GOOD FAITH AND FAIR DEALING
IN THE COMMERCIAL CONTRACT LAW

Viktorija Budreckienė

Mykolas Romeris University, Lithuania
viktorija.budreckiene@gmail.com

Abstract

Purpose – to analyze the commercial concept of good faith and fair dealing applicable in the UNIDROIT Principles of International Commercial Contracts, Draft Common Frame of Reference and Lithuanian commercial contract law.

Methodology – theoretical methods (analytic and systematic) had been applied in the research.

Findings – the author of the article concludes that the substantive content of good faith and fair dealing notion applied in Lithuanian commercial contract law should be specified taking into regard the peculiarities of business relations. What is more, the question, whether a businessman acted in good faith, should be answered with respect to common business practice of particular trade.

The case law of Lithuania also recognizes the peculiarities of commercial good faith and fair dealing notion. What is more, when determining if a businessman acted in good faith, courts also mention common commercial practice. However, it is doubted that courts really take this criteria into account and it can be guessed that often the application of this standard is limited only to mentioning. Due to application of common business practice criteria the content of good faith and fair dealing principle is even harder to unfold, especially, as it can be very difficult to prove the existence of such practice. Yet this is the problem not only of the court, but also the parties of the civil dispute, as the presentation of reasonable arguments and proofs is their right and obligation.

Research limitations/implications – the research has been limited to the analysis of commercial good faith and fair dealing doctrine in Lithuanian contract law, UNIDROIT Principles of International Commercial Contracts and Draft Common Frame of Reference.

Practical implications – the findings of the research can be applied by judges invoking good faith and fair dealing doctrine in commercial disputes, as well, by businessman determining the limits of their contractual freedom.

Originality/Value – A. Norkūnas, R. Balčikonis, S. Drazdauskas, A. Jakaitė, S. Arlauskas, R. Jakūbauskas, S. Cirtautienė and some other authors have analyzed particular aspects of general good faith and fair dealing principle in Lithuanian private law. Although these publications are important to this research in some particular aspects, the peculiarities of this notion applied precisely in Lithuanian commercial contract law have not been discussed. Taking into consideration the absence of legal doctrine in Lithuanian Republic the research is new and original. What is more, considering the importance of the stability of commercial turnover and
predictability of outcomes of possible disputes the research may be in particular valuable not only for scholars, but also for practitioners and businessmen.

**Keywords:** good faith and fair dealing, common business practice, businessmen.

**Research type:** general review.

**Introduction**

Good faith and fair dealing is a widely recognized value of private law\(^1\). Lithuanian legal system is no different: this principle is clearly established in Lithuanian Civil Code\(^2\) (hereinafter referred to as the CC)\(^3\) and often cited in the case law. However, the question has to be raised, whether the principle of good faith and fair dealing has the same meaning in general contract law and commercial contractual relations. Is a party to a contract – a businessman - acting in good faith\(^4\) seen the same as any other person contracting without business purposes? Maybe it should be admitted that the modern private law is based more on social values and shares one general concept of good faith and fair dealing? This could seem reasonable, if we admit that this principle is a moral value shared by every member of society. On the other hand, there is no doubt that commercial contractual relationships have their specifics and rules of general contract law may not always be applicable to it. Especially, when a certain rule is designed to protect the weaker party to the contract and its application in business relationship may not only be problematic, but also unreasonable.

The general concept of good faith and fair dealing has been analyzed by many scholars in Lithuania\(^5\). We should separately mention the article of A. Jakaitė\(^6\), as well,

---

\(^1\) Of course, this recognition has exceptions.


\(^3\) For example, the Article 6.158 of CC „Good faith and fair dealing“ states:

> 1. Each party of a contract shall be obliged to act in accordance with good faith in their contractual relationships.

> 2. The parties may not change or exclude by their agreement the duty established in Paragraph 1 of this Article*.

\(^4\) For the purposes of this article the term “good faith” shall have the same meaning as “good faith and fair dealing”, except in case it is clearly expressed otherwise and these two notions are compared or analyzed as separate criteria.


\(^6\) Although the research of A. Jakaitė is limited to the analysis of the general principle of good faith in pre-contractual relations with no particular emphasis on the specifics of commercial relations, examples of Lithuanian and foreign case law provided in the article are certainly relevant for this research. Jakaitė, A. 2011. Sąžiningumo imperatyvas įkisutartiniuose santykiuose: turinys ir taikymo problematika. TEISĖ, (79), 76-91.
recent article of S. Arlauskas and R. Jakūbauskas. Although these publications are important to this research in some particular aspects, good faith and fair dealing is mostly discussed with no emphasis on the peculiarity of commercial contractual law - rights and obligations inherent to business relationships.

Taking into the account the limited scope of this article, the author shall analyze commercial concept of good faith adopted in UNIDROIT Principles of International Commercial Contracts (hereinafter referred to as the UNIDROIT Principles)\(^1\), also Draft Common Frame of Reference (hereinafter referred to as the DCFR)\(^2\). At the end of the article the author shall try to discuss the content of good faith standard applied in Lithuanian commercial contract law.

**Good faith and fair dealing in UNIDROIT principles**

The Article 1.7 of UNIDROIT principles (Good faith and fair dealing) states: "(1) Each party must act in accordance with good faith and fair dealing in international trade. (2) The parties may not exclude or limit this duty".

So the text of the article reveals that the content of this standard should be analyzed taking into regard the international trade. As the authors of the Official Commentary emphasize, good faith and fair dealing should not be interpreted and applied in terms of national legal systems, but rather in international context\(^4\).

However, for the purposes of this research, the word "trade" is of significant importance. The authors of Official Commentary clearly acknowledge the specifics of the standard applied in commercial contractual relationship: "A further implication of the formula used is that good faith and fair dealing must be construed in the light of the

---

1 Authors note, that the conclusion of the court that the behavior of a party is contrary not only to the principle of good faith, but also to fair dealing, causes the problem of separation of these two notions. However, this issue has not been developed in detail, and analysis focuses on the content of the general principle of good faith. Arlauskas S.; Jakūbauskas, R. Sąžiningumo principas prievoliniuose teisiniuose santykiuose. Jurisprudence, 20 (4), 1368-1390.

2 UNIDROIT Principles have been analyzed as this soft law instrument is designed to regulate specifically commercial contracts. What is more, it is one of the essential documents, which have been used in drafting of CC (regarding contract law provisions).

3 DCFR is analyzed, first of all, because it is one of the newest instruments designed to be applied in contract law of the European region. What is more, this toolbox is of significant importance, as the drafting process has been initiated by EU institutions, also it is a result of cooperation of widely recognized legal experts of EU Member states, so it at least partly reflects the tendencies in the European Union (hereinafter referred to as the EU) policy and tendencies in the contract law sphere.

4 "The reference to "good faith and fair dealing in international trade” first makes it clear that in the context of the Principles the two concepts are not to be applied according to the standards ordinarily adopted within the different national legal systems. In other words, such domestic standards may be taken into account only to the extent that they are shown to be generally accepted among the various legal systems”. UNIDROIT Principles of International Commercial Contracts with Official Commentary. [interactive]. 1994. [accessed 2013-09-11], http://www.jus.uio.no/lm/unidroit.international.commercial.contracts.principles.1994.commented/toc.html
special conditions of international trade. Standards of business practice may indeed vary considerably from one trade sector to another, and even within a given trade sector they may be more or less stringent depending on the socio-economic environment in which the enterprises operate, their size and technical skill, etc.”

Of course, it cannot be denied that good faith and fair dealing is a moral standard. It is admitted that it “is clear from the language of Art. 1.7 (‘good’, ‘fair’) that the application of the provision requires a value judgment. It converts a moral or ethical precept into legal standard. <…> The function of good faith and fair dealing is “the mitigation of the rigor of the law in order to strike a balance between legal certainty and substantive justice and to achieve equitable solutions in exceptional cases”.

However, the objectiveness of this standard is highlighted. It is often stressed out that that Article 1.7 of UNIDROIT Principles should not be applied in the purpose of protection of rights of parties having weaker bargaining position. What is more, this limit is also applied in cases of contract concluded between businessmen having unequal bargaining position. So it is obvious that the content of such standard should not be understood the same as in cases of national good faith and fair dealing rules, which are often designed to protect the rights of weaker parties.

What is more, the objectiveness of the doctrine is explained also by its relation to the trade within it is applied. „This means that the content of such standard cannot be interpreted as applicable only in particular relationship to particular parties according particular circumstances. The objectiveness in this case means that the standard must have the same content to all participants of respective trade. Furthermore, decisions of judges and arbitrators if a party acted in good faith cannot be based only on their personal values and must correspond standards recognized in international trade. Of course, there is still a debate on the content of such international trade standard: how broad such recognition must be. But the fact that a distinguishing line must be drawn cannot be denied”. This extract explains the importance of specifics of commercial relationship – the behavior of a businessmen should necessarily be evaluated in the light of the trade in which he operates.

So we have to admit that good faith and fair dealing employed in UNIDROIT Principles definitely may be one of the examples proving that the content of this standard varies according to the type of relationships for which it is designed and commercial doctrine of this standard has its peculiarities.

---

1 Ibid.
2 This is one of the reasons, why it is sometimes criticised as being not reasonable solution for commercial transactions. Despite that, it is expressly employed in UNIDROIT Principles and even recognized as one of the fundamental standards of this soft law document.
5 Ibid.
Good faith and fair dealing in DCFR

Although general Article I. – I:103 of DCFR adopting good faith and fair dealing obligation and it’s commentary do not define any differences between good faith and fair dealing in business and other relations, the analysis of other articles shows that the authors of this soft law instrument intended to separate such concepts. An example – the unfairness test, defined in Article II.-9:405 (Meaning of “unfair” in contracts between businesses): „A term in a contract between businesses is unfair for the purposes of this Section only if it is a term forming part of standard terms supplied by one party and of such a nature that it use grossly deviates from good commercial practice, contrary to good faith and fair dealing“. The unfairness test defined in Article is definitely different from the ones which are defined in Articles II.-9:4032 and II.-9:4043. „While under these provisions a term is considered unfair if it „significantly disadvantages the other party, contrary to good faith and fair dealing“, the present Article requires the term to „grossly deviate from good commercial practice, contrary to good faith and fair dealing“. The reference to „good faith and fair dealing“, which is the common element of three unfairness tests, indicates that in all three cases „content control“ is a derivative of the general principle of good faith. Nevertheless, the standard applied under the present Article is considerably different from the one in the two preceding ones. In effect under the present Article a term is considered unfair only „if it deviates from good commercial practice“.

Another example of separation is also seen in regard to the scope of information duties: in determining, what information should be reasonably expected to be provided from one businessmen to another, it must be taken into account that in a commercial relationship the scope of the duty is quite different. This limits reasonable expectations of the businessman acquiring information to the extent which would not differ from good commercial practice. What is more, it is even suggested that the introduction of „good commercial practice“ criteria could be a solution to the problem of contradictions of Acquis communautaire (which in some sense includes DCFR) and commercial law.

However, it has to be noted that such distinction has been criticized. For example, M. W. Hesselink emphasized that the test under Article II.-9:405 of DCFR does not take into consideration the fact that business parties to the transaction may have very

1 DCFR I. – I:103 (Good faith and fair dealing): (1) The expression “good faith and fair dealing“ refers to the standard of conduct characterized by honesty, openness and consideration for the interests of the other party to the transaction in question. (2) It is, in particular, contrary to good faith and fair dealing for a party to act inconsistently with that party’s prior statements or conduct when the other party has reasonably relied on them to that other party’s detriment.
2 II.-9:405 (Meaning of “unfair” in contracts between a business and a consumer).
3 II.-9:405 (Meaning of “unfair” in contracts between non-business parties).
different bargaining power, for example, a contract concluded between large international company and one-man company. He offered to take inspiration from Germany, where the same test is applied in commercial and consumer relations. M. W. Hesselink also raised the question regarding the concept on which such distinction has been based. Despite that, the Commentary of this Article expressly states that “the “content control” is not justified by general assumption of unequal negotiation power between the parties, but a general assumption that the use of standard terms drafted in advance by one party enabled the party supplying these terms to restrict the other party’s contractual freedom”.

So it is clear that under DCFR there is a line, separating the application of good faith and fair dealing in business and other relations. What is more, good commercial practice standard can probably be considered as the essential element of such separation.

**Good faith and fair dealing in Lithuania**

The Supreme Court of Lithuania defines good faith as a measure of human behavior which is determined by the objective and subjective criteria. „Objectively, good faith is understood as human behavior, corresponding to the requirements of reasonableness and justice, i.e., careful and considerate behavior. Subjectively, good faith describes the mental state of a person in a particular situation, depending on the person's age, education, experience and facts. In order to determine whether a person acted in good faith, it is necessary to apply both of these criteria“.

The Article 6.158 of CC has been drafted under Article 1.7 of UNIDROIT Principles. As this Article of CC is applicable in all sorts of contractual relationships, the part „in international trade“ has been omitted and such solution is undoubtedly reasonable. However, some part of contracts regulated by CC and contractual disputes solved by Lithuanian courts are definitely commercial. For this reason, in cases when the contractual relationship is commercial, the common trade standards should be taken

---


3. The Supreme Court of Lithuania, Civil Division, 19 June 2013 ruling of the board of judges in the civil case D. J. v. J. B (case No. 3K-3-336/2013).

4. The Supreme Court of Lithuania, Civil Division, 21 September 2009 ruling of the board of judges in the civil case BUAB „Vikata ir Ko“ v. UAB „Daisruna ir Ko“ (case No. 3K-3-361/2009); The Supreme Court of Lithuania, Civil Division, 30 November 2010 ruling of the board of judges in the civil case AB „Alytaus tekstilė“ v. AB „Rytų skirstomieji tinklai“ (case No. K-3-485/2010) and others.

5. For the purpose of this article terms “good commercial practice”, “common business practice”, “common commercial practice”, “common trade standards” are used as synonyms, presuming that they define predominant business standards applied in particular trade sector.
into account, as it is done in Article 1.7 of UNIDROIT Principles. This notion is affirmed in one of the case law examples where the Supreme Court of Lithuania recognizes two separate concepts defined in the Article 6.158 of CC: “good faith” and “fair dealing”, and explains that the second one signifies the good faith in business, which means both: acting in accordance with general standards of the behavior applied to any person and specific standards of behavior existing in particular business sector¹.

Good faith and fair dealing provision is almost never applied alone – an article regulating precise aspect is mostly applied in conjunction. For this reason, good faith and fair dealing (without the application of other legal norms) rarely is the criteria having decisive role in the judgment – most often the infringement of good faith and fair dealing norm is also an infringement of other (more precise) legal provision. However, this is different in Actio Pauliana cases, where one of mandatory conditions for the satisfaction of the claim is bad faith of the defendant and third person. It should be noticed that common business practice is often mentioned in the decisions of the courts solving Actio Pauliana disputes between businessmen. Despite that, this criterion is almost never regarded as a decisive factor in determining whether a party acted in good faith. Courts often mention, that the conclusion of the transaction corresponded common business practice, but decide to satisfy Actio Pauliana claim, because they determine that a party knew or should have known that the transaction infringed the rights of the creditor. Yet this practice has exceptions. We should mention a decision of Supreme Court of Lithuania (2010) where the court ruled differently. Although, the claim was dismissed not only due to the fact that the conclusion of transaction corresponded business practice², this time the court minimally commented on its content: „Actio Pauliana cannot be explained in a way creating preconditions to contest transactions which at the time of conclusion were not forbidden and corresponded common commercial practice, despite the fact that at that moment the debtor also had obligations towards other creditors and later bankruptcy proceedings were started. Such interpretation and application of law raises legal uncertainty, distrust in the debtor who has financial problems and unreasonably limits the ability to operate and pursue settlement with all creditors avoiding bankruptcy <…>). Such decisions are often dictated by business logic and sometimes it is the only possibility to avoid the bankruptcy”³.

In the opinion of the author of this article, common business practice is almost unanalyzed in case law of Lithuania and she doubts that courts really take this criterion into account⁴. Most often the application is limited only to mentioning. On the other hand, it is obvious that the analysis of common commercial practice is a very complicated process, which is highly dependent not only on the qualification and experience in

¹ The Supreme Court of Lithuania, Civil Division 16 December 2008 ruling of the board of judges in the civil case AB “VST” v. UAB „Olympic Casino Group Baltija“(case No. 3K-3-572/2008).
² It has to be noted that common business practice is discussed in determining if the transaction infringed the rights of the creditor (other condition of Actio Pauliana case), but cannot be doubted that these conditions are very related and overlap.
³ The Supreme Court of Lithuania, Civil Division, 30 November 2010 ruling of the board of judges in the civil case AB „Alytaus tekstilė“ v. AB „Rytų skirstomieji tinklai“(case No. K-3-485/2010).
⁴ Except infrequent cases.
business relations of the judge, the time, which can be spared for the analysis, but also – on qualification of the parties who must prove the existence of such practice.

Conclusions

The distinction between general notion of good faith and its commercial equivalent is clearly expressed not only in UNIDROIT Principles, which are designed to be applied in international trade, but also in DCFR, which is drafted to be applied in consumer, non-business and commercial relationships. The analysis of these soft law instruments makes it clear that separation of general and commercial concepts of the principle has been recognized. What is more, common business practice of particular trade should be regarded as very significant for the application of good faith and fair dealing standard in commercial relationships; it should be applied in conjunction with the criteria of common business practice, inherent to particular business sector.

The Supreme Court of Lithuania also recognizes peculiarities and differences of good faith notion applied in commercial relations. What is more, when determining if a businessman acted in good faith, court mentions commercial practice as one of the criteria, important for such evaluation of the behavior. However, it is doubted that most courts really take it into account and it can be guessed that often the application of this standard is limited only to mentioning. But this is also the problem of parties of the dispute, as the presentation of reasonable arguments and proofs to the judge is their right and obligation.

References

The Supreme Court of Lithuania, Civil Division 16 December 2008 ruling of the board of judges in the civil case AB “VST” v. UAB „Olympic Casino Group Baltija“ (case No. 3K-3-572/2008).
The Supreme Court of Lithuania, Civil Division, 21 September 2009 ruling of the board of judges in the civil case BUAB „Vikata ir Ko“ v. UAB „Daisruna ir Ko“ (case No. 3K-3-361/2009).
The Supreme Court of Lithuania, Civil Division, 30 November 2010 ruling of the board of judges in the civil case AB „Alytaus tekstilė“ v. AB „Rytų skirstomieji tinklai“ (case No. K-3-485/2010).

The Supreme Court of Lithuania, Civil Division, 19 June 2013 ruling of the board of judges in the civil case D. J. v. J. B (case No. 3K-3-336/2013).


