2000. 574 in Code Civil, Edition Dalloz 2012, , page 978.
4. *Idem*, Civ. 1, 26 nov. 1996 Bull. Civ. I, no 415.
5. *Idem.*, Civ. 1, 31 janv. 1995, Bull. Civ. I, no. 57.
6. *Idem*, Soc. 18 mai 1999, D 2000, Somm. 84; Soc. 7 avr. 2004 D 2004 IR 1352). For this purpose, please see the other resolutions mentioned in op. cit, page 978.
7. *Idem*, Com. 31 mai 1994, RJDA 1994 no 1129, page 871), page 979 and other similar resolutions cited in the work..
8. It is illustrated by a mandate contract where the principal entrusted the attorney-in-fact the performance of business activities, but the former did not allow the latter to have prices comparable with those of competitors (*idem*, Com., 24 nov. 1998, Bull. Civ. 4, no 227, page 979); in such case, the

- principal was deemed to have acted in breach of the duty of loyalty.
9. *Idem*, Paris, 18 juin 1999 : JCP 2000. II. 10322, page 979.
 10. *Idem*, Soc. 25 fevr. 1992, D 1992. 390.
 11. *Idem*, Com. 20 oct. 1998, Bull. Civ. 4 no. 244, R p 242, JCPE 1999. 1101.
 12. Art. 2:302 PECL; our *highlights*.
 13. Com., 3 nov 1992, JCP 1993, II, 22164 p 64, Code Civil, Ed. Dalloz, page 64.
 14. The resolution complies with the provisions of art. 2:301: "*Negotiations Contrary To Good Faith*" of PECL Principles.
 15. The French case law itself, which we have quoted above and which has numerous resolutions passed for cases of breach of good faith in negotiations, does not use the concept of *bad faith*, but the more legally accurate and rigorous phrasing, in our opinion, of *breach of the duty of good faith* ("*manque a son obligation de bonne-foi*").
 16. We are not surprised to notice that this new regulation in our new civil code stems from art. 2:301, par. 3 PECL.