

DOCTOR OF PHILOSOPHY

A comparative evaluation of the legislative
controls on unfair terms and exemption
clauses in consumer and business
contracts in England and Brazil

Luciana Iwasa

2013

Aston University

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A COMPARATIVE EVALUATION OF THE LEGISLATIVE CONTROLS ON
UNFAIR TERMS AND EXEMPTION CLAUSES IN CONSUMER AND BUSINESS CONTRACTS
IN ENGLAND AND BRAZIL

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Thesis Summary

Aston University

A Comparative Evaluation of the Legislative Controls on Unfair Terms and Exemption Clauses in Consumer and Business Contracts in England and Brazil

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MPhil/PhD Management

2012

The purpose of the present study is to make a comparative evaluation of the legislative controls on unfairness in the context of B2B, B2C and small businesses contracts in England and Brazil. This work will focus on the examination of statutes and relevant case law which regulate exemption clauses and terms on the basis of their 'unfairness'.

The approach adopted by legislation and courts towards the above controls may vary according to the type of contract. Business contracts are more in line with the classical model of contract law according to which parties are presumably equals and able to negotiate terms. As a consequence interventions should be avoided for the sake of freedom of contract even if harmful terms were included. Such assumption of equality however is not applicable to small businesses contracts because SMEs are often in a disadvantageous position in relation to their larger counterparties.

Consumer contracts in their turn are more closely regulated by the English and Brazilian legal systems which recognised that vulnerable parties are more exposed to unfair terms imposed by the stronger party as a result of the inequality of bargaining power. For this reason those jurisdictions adopted a more interventionist approach to provide special protection to consumers which is in line with the modern law of contract.

The contribution of this work therefore consists of comparing how the law of England and Brazil tackles the problem of 'unfairness' in the above types of contracts. This study will examine the differences and similarities between rules and concepts of both jurisdictions with references to the law of their respective regional trade agreements (EU and the Mercosul). Moreover it will identify existing issues in the English and Brazilian legislation and recommend lessons that one system can learn from the other.

COMPARATIVE LAW - ENGLAND AND BRAZIL - CONTRACT LAW -
UNFAIR TERMS - EXEMPTION CLAUSES

Dedication

For my beloved husband Roberto for his unconditional love and support.

For my dear parents for their sacrifices, guidance and eternal love.

For all those who were there for me when I needed most.

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List of Abbreviations

B2B	Business-to-Business
B2C	Business-to-Consumers
C2C	Consumers-to-Consumers
DGFT	Director General of Fair Trading
EU	European Union
Mercosul	Southern Common Market
MSEs	Micro and Small Enterprises
OFT	Office of Fair Trading
SEBRAE	Brazilian Support Service for Micro and Small Businesses
SMEs	Small and Medium Enterprises
UCC	American Uniform Commercial Code

Legislation

Statutes/ Statutory Instruments

CA	Companies Act 2006
CPRs	Consumer Protection from Unfair Trading Regulations 2008
UCTA	Unfair Contract Terms Act 1977
UTCCR or Regulations	Unfair Terms in Consumer Contracts Regulations 1999

EU Law

CESL	Common European Sales Law
DCFR	Draft Common Frame of Reference
PECL	Principles of European Contract Law
PICC	Principles of International Commercial Contracts (Unidroit)
SBA	A Small Business Act for Europe
TEC	Treaty Establishing the European Community
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union

Directives

Directive 93/13/EEC	Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts
UCPD	Directive 2005/29/EC of the European Parliament and of the Council of 11 May 2005 on Unfair Commercial Practices
SCGD	Directive 99/44/EC of the European Parliament and of the Council of 25 May 1999 on Certain Aspects of the Sale of Consumer Goods and Associated Guarantees

Journals

ABA	American Bar Association
Ajuris	Associação dos Juizes do Rio Grande do Sul
Am J Comp L	American Journal of Comparative Law
Am Sociolog Rev	American Sociological Review
BLR	Business Law Review
Brit J Law & Soc	British Journal of Law and Society
CBLJ	Canadian Business Law Journal
CIL	Contemporary Issues in Law
CJQ	Civil Justice Quarterly
CLJ	Cambridge Law Journal
CLP	Current Legal Problems
CML Rev	Common Market Law Review
Colum L Rev	Columbia Law Review
Comm L World Rev	Common Law World Review
Comm Law	Commercial Lawyer
Consum LJ	Consumer Law Journal
Cornell L Rev	Cornell Law Review
CTLR	Computer and Telecommunications Law Review
Denning LJ	Denning Law Journal
Disp Resol J	Dispute Resolution Journal
Duke LJ	Duke Law Journal
EBL Rev	European Business Law Review
EL Rev	European Law Review
ERCL	European Review of Contract Law

ERPL	European Review of Private Law
Harvard Intl LJ	Harvard International Law Journal
Harv L Rev	Harvard Law Review
HLJ	Hertfordshire Law Journal
IBFL	International Banking and Financial Law
IBL	International Business Lawyer
IBLJ	International Business Law Journal
ICCLR	International Company and Commercial Law Review
ICLQ	International & Comparative Law Quarterly
IJLMA	International Journal of Law and Management
IMP	Industrial Marketing and Purchasing Journal
Int ALR	International Arbitration Law Review
Int Bank L	International Banking Law
Iowa L Rev	Iowa Law Review
Israel L Rev	Israel Law Review
J Law & Soc	Journal of Law & Society
J Legal Hist	Journal of Legal History
JO & R	Journal of Obligations and Remedies
JWTL	Journal of World Trade Law
JBL	Journal of Business Law
JCL	Journal of Contract Law
JCP	Journal of Consumer Policy
JEL	Journal of Environmental Law
JIBL	Journal of International Banking Law
JIBLR	Journal of International Banking Law and Regulation
Law & Phil	Law and Philosophy
LCP	Law and Contemporary Problems
LQR	Law Quarterly Review
LS	Legal Studies
Marq L Rev	Marquette Law Review
MJ	Maastricht Journal of European and Comparative
Law	
MLR	Modern Law Review
MULR	Melbourne University Law Review
OJLS	Oxford Journal of Legal Studies

R CEJ	Revista Centro de Estudos Judiciários
SJ	Solicitors' Journal
SLT	Scots Law Times
Tr L	Trading Law
Tul L Rev	Tulane Law Review
U Chi L Rev	University of Chicago Law Review
U Pa L Rev	University of Pennsylvania Law Review
UTLJ	University of Toronto Law Journal
UCL Juris Rev	UCL Jurisprudence Review
Va L Rev	Virginia Law Review
Val U L Rev	Valparaiso University Law Review
Wake Forest L Rev	Wake Forest Law Review
Web JCLI	Web Journal of Current Legal Issues
WMLR	William and Mary Law Review

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CHAPTER 1. INTRODUCTION

1.1. Context of the research

Contracts are an inevitable part of the daily relations of the members of a society and they play a vital role of providing a minimum stability to agreements since they operate as means to regulate and enforce those agreements.¹ Where parties to contract are in an equal position and are able to negotiate terms (generally in contracts between businesses), interferences should be avoided and the freedom of contract should prevail.²

However such equality between parties is not present in all contractual relationships (e.g., consumer and small business contracts) and the party who retains a predominant bargaining strength often abuses its relative superior position to impose terms, such as unreasonable exemption clauses, which benefit its own interests to the detriment of the interests of the other party.

A number of jurisdictions including *England* and *Brazil* recognised the need to interfere in those contracts where the imbalance between parties may give rise to the exploitation of the weaker party. As a consequence they have enacted legislative controls which purport to prevent the inclusion or invalidate terms that may be regarded as 'unfair' on the basis that those terms may harm the interests of one of the parties or frustrate his legitimate expectations.

Presently the law has to find a balance between the need to prevent this unfairness in contractual relations and the 'demands of certainty and stability' in contracts which may be affected by excessive interventions.³ This balance will tilt differently towards one side (freedom of contract) or the other (intervention) in business and consumer contracts.

¹ The law of contracts provide remedies in case obligations voluntarily assumed are broken. See Laurence Koffman and Elizabeth Macdonald, *The Law of Contract* (7th edn, Oxford University Press 2010) 1.

² This non-interventionist approach can be found in *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827 (HL) and *Watford Electronics Ltd v Sanderson CFL Ltd* [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696.

³ Mindy Chen-Wishart, *Contract Law* (3rd edn, Oxford University Press 2010) 461.

1.1.1. Objective of the research

The purpose of this thesis is to examine those legislative controls on exemption clauses and unfair terms in B2B, B2C and small businesses contracts in a comparative analysis of the English and Brazilian legal systems.

This work will focus on pieces of legislation which exert a 'direct statutory control'⁴ over exemption clauses and terms on the basis of their 'unfairness'. It will be carried out in the light of the *Unfair Contract Terms Act 1977* and the *Unfair Terms in Consumer Contracts Regulations 1999* which according to Macdonald 'are probably the two single most significant pieces of legislation in the field of contract law in the UK. Together they provide a powerful weapon against unfair terms'.⁵ As the criterion of application of UCTA and UTCCR is the unfairness of terms, they are not limited to the 'legislative regulation of specific terms (e.g., the consumer credit legislation)⁶ or particular types of contracts.⁷ This will allow a comparative analysis with the *Brazilian Federal Constitution, Civil Code* and *Consumer Protection Code* which also prescribe rules against unfairness applicable to terms in general.⁸

The research therefore will examine pieces of legislation which deal with the unfairness of terms through the use of 'general clauses' such as *good faith* and *significant imbalance* in the UTCCR and *reasonableness* in UCTA.⁹ The Brazilian law in its turn adopts principles such as *good faith* and the *social function of the contracts*. Special attention will be drawn to *good faith* because it is a concept which highlights the differences between the legal systems in question and it is an important way of controlling unfairness in Brazil and the EU.

⁴ Ibid. According to Chen-Wishart in addition to these direct statutory controls there are also indirect controls over terms because before the validity of a term can be challenged it is necessary to determine whether the 'contested statement': is a term of the contract, is incorporated into the contract and covers the events in question.

⁵ Elizabeth Macdonald, 'Unifying Unfair Terms Legislation' (2004) 67(1) MLR 69, 69.

⁶ Jill Poole, *Textbook on Contract Law* (10th edn, Oxford University Press 2010) 244.

⁷ As opposed to statutes which regulate particular types of contracts to 'counter unfairness' such as Sale of Goods Act 1979, Landlord and Tenant Act 1985, Employment Rights Act 1996, Defective Premises Act 1972 and so forth. See Chen-Wishart (n 3) 501-502.

⁸ The provisions of the Consumer Protection Code are in principle limited to consumer contracts, but they have been applied by analogy to other types of contracts (such as small businesses contracts).

⁹ Chris Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (2012) 71(2) CLJ 412

In addition reference to other statutes and regulations will be made when appropriate, including the law of the regional trade agreements from which England and Brazil are Member States (*European Union* and *Mercosul* respectively) in view of the influence of the latter over the domestic contract law of those countries.

The above comparison between the law of England and Brazil aims to examine similarities and differences in how different legal systems which adopt distinct legal traditions (common law and civil law respectively) deal with the same legal problem (unfairness in B2B and B2C contracts). This study will also diagnose unresolved issues which permeate the relevant legislation and case law of both jurisdictions and compare problems that affect their law. A comparative evaluation between the English and Brazilian legal systems will ultimately allow the identification of the best solutions which have been applied by one legal system and that can be incorporated by the other in order to improve the way that this system deals with the problem of unfairness.

1.1.2. Relevance of the research

As seen previously this comparative study will allow English and Brazilian comparatists, legislators and courts to find 'models of law' in the other legal system which they may consider worth enacting in their own jurisdiction (e.g., to develop or reform the law).¹⁰ They may also use the comparison to fill gaps in the legislation or case law of their country.¹¹ For instance the adoption of good faith as a general clause similar to the one which has been efficiently applied by the Brazilian legal system could potentially allow British courts to protect parties in more cases of unfairness, in particular at the negotiation stage where currently there is no such protection.

This comparison can also be of practical significance in the context of *transnational transactions*. Exchanges involving businesses and consumers of different countries have led to an increasing interaction between the contract law of distinct jurisdictions. Comparative studies therefore have become essential to facilitate those interactions in a globalised world.

¹⁰ Peter De Cruz, *Comparative Law in a Changing World* (3rd edn, Routledge-Cavendish 2007) 20.

¹¹ *Ibid.* 21. See also *Fairchild v Glenhaven Funeral Services Ltd* [2002] UKHL 22.

This work will tackle an important aspect of contractual relations which has a significant impact over the establishment of trust between parties (including businesses), stability of the agreements and consumer confidence in cross-border transactions. Furthermore this study will involve the law of England and Brazil which are among the largest economies in the world. In fact 'the Brazilian economy has overtaken the UK economy in 2011 to become the world's 6th largest economy'.¹²

The UK government has supported the development of a 'stronger trading relationship with Brazil' to explore commercial opportunities arising from the economic growth of the latter which includes negotiations on an 'EU-Mercosul Free-Trade Agreement'.¹³ This is an indication that the volume of contractual relations between English and Brazilian parties is likely to increase significantly in the forthcoming years; therefore comparative studies such as the present one will be of great utility to assist negotiations or guide national courts in legal disputes involving both jurisdictions. De Cruz noted that 'in the ascertainment and application of foreign law in national courts, the comparative method is not just a requirement, but a necessity'.¹⁴

Consequently the fact that presently there are no studies comparing the legal systems of England and Brazil in this context means that this work may offer some guidance and reassurance to English businesses or individuals who are willing to negotiate with a Brazilian party, or vice versa, but are unsure how the legislation of the other legal system will protect their interests and whether they will be exposed to terms that can harm their interests.¹⁵

1.1.3. The English and Brazilian legal systems: a comparison

The present work will involve the comparison of English and Brazilian contract law which adopt respectively two of the main legal traditions: the civil law and common law.¹⁶ A

¹² See the latest *World Economic League Table* published in December 2011 by the Centre for Economics and Business Research (CEBR) <<http://www.cebr.com/wp-content/uploads/Cebr-World-Economic-League-Table-press-release-26-December-2011.pdf>> accessed 18 July 2012.

¹³ See Foreign Affairs Committee, *UK-Brazil Relations: Ninth Report of Session 2010-12* (HC 2010-12, 949) paras 1-11 and Foreign Affairs Committee, *UK-Brazil Relations: Response of the Secretary of State for Foreign and Commonwealth Affairs* (Cm 8237, 2011) paras 3-31.

¹⁴ De Cruz (n 10) 22-23.

¹⁵ For instance before setting up an international company, the latter need to acquire 'a good understanding of the legal requirements with which the company will have to comply and the legal framework within which the company will have to transact its business'. See *Ibid.* 23.

¹⁶ René David and John E. C. Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (3rd edn, Stevens & Sons 1985).

comparative study involving contrasting legal systems will provide a distinctive perspective on the analysis of their rules, concepts and legal problems.

Brazil adopts the *civil law* tradition also known as 'Romano-Germanic family',¹⁷ which is based on the Roman '*ius civiles*' and has its origin in Europe. Civil law is nowadays one of the most widespread legal traditions in the world and its concepts and rules are quite abstract and general. It applies a '*deductive* style of reasoning' (of general principles to specific cases).¹⁸ By comparison, England is a member of the *common law* family which applies an *inductive* reasoning (from particular cases to more general principles).¹⁹ Originally, this family was based on judicial decisions and was more concerned to provide a concrete solution for a problem than create general and systematic rules as the civil law.

Those differences between the legal systems of England and Brazil may enrich a comparison between them, enabling the identification of unexpected similarities or distinct ways to deal with a common problem or situation.

1.1.3.1. The English legal system

Although common law is England's legal system, legislation enacted by Parliament is currently its 'predominant method of law-making'.²⁰ Consequently the significance of statutory controls over unfair terms has been increasing, but courts still play an important role in the interpretation of statutes through case law. Although in England there are various pieces of legislation and common law rules that aim to control the unfairness of terms,²¹ this study will focus on UCTA and the UTCCR 1999 for the reasons examined above.

English law has been increasingly influenced²² by European law through Treaties²² (primary EU legislation) and secondary EU legislation which includes regulations, directives,

¹⁷ See René David, *Major Legal Systems in the World Today* (4th edn, Martins Fontes 2002) 111.

¹⁸ Chen-Wishart (n 3) 6-7.

¹⁹ *Ibid.*

²⁰ Gary Slapper and David Kelly, *The English Legal System* (11th edn, Routledge 2010-2011) 78.

²¹ For instance, in the context of consumers: Consumer Credit Act 1974, Sale of Goods Act 1979, Supply of Goods and Services Act 1982, Consumer Protection Act 1987, Consumer Protection (Distance Selling) Regulations 2000 (SI 2000/2334). There are also common law rules regarding incorporation and construction of exemption clauses.

²² Section 2(1) of the European Communities Act 1972.

decisions, recommendations and opinions.²³ Such influence is due the fact that England is a member of the *European Union* and has to comply with its law. The EU in its turn is a supranational organisation composed of 27 Member States²⁴ and was established by the Treaty on European Union (Maastricht Treaty)²⁵ in 1992 based on a community of political and economic interests.²⁶

Consumer protection is one area which has been significantly affected by the EU law.²⁷ For instance, important changes were introduced by the *Directive on Unfair Terms in Consumer Contracts*²⁸ and more recently the *Directive on Consumer Rights*²⁹ aims to enhance the protection of consumers within the common market.

1.1.3.2. The Brazilian legal system

The Brazilian legal system adopts the civil law tradition; thus its primary source is the law *lato sensu*.³⁰ The most authoritative law is the Federal Constitution, followed by Codes and other federal statutes.

The understanding of the current contractual regimes applied in Brazil will require a brief overview of significant changes which occurred in the Brazilian law of contracts. Until 1991 there were basically two main regimes: the 'civil' and the 'commercial'.³¹ The *civil*

²³ Article 288 (ex article 249 TEC) of the Consolidated versions of the Treaty on European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU).

²⁴ Trevor C. Hartley, *European Union Law in a Global Context: Text, Cases and Materials* (Cambridge University Press 2004) 1-14. The current EU member countries are: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Ireland, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom.

²⁵ [1992] OJ C191/01.

²⁶ 'The establishment of the European Coal and Steel Community (ECSC) in July 1952 was the first step towards a supranational Europe. For the first time the six Member States of this organisation relinquished part of their sovereignty (...) in favour of the Community'. See <http://europa.eu/legislation_summaries/institutional_affairs/treaties/treaties_eec_en.htm> accessed 12 October 2012. The ECSC was followed by the establishment of the European Economic Community (EEC) through the adoption of the Treaty of Rome in 1957 (which aim included the creation of a community and the establishment of a common market 'by the removal of obstacles to the free movement of capital, goods, people and services') and then by the establishment of the European Union (EU) through the adoption of the Maastricht Treaty. See Philip Waller-Thody, *Historical Introduction to the European Union* (Routledge 1997) xii.

²⁷ Article 169 (ex article 153 TEC) of the Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union expressly prescribes the consumer protection by the European Community and articles 206 and 207 (ex articles 131 and 133 TEC) establish a common commercial policy for the EU.

²⁸ Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts [1993] OJ L95/29.

²⁹ Commission, 'Proposal for a Directive on Consumer Rights' COM (2008) 614 final.

³⁰ David, *Major Legal Systems in the World Today* (n 17) 111.

³¹ Fábio Ulhoa Coelho, *Curso de Direito Comercial – volume 3* (3rd edn, Saraiva 2002)18.

regime was governed by the revoked Brazilian Civil Code (Act 3071 of 1916) and was applicable to all contracts made between private parties.³² On the other hand the *commercial* regime was applicable to contracts made between businesses and it was governed by the Commercial Code (Act 556 which dates back to 1850).³³

In 1990, the advent of the Consumer Protection Code created a third regime in private law called '*consumerist*'³⁴ resulting in the coexistence of three contractual regimes: the commercial for B2B contracts, the consumerist for B2C contracts and the civil for contracts between non-businesses.

This classification lasted until the enactment of the new Civil Code in 2002 (Act 10406)³⁵ which promoted the *legislative unification* of the private law and the rules of contracts; hence it revoked the first part of the Act 556/1850 that dealt with commercial contracts and its own predecessor (Act 3071/1916) as a whole. As a consequence presently there are only two regimes of contracts. The first one is the '*consumerist*' that is regulated by the Consumer Protection Code and deals with all contracts involving consumers and sellers or suppliers. The second is the '*civil*' that is applied to the remaining contractual relations, civil or commercial, under the provisions of the new Civil Code.³⁶

This internal legislation of Brazil may be influenced by the regulations of the *Mercosul* (or Mercosur)³⁷ which is a Regional Trade Agreement with an intergovernmental nature³⁸ that this country is a Member State alongside Argentina, Paraguay, Uruguay and more recently

³² Except for employment contracts that had special rules. This Civil Code was substantially influenced by the German Civil Code ('Bürgerliches Gesetzbuch' or BGB of 1900). Ibid.

³³ The Commercial Code was based on the Codes of Portugal, France and Spain.

³⁴ Article 48 of the Federal Constitution Transitional Provisions prescribed that the National Congress had to draw the Consumer Protection Code up within 120 days of the Constitution's promulgation. The constituent opted for a Code rather than a statute to provide a more comprehensive protection to consumer rights (although it was formally enacted as an Act). See Ada Pellegrini Grinover and others, *Código Brasileiro de Defesa do Consumidor - Direito Material (Arts 1º a 80 e 105 a 108) - Vol. I* (10th edn, Forense 2011) 6-7. Although this Code was published on 12/09/90, it came into force on 11/03/1991 (180 days after its publication according to its article 118).

³⁵ The Civil Code was published on 10/01/02, but it came into force on 13/01/03 (1 year after its publication according to its article 2044).

³⁶ Martins proposed that what differs a commercial obligation from a civil obligation is the nature of the act that gave origin to it. See Fran Martins, *Contratos e Obrigações Comerciais* (16th edn, Forense 2010) 10.

³⁷ '*Mercosul*' is the abbreviation for 'Mercado Comum do Sul' (in Portuguese) and 'Mercosur' is the abbreviation for 'Mercado Común del Sur' (in Spanish) that means *Southern Common Market*.

³⁸ The Mercosul differently from the EU does not intend to become a supranational organisation. Its Member-States have 'veto power' and the administrative and normative decisions must be taken by unanimity. See Eduardo Antônio Klausner, *Direito do Consumidor no Mercosul e na União Européia: Acesso e Efetividade* (Juruá 2006) 63.

Venezuela.³⁹ Mercosul was founded in 1991 by the *Treaty of Asunción* which was subsequently amended by the *Treaty of Ouro Preto* in 1994 and aims to achieve the economic integration of its members. Currently Mercosul is a customs union, but it is close to reach its main objective of becoming a common market.⁴⁰ It purports to promote a 'free movement of goods, services and factors of production between countries'⁴¹ and it is 'seen as the most dynamic and successful regional trade organisation other than the EU.'⁴²

Its Members States are committed to 'harmonize their legislation in the relevant areas in order to strengthen the integration process'.⁴³ Although there are no Resolutions that deal expressly with unfair terms,⁴⁴ the fundamental rights of the consumers in the Mercosul include 'the balance of consumer relations, ensuring the respect for the values of dignity and loyalty, based on good faith' and 'the protection against abusive clauses and abusive commercial practices'.⁴⁵

In 1997 the Technical Committee number 7 (CT 7) of the Mercosul proposed a *Consumer Protection Protocol* which intended to unify the consumer legislation of all Member States. The latter however rejected this Protocol for various reasons. Brazil's opposition was based on the fact that the level of protection offered by this Protocol was inferior to the protection prescribed by the Brazilian Consumer Protection Code; whereas other Member States (e.g., Uruguay and Paraguay) considered the level of consumer protection given too high as compared to their domestic legislation, especially with regard to certain contractual protections such as the prohibition of abusive clauses.⁴⁶

³⁹ In addition to those five full members it has also five 'associate members': Bolivia, Chile, Colombia, Ecuador and Peru. Venezuela signed a membership agreement in June 2006, but its entry was pending ratification by the Congress of Paraguay. The fact that Paraguay is currently suspended from the Mercosul on the basis of the 'interruption of its democratic order' (due to the summary impeachment of its President) allowed Venezuela to become a full member in July 2012.

⁴⁰ Edgard Oliveira Lopes, 'A Tutela Consumerista na União Européia e no Mercosul' <http://www.ambito-juridico.com.br/site/index.php?n_link=revista_artigos_leitura&artigo_id=4109> accessed 08 August 2011, 3.

⁴¹ See article 1 of the Treaty of Asunción.

⁴² Charles Grant, 'Europe, Mercosul and Transatlantic Relations: A British Perspective' in H Jaguaribe and ÁD Vasconcelos (eds), *The European Union, Mercosul and the New World Order* (Frank Cass 2003) 50. 'MERCOSUR is arguably the most successful and ambitious example of regional integration in Latin America'. See Gian Luca Gardini, 'Mercosur: What you see is not (always) what you get' (2011) 17(5) ELJ 683, 684.

⁴³ See article 1 of the Treaty of Asunción.

⁴⁴ See <<http://www.sice.oas.org/trade/mrcsrs/resolutions/indice.asp>> accessed 25 September 2012.

⁴⁵ See items 'b', 'i' and 'j' of the *Presidential Declaration of the Fundamental Consumers' Rights of the Mercosul* (15/12/2000).

⁴⁶ Klausner (n 38) 68-69.

Consequently although consumers are adequately protected in Brazil, they cannot find the same level of protection in cross-border transactions involving other members of the Mercosul. This leaves Mercosul one step behind the European Union as the EU has numerous directives which purport to ensure the same level of consumer protection within its internal market, as will be discussed in chapter 3.

1.2. Methodology: comparative law

Methodology 'amounts to a systematic procedure that a scholar applies as part of an intellectual enterprise',⁴⁷ which in the case of the present study is the examination of what are the legislative controls on 'unfairness' in England and Brazil, the assessment of their unresolved issues and the evaluation of lessons that one legal system can learn from the other.

As this work purports to compare rules and concepts of the English and Brazilian legal systems the most suitable methodology to achieve its goals is *comparative law* which can be defined as 'the comparison of the different legal systems of the world',⁴⁸ hence in a comparative law research 'the obvious method is *comparison*; i.e., juxtaposing, contrasting and comparing'.⁴⁹ Sacco however noted that there is not only one method of comparison;⁵⁰ thus legal scholars should employ the 'method of investigation and analysis best suited' to 'achieve a goal or desire to understand something'.⁵¹ In other words, an appropriate and feasible method should be chosen to address the research questions of this particular investigation.⁵²

The first step in the comparison consists of the choice of suitable legal systems which shall take into account the aims of the specific comparative study.⁵³ Although there is not an established criterion in the selection of the best system to be used in a comparative

⁴⁷ Elizabeth Fisher and others, 'Maturity and Methodology: Starting a Debate about Environmental Law Scholarship' (2009) 21 JEL 213, 226.

⁴⁸ Konrad Zweigert and Hein Kötz, *An Introduction to Comparative Research* (3rd edn, Oxford University Press 2008) 2. According to De Cruz comparative law 'describes the systematic study of particular legal traditions and legal rules on a comparative basis'. De Cruz (n 10) 3.

⁴⁹ A. Esin Örüçü, 'Methodology of Comparative Law' in JM Smits (ed) *Elgar Encyclopedia of Comparative Law* (Edward Elgar Publishing 2006) 446.

⁵⁰ Rodolfo Sacco, *Introdução ao Direito Comparado* (Revista dos Tribunais 2001) 33.

⁵¹ David Feldman, 'The Nature of Legal Scholarship' (1989) 52 MLR 498, 502-503.

⁵² According to Cryer, Hervey and Sokhi-Bulley 'methodology' guides our thinking or questioning and has a theoretical connotation; whereas 'method' is the actual way in which the research project is pursued. Robert Cryer, Tamara Hervey and Bal Sokhi-Bulley, *Research Methodologies in EU and International Law* (Hart Publishing 2011) 5.

⁵³ Örüçü (n 49) 443.

analysis with one's own system, some comparatists may argue that the Brazilian law is not be the most appropriate choice for a comparison. According to them the so-called 'mature legal systems' should be preferred to the 'affiliated' ones, because the former often give origin to other systems and they are in a more advanced stage of development which implies more perfected ways of solving legal problems.⁵⁴ Those 'mature systems' are also called 'ordinary places' and they usually include France, Germany and Italy to represent civil law jurisdictions; whereas common law jurisdictions are normally represented by England and the United States.⁵⁵

In line with the above classifications the Brazilian legal system shall be regarded as an 'affiliated' or 'extraordinary place'. Such 'extraordinariness' of the Brazilian law however should not be deemed as a disadvantage; on the contrary, it may actually enrich the present study. For instance Örüçü suggested that 'the future of comparative legal studies is tied both theoretically and practically to an appreciation of diversity. In fact, (...) the more "extraordinary" the place, the more important comparative legal studies become'.⁵⁶ The Brazilian legislation transposed rules and principles from European jurisdictions (e.g., Portugal, France and Germany) and adapted them to its own reality and characteristics (such as geographical conditions and population distribution).⁵⁷ As a result the inclusion of this legal system in the present comparative analysis may provide distinct insights into *how* and *why* the legislative controls on unfairness were developed and applied in the way they are today in England and Brazil as 'hidden understandings are uncovered when we try to find out why foreign legal rules, approaches and the like are different from ours'.⁵⁸

Following the choice of the relevant legal systems, comparatists should determine whether the comparison will be at *macro* or *micro-level*.⁵⁹ The proposed research will be a *micro-comparison* limited to the analysis of a specific topic (legislative controls on unfairness) in certain types of contracts (B2B, B2C and small businesses contracts) as it

⁵⁴ Zweigert and Kötz (n 48) 41.

⁵⁵ See A. Esin Örüçü, 'Comparatists and Extraordinary Places' in P Legrand and R Munday (eds), *Comparative Legal Studies: Traditions and Transitions* (Cambridge University Press 2003) 468.

⁵⁶ Ibid. 470. See also Colin R. Baxter and Kingsley T.W. Ong, 'A Comparative Study of the Fundamental Elements of Chinese and English Company Law' (1999) 48(1) ICLQ 88, 89.

⁵⁷ David and Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (n 16) 23-24. For instance the Brazilian Consumer Protection Code was influenced by EU Directives (84/450/EEC and 85/374/EEC), the French '*Projet de Code de la Consommation*', the Portuguese Executive Order 446/85 and the German AGB Gesetz (1976). See Grinover and others (n 34) 7-8.

⁵⁸ Mark Warrington and Mark Van Hoecke, 'Legal Cultures, Legal Paradigms and Legal Doctrine: Towards a New Model for Comparative Law' (1998) 47(3) ICLQ 495, 497.

⁵⁹ Macro-comparison 'refers to the study of two or more entire legal systems' whereas micro-comparison 'generally refers to the study of topics or aspects of two or more legal systems'. See De Cruz (n 10) 233.

would not be feasible to analyse all possible ways to control unfair terms in all types of contracts.

Moreover the research problem could not possibly be analysed in the context of *common law* and *civil law* as a whole because, although they have certain characteristics which define them as distinct legal families, they were adopted by various countries throughout the globe which adapted them to their own needs and peculiarities. Consequently part of their rules and concepts may have some degree of variation between different jurisdictions, even if they are part of the same legal family. For this reason this work was circumscribed to the examination of the English and Brazilian legal systems which were used as examples of common law and civil law jurisdictions respectively.

In the context of a micro-comparison 'it has been widely argued that the true basis of comparative law is "functional equivalence".⁶⁰ The latter is advocated by Zweigert and Kötz who contended that 'in law the only things that are comparable are those which fulfil the same function'.⁶¹ In line with this approach the proposed work will involve the analysis of legal provisions (and relevant case law) in England and Brazil which perform an equivalent function of controlling the unfairness of contractual terms.⁶²

The identification of equivalents through their function may enable a more flexible comparison and prevent misleading results which could occur if the analysis was limited to terminologies.⁶³ For instance the English expression 'unfair terms' has the same function and meaning as 'abusive clauses' in Brazil, whereas 'good faith' has broadly the same meaning in both countries but a different scope.⁶⁴

After determining the existence of the functional equivalence of relevant rules and concepts, the latter should be described and examined in the context of each legal system separately to prevent comparatists looking at them from only the point of view of their

⁶⁰ Örucü, 'Methodology of Comparative Law' (n 49) 443.

⁶¹ Zweigert and Kötz (n 48) 34.

⁶² The research should prioritise primary sources hence secondary sources are only used to reinforce a certain interpretation, highlight apparent issues and suggest solutions. See Mike McConville and Wing Hong Chui, *Research Methods for Law* (Edinburgh University Press 2007) 23.

⁶³ Örucü, 'Methodology of Comparative Law' (n 49) 448.

⁶⁴ In Brazil good faith is applicable to B2C and B2B contracts; whereas in England it is limited to consumer contracts.

own system.⁶⁵ For this reason the examination of the relevant legislative controls and case law in England and Brazil will precede further comparison.

At the comparative stage comparatists should identify the differences and similarities of the relevant legal systems concerning the concepts and rules under scrutiny. They should also endeavour to explain the reasons behind those divergences and resemblances (e.g., concepts with same roots).⁶⁶ It is important to take into account the characteristics of the legal systems involved as they provide the context for the comparison and may assist with the understanding of those differences and similarities (e.g., lack of a general rule or acceptance of pre-contractual liability in English law *versus* 'culpa in contrahendo' in civil law).

Finally comparatists should make a critical evaluation of the solutions offered by each legal system to the problem in question (e.g., 'unfairness' of terms) and they may conclude that solutions from one system are more, less or equally efficient in relation to another.⁶⁷ They may recognise issues on those solutions and may also suggest an alternative one.⁶⁸ Therefore the final part of the thesis will identify unresolved problems in the current legislation and suggest contributions that one system can make to the other.

1.3. Unfair terms and exemption clauses

The proposed work will revolve around the concepts of *unfair terms* and *exemptions clauses*; hence the need to define them in this preliminary chapter to avoid misunderstandings about their meaning in the context of this study.

Unfairness is commonly opposed to the idea of justice or equality. Each legal system has its own sense of fairness that may vary according to the customs and beliefs of the local community. Rawls contended that the basic structure of a society is composed by principles of fairness or justice which 'are the result of a fair agreement or bargain' between moral individuals in a symmetrical position.⁶⁹ According to Rawls the legislation of this society shall be made in accordance with this conception of justice that was agreed

⁶⁵ See Zweigert and Kötz (n 48) 43.

⁶⁶ Örüçü, 'Methodology of Comparative Law' (n 49) 449.

⁶⁷ Zweigert and Kötz (n 48) 46-47.

⁶⁸ 'Looking at foreign law can bring a deeper understanding of problems they face - perhaps even unexpected ideas for solving them'. See Basil S. Markesinis, 'Comparative law - A Subject in Search of an Audience' (1990) 53(1) MLR 1, 21.

⁶⁹ John Rawls, *A Theory of Justice: Revised Edition* (Belknap Press 1999) 10-13.

upon and a scheme of cooperation shall benefit all members of the society, in particular the 'least advantaged'.⁷⁰

In the context of contracts there are two types of 'unfairness' or 'fairness': *procedural* and *substantive*. This dichotomy is based on the ideas of Professor Leff who made the distinction between the unfairness that occurs in the 'process of contracting' (procedural) and the unfairness of the content of contracts (substantive).⁷¹ In other words, whereas procedural unfairness 'focuses on issues such as fraud and duress' and 'is concerned with the fairness of the contracting process', substantive unfairness 'is concerned with the fairness of the *outcome* of that process'.⁷² Discussions involving fairness in contracts will often make reference to this dichotomy.⁷³

As *fairness* and *unfairness* are vague concepts, each jurisdiction will define them according to the purpose of the statute in which they are employed. In Brazil unfair terms are known as *abusive clauses*. They can be defined 'as those clauses which are notably unfavourable to the weaker party (e.g., consumer) in a contractual relationship'.⁷⁴ Those clauses are inconsistent with good faith and equity as they allow the party economically dominant to exploit the vulnerable party.⁷⁵

In England a term which has not been individually negotiated is considered 'unfair' if it is 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'.⁷⁶ There are discussions on whether 'good faith' and 'significant imbalance' in the context of this provision can be regarded as a substantial or a procedural requirement or both.⁷⁷

⁷⁰ Ibid.

⁷¹ Arthur Allen Leff, 'Unconscionability and the Code – The Emperor's New Clause' (1967) 115 U Pa L Rev 485, 487.

⁷² Stephen A. Smith, 'In Defence of Substantive Fairness' (1996) 112(Jan) LQR 138, 140.

⁷³ For instance, Trebilcock made reference to this dichotomy whilst examining the basis for the decision in *Schroeder Music Publishing Co. Ltd. v Macaulay (Formerly Instone)* [1974] 1 WLR 1308. See Michael J. Trebilcock, 'The Doctrine of Inequality of Bargaining Power: Post-Benthamite Economics in the House of Lords' (1976) 26 U. Toronto L.J. 359, 369-384.

⁷⁴ Grinover and others (n 34) 570.

⁷⁵ Vidal Serrano Nunes Júnior and Yolanda A. P. S. De Matos, *Código de Defesa do Consumidor Interpretado* (4th edn, Saraiva 2009) 231.

⁷⁶ See reg. 5(1) of the UTCCR 1999. Such definition will be analysed in more detail in chapter 3.

⁷⁷ R Brownsword, G Howells and T Wilhelmsson, 'Between Market and Welfare: Some Reflections on Article 3 of the EC Directive on Unfair Terms in Consumer Contracts' in C Willett (ed) *Aspects of Good Faith* (Blackstone 1995) 30. See also chapter 3 for further details.

The protection of the weak party against the abuse of the unequal bargaining power is also the basis of the doctrine of *unconscionability* which allows English courts to protect parties from procedural unfairness through the application of concepts such as duress, undue influence and misrepresentation (they are however outside the scope of the present study).⁷⁸

Exemption clauses may be also regarded as unfair if they were included in a contract where parties had no equal bargaining strength. They are defined as terms which purport to exclude or limit liability and may 'undermine or totally defeat the innocent's party's expectations by depriving him of compensation for loss caused by the other party's breach'.⁷⁹ Consequently they are subject to legislative control and can be rendered unenforceable by UCTA and UTCCR 1999 even if they were incorporated as a term and covered the loss in question, as will be seen in chapters 2 and 3. This control is also justified by the fact that 'rights and duties under a contract cannot be considered evenly balanced unless both parties are equally bound by their obligations' according to the Office of Fair Trading.⁸⁰

1.4. Good faith

This work will also make recurrent references to *good faith*. Brownsword suggested that this concept can be considered an eminently appropriate topic for a comparative study because it 'takes us right to the heart of contract law' as it tackles the ethics that govern the way that contracting parties 'should relate to one another'.⁸¹ Indeed in the context of this work good faith will underline fundamental differences between the Brazilian and English law.

Good faith is an 'elusive' concept to define as it can assume various meanings in different legal systems and types of contracts,⁸² thus 'juristic views on and the legal conceptualization of the idea of good faith may often vary across the cultural divides and

⁷⁸ Jill Poole, *Textbook on Contract Law* (11th edn, Oxford University Press 2012) 574-578.

⁷⁹ Chen-Wishart (n 3) 448.

⁸⁰ Office of Fair Trading, *Unfair Contract Terms Guidance* (September 2008) 13-14.

⁸¹ Roger Brownsword, 'Individualism, Cooperativism and an Ethic for European Contract Law' (2001) 64(4) MLR 628, 630.

⁸² Pedro Barasnevičius Quagliato, 'The Duty to Negotiate in Good Faith' (2008) 50(5) International Journal of Law and Management 213, 215. Cordero-Moss observed that 'there is no uniform notion of good faith and fair dealing that might be valid for all types of contracts on an international level'. See Giuditta Cordero-Moss, 'International Contracts between Common Law and Civil Law: is Non-state Law to be Preferred? The Difficulty of Interpreting Legal Standards Such as Good Faith' (2007) Global Jurist (Advances) 1, 30.

legal traditions'.⁸³ Nonetheless, it is generally linked to the idea of honesty, loyalty and trust.⁸⁴ This concept was originated in Roman law as *bona fides* and since then it has been incorporated in various legal systems.⁸⁵

In the context of contract law, good faith is applied in two different senses: *subjective* and *objective*.⁸⁶ The *subjective* good faith can be described as 'a requirement of morality in its intentional or psychological aspect' to act in an honest and fair manner.⁸⁷ It is based on the belief or will of a party to behave in conformity with the law even when the assumption is mistaken.⁸⁸ For instance, a person may act in subjective good faith if he believes that his behaviour is legal and moral and he is unaware that he may be harming other people's rights.⁸⁹

There are however objections to this subjective conception of good faith due to the difficulties in verifying the true intentions of the party. Additionally 'a moral interpretation of good faith may be open to criticism because prescribed outcomes are implausible or uncertain'.⁹⁰

Consequently the *objective* good faith is arguably more in line with the need of *predictability* and *certainty* of contracts as it is the behaviour of a person and other external aspects that are evaluated, independently of his opinion or psychological aspects.⁹¹ It is described as a social archetype or legal standard that each person should

⁸³ Lorena Carvajal-Arenas and A F M Maniruzzaman, 'Cooperation as Philosophical Foundation of Good Faith in International Business-Contracting: A View Through the Prism of Transnational Law' <http://ouclf.iuscomp.org/articles/carvajal_maniruzzaman.shtml> accessed 05 July 2012.

⁸⁴ A duty of good faith 'will generally embrace: (1) a duty to act honestly and (2) a duty to have regard to the legitimate interests of the other party'. See Michael Furmston, Takao Norisada and Jill Poole, *Contract Formation and Letters of Intent: A Comparative Assessment* (John Wiley & Sons 1998) 274.

⁸⁵ 'Good faith' comes from the Latin *fides* which means: trust; promise of safe conduct; fulfilment of a promise; certainty, the true meaning. See P. G. W. Glare, *Oxford Latin Dictionary* (Oxford University Press 1982) 697-698. *Bona fides* in its turn means: honesty, honour; to observe one's obligations, sincerity; sense of duty towards others, loyalty, allegiance, to remain loyal. See Michiel De Vaan, *Etymological Dictionary of Latin: And the Other Italic Languages* (Leiden Indo-European Etymological Dictionary Series, Brill 2008) 218.

⁸⁶ The distinction between objective ('Treu und Glauben') and subjective ('Gutter Glauben') good faith can be found in the German Civil Code (BGB of 1900). Powell observed that English contract law has cases that contain elements of subjective or objective good faith but there is no overriding requirement of good faith. Raphael Powell, 'Good Faith in Contracts' (1956) 9 CLP 16, 23-24. See also Roger Brownsword, 'Good Faith in Contracts Revisited' (1996) 49 CLP 111, 116.

⁸⁷ Francois Dienes, 'The Requirement of Contractual Co-operation in International Trade' (1999) 7 IBLJ 737, 763.

⁸⁸ Miguel Reale, 'A Boa-Fé no Código Civil' <<http://www.miguelreale.com.br/index.html>> accessed 30 December 2010.

⁸⁹ Edilson Pereira Nobre Júnior, 'O Princípio da Boa-Fé e o Novo Código Civil' (2003) Rio de Janeiro, maio/jun, v. 99, f. 367 Revista Forense 69, 74.

⁹⁰ Brownsword, 'Good Faith in Contracts Revisited' (n 86) 143-144.

⁹¹ José Roberto Castro Neves, 'Boa-fé Objetiva: Posição Atual no Ordenamento Jurídico e Perspectivas de sua Aplicação nas Relações Contratuais' (2000) Rio de Janeiro, jul./set, v. 96, f. 351 Revista Forense 161, 161.

fit in order to act with honesty, probity and loyalty.⁹² Therefore the objective good faith as a model of conduct is preferable to the subjective one because it can be objectively assessed by courts and parties; hence it is the one adopted by the English and Brazilian law. It requires negative and positive behaviours as parties should refrain from acting dishonestly; at the same time that they should act cooperatively in order to achieve the objective of the contract.⁹³

1.4.1. Good faith in negotiation, performance and enforcement

Another fundamental classification involving good faith is based on the contractual stage in which this concept is applied: *negotiation*, *performance* or *enforcement*. Such application may vary significantly among distinct legal systems.⁹⁴

For instance English law does not recognise a general duty to negotiate in good faith.⁹⁵ According to common law there should not be the imposition of liability before parties are actually bound by a contract even if one party acts in bad faith during the bargaining process.

On the other hand, good faith performance was incorporated into English law through the *Unfair Terms in Consumer Contracts Regulations 1999*. Similarly the American law expressly prescribes the duty of good faith at performance and enforcement stage.⁹⁶ According to this duty parties have to behave with loyalty towards a common purpose that was agreed between them in order to not frustrate the legitimate expectations of the other party. Additionally a duty of good faith at the enforcement stage may be applicable to prevent the 'innocent party' from withdrawing in bad faith from a contract when the other party performs defectively.⁹⁷

⁹² Reale (n 88).

⁹³ Renata Domingues Barbosa Balbino, 'O Princípio da Boa-Fé Objetiva no Novo Código Civil' (2002) São Paulo, v. 22, f. 68 Revista do Advogado 111, 114.

⁹⁴ John Carter and Michael P. Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part I' (1994) 8 JCL 1, 4.

⁹⁵ In principle, 'there is no general rule in Common Law requiring the parties to negotiate in good faith'. See Quagliato (n 82) 217.

⁹⁶ In the words of the Uniform Commercial Code § 1-203 'every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement'. § 1-201 (19) 'good faith' means 'honesty in fact in the conduct or transaction concerned'. Similarly the Restatement (Second) of Contracts prescribes in its §205 that 'every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement'.

⁹⁷ In *Arcos Ltd v EA Ronaasen & Son* [1933] AC 470 (HL) it was discussed whether a party could reject goods because they did not conform to the description in the contract even though they were still merchantable. If the rejection was made not because the goods were not fit for their original purpose but because the buyer

By comparison, in Brazil the principle of good faith is regarded as the 'maximum paradigm for protection in contractual relationships'⁹⁸ and it can be applied at all contractual stages (negotiation, performance and enforcement). In this jurisdiction a party has to exercise his rights within the limits imposed by such general clause, thus good faith must be consistently observed.⁹⁹

Therefore as is the case in most civil law jurisdictions, Brazil recognises an obligation of good faith in negotiations that 'generally provides a remedy for a wrongful conduct produced by a bad faith act' through the application of the *culpa in contrahendo* doctrine.¹⁰⁰ On the other hand, the principle of good faith in the performance of the contract is expressly prescribed by the Civil Code.¹⁰¹

The application of good faith at the enforcement stage in its turn can be inferred from the interpretation of the principles of contractual balance and trust that are prescribed by the Consumer Protection Code.¹⁰² They provide some leeway to judges decide on the fairness of parties' relationships and whether the enforcement has been in accordance to parties' reasonable expectations.¹⁰³

1.4.2. Common roots of good faith

The civil law tradition had its origin in Roman law and it was in the latter that the concept of good faith as a model of conduct was established.¹⁰⁴ Therefore when the civilian system was disseminated to countries of Continental Western Europe and later to their colonies throughout the world, so did its fundamental concepts.¹⁰⁵

wanted to get a better deal due to changes in the market; then the supplier should be entitled to some protection to his reasonable expectations (although this was not the understanding of the House of Lords in that case).

⁹⁸ Alinne Arquette Leite Novais, 'O Princípio da Boa-Fé e a Execução Contratual' (2001) São Paulo, dez, v. 90, f. 794 Revista dos Tribunais 56, 71.

⁹⁹ Article 187 of the Civil Code.

¹⁰⁰ Quagliato (n 82) 213.

¹⁰¹ Article 422 of the Civil Code.

¹⁰² See article 4, III of the Consumer Protection Code. In addition article 42 and sole paragraph of the same Code provides another example of good faith enforcement when it determines that in the collection of debts, the debtor shall not be exposed to ridicule, nor subjected to any constraint or threat. If the creditor charges the consumer a debt that he does not own he will be behaving in bad faith.

¹⁰³ Novais (n 98) 71-73. See also chapter 3 for good faith at post-contractual stage.

¹⁰⁴ Neves (n 91) 161.

¹⁰⁵ According to David, civil law is a subgroup of the *Western law* which was developed from the Roman law. See David, *Major Legal Systems in the World Today* (n 17) 35.

As a former Portuguese colony, Brazil had its legal foundation based on European law, which continues to influence its legislative development until the present time. As a consequence Brazilian law contains various concepts and principles inherited from Roman law and from the legislation of European countries (e.g., good faith was derived from the German law).¹⁰⁶

On the other hand, the development of the English law started during the Anglo-Norman period (1066 AC) and since then it has been shaped by historical events and local customs of this country which resulted in an autonomous legal system called *common law*.¹⁰⁷ The latter has spread across most English-speaking countries and members of the Commonwealth.¹⁰⁸

However, since the UK became a member of the European Union, the English law has been influenced by the EU law, which in its turn has been greatly influenced by civil law which is the legal system adopted by the vast majority of its Members States. For instance, the *Directive on Unfair Terms in Consumer Contracts* (93/13/EEC) adopted the concept of good faith as a result of the influence exerted by the EU civilian jurisdictions, notably the German law.¹⁰⁹ Youngs remarked that this directive is 'an interesting example of European law forming a bridge by which an area of law from one system (the concept of good faith under §242 of the BGB (...)) becomes part of others'.¹¹⁰ Nevertheless the incorporation of this concept in England has not been as straightforward as in most EU Member States.

Therefore it is possible to conclude that the concept of good faith applied in both England and Brazil has its roots in *German law* (which was inspired by Roman law).¹¹¹ For this

¹⁰⁶ See Grinover and others (n 34) 535-536 and 570.

¹⁰⁷ See Zweigert and Kötz (n 48) 181-182. Despite the fact that England was under the control of the Romans for about four centuries in the past (43 AD - 410 AD) this country did not incorporate the Roman law, but instead it developed its own legal system over the next centuries.

¹⁰⁸ David, *Major Legal Systems in the World Today* (n 17) 351.

¹⁰⁹ The Directive on Unfair Terms in Consumer Contracts (93/13/EEC) was greatly influenced by the German Standard Contract Terms Act (AGB-Gesetz). Although this statute was repealed and replaced by §§ 305 et seq. of the German Civil Code (BGB) in 2002, the latter maintained the application of good faith in the context of pre-formulated standard contracts. See Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 3.60.

¹¹⁰ Raymond Youngs, *English, French and German Comparative Law* (2nd edn, Routledge-Cavendish 2007) 622-623.

¹¹¹ See chapter 3. According to Collins one of the approaches 'towards interpretation of the Directive could draw upon the traditional conceptions of good faith in contract law in civil law systems, particularly from German law, but ultimately from the Roman Law roots'. See Hugh Collins, 'Good Faith in European Contract Law' (1994) 14(2) OJLS 229, 250.

reason, a comparative study of the application of 'good faith' in the Brazilian law may assist a greater understanding of its meaning and scope in English law.

1.5. Background and underpinning theories

The understanding of *why* and *how* the regimes that govern B2B and B2C contracts were developed in the present way will require the examination of their underpinning contract law theories as well as of the social and economic background which influenced such development.

The law of contract reflects the prevailing 'politico-economic philosophy' and values of a particular society in a certain time.¹¹² 'Law is embedded within society, and society oozes into law through every pore'.¹¹³ Consequently social changes (e.g., industrialisation) have shaped the development of contract law which has moved from a *classical* model to a *modern* approach.

The *classical* contract theory was developed in the eighteenth and nineteenth centuries when the individualist philosophy of *laissez faire* prevailed.¹¹⁴ At the heart of this theory were the freedom of contract and the adversarial ethic according to which parties have the autonomy to negotiate terms in conformity with their will and the pursuance of their self-interest. Contractual parties were assumed to have equal or equivalent bargaining strength and the capability to protect their own interests. In this context courts should not influence or adjust terms agreed by parties even if they were unfair. However they were supposed to enforce those terms according to parties' intentions¹¹⁵ as well as to prevent procedural unfairness (e.g. fraud, undue influence) that could interfere with the voluntariness of consent.¹¹⁶

A number of countries with industrialised economies, including England and Brazil, had this approach in relation to contracts changed significantly with the major economic

¹¹² Poole, *Textbook on Contract Law* (n 78) 3.

¹¹³ Brian Z. Tamanaha, *Beyond the Formalist-Realist Divide: The Role of Politics in Judging* (Princeton University Press 2009).

¹¹⁴ According to Friedman the doctrine of the *laissez faire* means that 'interference of government in business and economic affairs should be minimal. Adam Smith's *The Wealth of Nations* (1776) described *laissez-faire* economics in terms of an INVISIBLE HAND that would provide for the maximum good for all, if businessmen were free to pursue profitable opportunities as they saw them'. See Jack P. Friedman, *Dictionary of Business Terms* (3rd edn, Barron's Educational Series, Inc. 2000) 372.

¹¹⁵ Patrick S. Atiyah, *The Rise and Fall of Freedom of Contract* (Clarendon Press 1979) 681. See also *The Moorcock* (1889) 14 PD 64 (CA), 70.

¹¹⁶ Hugh Collins, *The Law of Contract* (4th edn, Butterworths 2003) 271.

transformations caused by the development of the modern mass production and the consumption in large scale. In order to offer products and services to an indeterminate number of people, suppliers started to make use of *standard form contracts* as individual agreements became impractical.¹¹⁷ Although those 'contracts of adhesion' are not pernicious *per se*, they have facilitated the inclusion of exemption clauses and unfair terms.¹¹⁸ They have also aggravated the *inequality of bargaining power* between parties because the dominant party often drafts terms in advance and do not leave room for negotiation.¹¹⁹ Moreover in some trades the standard form contracts of most sellers and suppliers show little variation among them, thus the options available to the weak party are very limited and their freedom of choice is merely apparent.¹²⁰

In the twentieth century those imbalances led to the recognition of the need of a more interventionist approach in bargains to prevent unfairness and abuses in contracts where one party is vulnerable in relation to the other.¹²¹ The classical contract law became inadequate to regulate relationships in which parties do not share equal resources, because in the absence of economic equality the freedom of contract 'can be merely the recipe for exploitation and injustice'.¹²²

Consequently the classical principle that terms of contracts are determined by parties and only they can modify or suppress such terms is now limited by legislation.¹²³ The classical

¹¹⁷ This *standardisation* is 'an unavoidable result of the economic relations because it works as a decisive factor of the rationalisation and economy of the business activity and enable the celerity, security and stability of the market relations'. See Rosalice Fidalgo Pinheiro, 'Boa-fé e Equilíbrio na Interpretação dos Contratos de Consumo' (2007) Rio de Janeiro, mar./abr, v. 103, f. 390 Revista Forense 161, 163

¹¹⁸ 'Standard form contracts' are also known as 'contracts of adhesion' because they are unilaterally determined by one of the parties and there is no room for negotiation; therefore in order to conclude the contract the other party has to adhere to the imposed terms. See Grinover and others (n 34) 528-529.

¹¹⁹ Inequality of bargaining power is defined by Beale as 'ignorance, vulnerability to persuasion, desperate need, lack of bargaining skill or simple lack of influence in the market place'. Hugh Beale, 'Inequality of Bargaining Power' (1986) 6(1) OJLS 123, 125.

¹²⁰ Paolisa Nebbia, 'Standard Form Contracts between Unfair Terms Control and Competition Law' (2006) 31 EL Rev 102, 103. Lord Diplock observed in *Schroeder Music Publishing Co. Ltd. v Macaulay (Formerly Instone)* [1974] 1 WLR 1308, 1316 that as a 'result of the concentration of particular kinds of business in relatively few hands' the stronger party may include harsh terms in standard form contracts leaving the weak party with the limited option of 'take it or leave it'.

¹²¹ '(...) Freedom of contract is no longer the sole paradigm of Contract Law. In the 20th century, it has gained the company of an opposing paradigm, that of protecting the weak party'. See Ewoud Hondius, 'The Protection of the Weaker Party in a Harmonised European Contract Law: A Synthesis' (2004) 27(3) JCP 245, 246. This prompted the enactment of legislative acts such as the Consumer Credit Act 1974 (as amended) and the UCTA 1977. In Brazil its Civil Code provides general rules applied to civil and business contracts that impose limits to the freedom of contract in order to avoid unfairness. Moreover, the Consumer Protection Code contains provisions against 'abusive clauses'. At European level, the EU issued directives (e.g., Directive on Unfair Terms in Consumer Contracts and Doorstep Selling Directive) that aimed to protect consumers within the common market through the use of minimum harmonisation clauses.

¹²² Koffman and Macdonald (n 1) 5.

¹²³ Orlando Gomes, *Contratos* (18th edn, Forense 1998) 22-25.

theory was superseded by a *collective theory* of contract according to which the will of the parties is no longer the main source of judicial interpretation.¹²⁴ Courts should take into account the social interests and collective values involved as well as the *reasonable expectations* of the parties, especially of the weaker party.¹²⁵

Furthermore ideas such as inequality of bargaining power, reasonableness, unconscionability and good faith have been introduced to give effect to a more interventionist approach in the *modern* law of contract. It does not mean that the latter has rejected the freedom of contract and other classical principles altogether. They are still in place where parties have equivalent bargaining power, thus they are applicable to B2B contracts where parties are able to negotiate terms. Courts will only intervene in the absence of such balance between business parties as in *Motours Ltd v Euroball (West Kent) Ltd*¹²⁶ where non-negotiated terms were imposed by a dominating business in a standard form contract. Such imbalance often can be found in small businesses contracts because SMEs are usually weaker in the face of large businesses.

A more recent theory advocated by Adams and Brownsword incorporated the previous theories and proposed a framework to be used by interpreters of contract law.¹²⁷ Such framework can be efficiently applied to explain the different approaches employed in the context of B2C and B2B contracts;¹²⁸ thus the present work will make constant references to this theory in order to illustrate the distinctions between those types of contracts.

According to this framework there are two competing judicial ideologies, *Formalism* and *Realism*, that reflect the different attitudes of judges towards the application of the so-called 'rule book'.¹²⁹ Formalists apply the rule-book material without questioning it even if

¹²⁴ See Poole, *Textbook on Contract Law* (n 78) 8-9.

¹²⁵ Claudia Lima Marques, 'Notas sobre o Sistema de Proibição de Cláusulas Abusivas no Código Brasileiro de Defesa Do Consumidor: Entre a Tradicional Permeabilidade da Ordem Jurídica e o Futuro Pós-Moderno do Direito Comparado' (2000) Porto Alegre, fev, v. 47, f. 268 *Revista Jurídica* 39, 60. According to this *collective theory* the expectations of a party reasonably held should be protected irrespectively of the other party's will. See Johan Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 *LQR* 433, 442.

¹²⁶ [2003] EWHC 614 (QB), [2003] All ER (D) 165.

¹²⁷ Roger Brownsword and John N. Adams, 'The Ideologies of Contract' (1987) 7 *LS* 205, 205. See also Roger Brownsword, *Contract Law: Themes for the Twenty-first Century* (2nd edn, Oxford University Press 2006) and Roger Brownsword and John N. Adams, *Understanding Contract Law* (5th edn, Sweet & Maxwell 2007).

¹²⁸ It can also explain some differences between civil law (more formalist) and common law (more realist).

¹²⁹ 'Rule book' is a general term that refers to the traditional texts considered collectively that equates the study of law to the study of legal terms ('black-letter approach'). See Brownsword and Adams, *Understanding Contract Law* (n 127) 3-4. Brownsword and Adams, 'The Ideologies of Contract' (n 127) 213.

the result is inadequate or unfair;¹³⁰ whereas realists consider the fairness of the result more important than the simple application of the rule-book.¹³¹

It is possible to argue that the Brazilian law tends to adopt a more *formalist* approach because civilian jurisdictions normally consider their respective legal systems complete and comprehensive;¹³² thus judges are in principle limited to the application of the legislator's will and should not make new law.¹³³ This is in line with the 'principle of separation of powers' that prescribes that the Legislative, Executive and Judicial powers are independent and harmonious; consequently each power should be limited to its own function.¹³⁴ Nonetheless the Brazilian legislation prescribes general clauses (e.g., good faith) that mitigate such formalism and allows some flexibility to judges to make decisions according to their understanding of fairness in individual cases.

By comparison in England 'most modern judges tend to adopt a *realist* approach'¹³⁵ and courts may apply equity when the application of rules leads to an unsatisfactory or harsh decision. Atiyah argued that there is a willingness of courts to pursue an individualised justice which may favour judicial discretion over legal rules,¹³⁶ but Tamanaha observed that this discretion is still delimited by law.¹³⁷

Such realist approach is underpinned by the following contractual ideologies: *consumer-welfarism* and *market-individualism*. The *consumer-welfarism* ideology is more

¹³⁰ In *Butler Machine Tool Co v Ex-cell-o Corp (England)* [1979] 1 WLR 401, 405 Lawton LJ maintained in a discussion concerning the 'battle of the forms' that 'in my judgment, the battle has to be conducted in accordance with set rules'.

¹³¹ According to Devlin LJ 'the true spirit of the common law is to override theoretical distinctions when they stand in the way of doing practical justice.' See *Ingram v Little* [1961] 1 QB 31 (CA), 73.

¹³² David, *Major Legal Systems in the World Today* (n 17) 111-112.

¹³³ Tamanaha observed that formalist jurists 'believed that the law was comprehensive and logically ordered, and in new situations judges *did not make law* (even when declaring new rules) but merely discovered and applied preexisting law.' See Tamanaha (n 113) 13. Similarly Reeves added that 'it is not the court's place in the system of governance to develop the standards and policies that are to guide a state's behavior'. Anthony R. Reeves, 'Do Judges have an Obligation to Enforce the Law? Moral Responsibility and Judicial Reasoning' (2010) 29(2) *Law & Phil* 159, 165.

¹³⁴ The *separation of powers* is expressly prescribed by article 2 of the Brazilian Federal Constitution. Nevertheless the latter adopted the American doctrine of 'check and balances' according to which the independence of the powers is not absolute and there is a mutual interference among them that aim to control the exercise of their functions in order to prevent abuses and arbitrariness. See Alexandre Moraes, *Direito Constitucional* (13th edn, Atlas 2003) 187.

¹³⁵ Poole, *Textbook on Contract Law* (n 78) 10.

¹³⁶ Atiyah observed that many decisions made in the early 19th century may appear unjust because courts applied general rules to different situations irrespectively of their adequacy to the facts. See Patrick S. Atiyah, 'From Principles to Pragmatism: Changes in the Function of the Judicial Process and the Law' (1980) 65 *Iowa L Rev* 1249, 1252-1255.

¹³⁷ This is what Tamanaha calls *balanced realism* because 'skeptical realism promotes the equally unrealistic opposite image of human judges pursuing their personal preferences'. See Tamanaha (n 113) 194-195.

interventionist and prevails in the context of consumer contracts. According to this approach B2C contracts should be closely regulated to protect consumers from being exploited by a stronger party (seller or supplier) as a result of the inequality of bargaining power. In line with this ideology, unjust enrichment and bad faith are not tolerated whereas the protection of the reasonable expectations of the parties should be observed.¹³⁸ Overall consumer-welfarism is more flexible than the market-individualism and promotes the application of the principles of reasonableness and fairness that can be found in UCTA and the UTCCR 1999 respectively.

The *market-individualism* in its turn is the prevailing ideology in the context of B2B contracts. According to it the main purpose of a contract is to facilitate 'competitive exchange'; thus commercial practice should be taken into account and restrictions should be minimal and clearly defined.¹³⁹ Furthermore while on one hand parties are free to choose their partners and terms, on the other hand they should be held to their bargains (principles of freedom of contract and 'sanctity of contracts').¹⁴⁰ In other words, as long as agreements are freely negotiated, courts can legally enforce them for the sake of the stability of the market. However apart from enforcing agreed terms, judicial interferences should be kept to a minimum and courts should give effect to the intentions of the parties.

There are two types of market-individualism: '*static*' and '*dynamic*'. The *static market-individualism* is underpinned by an individualist ethic which is based on the idea that one party can pursue his own interests in disregard of the other party's interests and there are hardly any excuses for the non-performance.¹⁴¹ The restrictions imposed on parties are limited to the prohibition of fraud and coercion that can undermine the reality of consent and affect the freedom of contract.¹⁴²

It is in line with the *classical* model, thus the function of contract law is to provide a framework where parties can freely agree their exchanges and maximise their individual utility. The *adversarial* ethic is still present in the English contract law especially in contracts between businesses parties and it was used as argument in *Walford v Miles*¹⁴³

¹³⁸ Brownsword and Adams, 'The Ideologies of Contract' (n 127) 210-213.

¹³⁹ Ibid. 206-210.

¹⁴⁰ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 50-53.

¹⁴¹ Ibid. 139.

¹⁴² Ibid. 143.

¹⁴³ [1992] 2 AC 128.

for the rejection of the application of a duty to negotiate in good faith in a B2B contract.¹⁴⁴ In the Brazilian law however this individualist ethic is mitigated by the application of the principles of the social function of the contracts and good faith which are applicable to contracts in general.¹⁴⁵

Additionally according to the static market-individualism the main function of the law of contract is to establish 'ground rules' to the market operation 'in such a way that all those who deal in the contract-constituted market place know exactly where they stand'.¹⁴⁶ It therefore promotes *certainty* in agreements, which is essential to B2B contracts where parties can freely negotiate terms in relatively equal conditions; hence it can still be found in English law in such a case.¹⁴⁷

Nevertheless the application of the *static* market-individualism approach may have harsh results. For instance courts may have to employ a literal interpretation of the terms which may not reflect the reasonable expectations of the parties according to the circumstances. Consequently a more flexible approach adopted by the *dynamic* market-individualism may adapt better to 'the practice and expectations of the contracting community' that are susceptible to constant changes.¹⁴⁸ Case law has shown that courts have made decisions that are more consistent with the dynamic market-individualism than the static,¹⁴⁹ such as in *Investors Compensation Scheme Ltd v West Bromwich Building Society (No.1)*¹⁵⁰ and *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd*¹⁵¹ where the House of Lords

¹⁴⁴ 'The concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations'. *Walford v Miles* [1992] 2 AC 128 138.

¹⁴⁵ See article 421 of the Civil Code.

¹⁴⁶ The ground rules are: a) contract comes into existence when terms were fully specified and freely agreed upon; b) only parties can be benefited/ burdened by its terms; c) the innocent party's expectation of performance is protected in case of breach. See Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 139.

¹⁴⁷ *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827 (HL).

¹⁴⁸ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 138.

¹⁴⁹ In *Blackpool and Fylde Aero Club v Blackpool BC* [1990] 1 WLR 1195 (CA) the Court of Appeal offered some protection to the plaintiff before the conclusion of a contract. In *Darlington Borough Council v Wiltshier Northern Ltd* [1995] 1 WLR 68 the same court accepted that third parties may recover damages in some situations.

¹⁵⁰ Jill Poole, *Casebook on Contract Law* (11th edn, Oxford University Press 2012) 237-238. The contextual interpretation ascertains 'the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract'. See *Investors Compensation Scheme Ltd v West Bromwich Building Society (No.1)* [1998] 1 WLR 896, 912.

¹⁵¹ [1997] AC 749, [1997] 2 WLR 945.

interpreted the words of the contract 'in a way that a reasonable commercial person would construe them'.¹⁵²

Dynamic market-individualism therefore is in line with a more *cooperativist ethic* according to which parties are expected to take into account the other party's interests and to share unforeseen risks.¹⁵³ There are limits to the pursuit of self-interest and parties are expected to act in accordance with *good faith and fair dealing*.¹⁵⁴ This approach can be expressly found in European initiatives such as *Principles of International Commercial Contracts* (PICC),¹⁵⁵ *Principles of European Contract Law* (PECL),¹⁵⁶ *Draft of Common Frame of Reference* (DCFR)¹⁵⁷ and more recently in the *Common European Sales Law* (CESL).¹⁵⁸¹⁵⁹

Brownsword suggested that the replacement of the classical adversarial ethic by an ethic of cooperation, through the adoption of a good faith regime, would allow the protection of contractors at all stages of the contracting process against exploitation and opportunism.¹⁶⁰ For this reason English law may benefit from the adoption of a general principle of good faith as a way to prevent unfairness in contracts including at the negotiation stage. The Brazilian law may serve as a good example of a legal system which has successfully applied this overriding principle in B2B and B2C contracts.

It is possible to argue that this cooperativist ethic of the *dynamic market-individualism* may have approximated the approach adopted in the context of B2B contracts with the approach applied in B2C contracts (consumer-welfarism) as both reject bad faith and the individualist ethic. Consequently both types of contracts may have an inclination to

¹⁵² See *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749, [1997] 2 WLR 945, 771. *Bank of Credit and Commerce International SA (In Liquidation) v Ali (No.1)* [2001] UKHL 8, [2002] 1 AC 251, [2001] 2 WLR 735 also adopted a contextual interpretation.

¹⁵³ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 67.

¹⁵⁴ *Ibid.* 143.

¹⁵⁵ See article 1.7 of PICC.

¹⁵⁶ See articles 1:102, 1:201, 1:305, 2:301, 4:110 of PECL. The application of such cooperativist ethic has been expressly prescribed in article 1:202 which says 'each party owes to the other a duty to co-operate in order to give full effect to the contract'.

¹⁵⁷ See articles I. – 1:103, II. – 1:102 of the DCFR.

¹⁵⁸ See articles 2(b) 83 and 86 of the CESL.

¹⁵⁹ These Principles do not have the binding force of either national law or international treaties or conventions (they are so-called 'soft law'). See Cristiano Pettinelli, 'Good Faith in Contract Law: Two Paths, Two Systems, The Need for Harmonisation' <<http://www.diritto.it/docs/20772-good-faith-in-contract-law-two-paths-two-systems-the-need-for-harmonisation>> accessed 15 February 2012.

¹⁶⁰ See Brownsword, 'Good Faith in Contracts Revisited' (n 86) 113-139 and Roger Brownsword, 'Two Concepts of Good Faith' (1994) 7 JCL 197. Collins agreed that 'the law must impose certain duties of co-operation in the formation and performance of contracts, which reflect the need to secure reliable and worthwhile opportunities for market exchanges'. See Collins, *The Law of Contract* (n 116) 33.

protect the reasonable expectations of the parties and to promote a more balanced relationship between them. The principle of good faith therefore may be an effective tool to achieve such purposes in the Brazilian and English legal systems.

1.6. Structure of the thesis

The thesis consists on seven chapters. The aim of this introductory chapter is to contextualise the study starting with an overview of the two legal systems involved and the definition of concepts which are fundamental to the topic under analysis (unfair terms, exemption clauses and good faith). It also describes the elected methodology (comparative law) which will guide the research as well as the theories which underpin the study.

The second chapter exams the legislative controls on unfairness in the context of business contracts in the English and Brazilian legal systems. It analyses the relevant legislation in both legal systems separately and then comparatively. In general those contracts are still consistent with the classical law of contract where there is the prevalence of the freedom of contract and the adversarial ethic.

It moves on to the same analysis in chapter 3 but in the context of consumer contracts which reflects the transition from the classical model to the modern law of contract where concepts such as good faith, reasonableness and fairness were incorporated into pieces of legislation and decisions of the courts.

Following the analysis of the topic in the context of B2B contracts and B2C contracts where the relevant legislation is clearly distinct from each other, chapter 4 tackles the protection afforded to small businesses which is in a *grey area* between the other two categories of contracts. Therefore for the purpose of this work, contracts involving SMEs are dealt separately from the other B2B contracts because small businesses do not negotiate in an equal position with large businesses.

Subsequently the study examines in chapter 5 unresolved issues of the legislation and case law analysed in the previous chapters and in chapter 6 it makes an evaluative comparison of the legal solutions offered by the Brazilian and English law systems and proposes lessons that they may learn from each other. Finally the conclusion of the thesis

is dedicated to the contributions of the research and it includes recommendations which can be derived from it.

CHAPTER 2. ANALYSIS OF THE LEGISLATIVE CONTROLS ON UNFAIRNESS IN BUSINESS CONTRACTS IN ENGLAND AND BRAZIL

2.1. Context

Freedom of contract is generally accepted as a principle which governs agreements between parties as long as they are not contrary to the public policy or harmful to the parties' interest.¹⁶¹ This principle prevailed in classical contract law and it is still applicable to businesses contracts where there is the assumption that parties are able to freely negotiate terms and agree with the inclusion of exemption clauses for allocation of risks. The consequences of a B2B contract are determined by the parties' intention, thus courts should avoid interfering with agreed terms even if they are apparently unfair.¹⁶²

In practice however business parties often 'prefer to make practical adjustments or compromises rather than stand on their strict legal rights'.¹⁶³ Such observation is supported by *empirical studies* carried out by Macaulay¹⁶⁴ followed by Beale and Dugdale.¹⁶⁵ They suggested that businessmen are more inclined to recourse to *trade custom* because the latter is more flexible and adaptable to their needs and unforeseen events. Those studies also indicated the prevalence of a *cooperativist ethic* among businesses that wish to maintain long-term commercial dealings. As a consequence the adoption of alternative ways to solve conflicts seemed to be more advantageous than the use of contractual remedies that are generally costly and may damage their reputation.¹⁶⁶

Although parties may opt to not make use of the law of contract to settle disputes between them, they still have to observe the relevant legislation which limits their behaviour. Those restrictions aim to ensure that the weak party will be protected from exploitation in B2B contracts where there is no actual equality between parties. Such

¹⁶¹ According to Brownsword 'term freedom' can be limited when it is harmful to the interest of: a third party, one or both contracting parties or to the public interest. See Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 52.

¹⁶² Atiyah, *The Rise and Fall of Freedom of Contract* (n 115) 681. See also *The Moorcock* (1889) LR 14 PD 64 (CA) 70.

¹⁶³ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 4.

¹⁶⁴ Stewart Macaulay, 'Non-Contractual Relations in Business: A Preliminary Study' (1963) 28 *Am Sociolog Rev* 55.

¹⁶⁵ Hugh Beale and Tony Dugdale, 'Contracts between Businessmen: Planning and the Use of Contractual Remedies' (1975) 2 *Brit J Law & Soc* 45.

¹⁶⁶ 'You don't read legalistic contract clauses at each other if you ever want to do business again'. See Macaulay (n 164) 61. According to Atiyah there are 'many bilateral long-term relationships' which tend increasingly to 'regulate their internal arrangements without the aid of contract'. See Atiyah, *The Rise and Fall of Freedom of Contract* (n 115) 724.

protection will therefore be particularly important to small businesses that are generally more vulnerable in the market, as will be examined in chapter 4.

2.2. Legislative control on unfairness in business contracts in England

In England, in the mid twentieth century, the recognition of the need for *intervention* in contracts conflicted with the *classical* view which was until then the prevailing approach. The latter embraced ideas such as freedom of contract and 'calculability of risk allocation' in business contracts;¹⁶⁷ moreover parties could pursue their self-interest even if it harmed the other's party interests.¹⁶⁸

Therefore although in *Suisse Atlantique Société d'Armement Maritime S.A. v N.V. Rotterdamsche Kolen Centrale*¹⁶⁹ the House of Lords still maintained the importance of the freedom of contract and the observance of the parties' intentions, in subsequent years the increasing pressure on controlling contractual relationships resulted in the enactment of the Unfair Contract Terms Act 1977.¹⁷⁰ This Act 'aimed at bridging the recognised gap between the classical theory of contract law and the social reality'.¹⁷¹ UCTA declares invalid certain provisions independently whether they were freely agreed or whether the protected party preferred to decline such protection in exchange for better prices or conditions. Its scope however is limited to the regulation of exemption clauses that are inserted in B2B and B2C contracts.¹⁷²

¹⁶⁷ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 59-60.

¹⁶⁸ For instance Lord Cockburn remarked that 'the question is not what a man of scrupulous morality or nice honour would do under such circumstances. The case put of the purchase of an estate, in which there is a mine under the surface, but the fact is unknown to the seller, is one in which a man of tender conscience or high honour would be unwilling to take advantage of the ignorance of the seller; but there can be no doubt that the contract for the sale of the estate would be binding'. See *Smith v Hughes* (1871) LR 6 QB 597 , 603-604.

¹⁶⁹ 'In my view, it is not right to say that the law prohibits and nullifies a clause exempting or limiting liability for a fundamental breach or breach of a fundamental term. Such a rule of law would involve a restriction on freedom of contract (...)'. See *Suisse Atlantique Société d'Armement Maritime S.A. v N.V. Rotterdamsche Kolen Centrale* [1967] 1 AC 361 , 392.

¹⁷⁰ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 60-61.

¹⁷¹ Hugh Beale, 'Unfair Contract Terms Act 1977 [comments]' (1978) 5 Brit J Law & Soc 114, 114.

¹⁷² *Exemption clauses* include *exclusion clauses* (that purport to exclude liability or remedies) and *limitation clauses* (that purport to limit the liabilities or remedies). S. 13(1) of UCTA contains an extended definition of exemption clauses: '(a) making the liability or its enforcement subject to restrictive or onerous conditions; (b) excluding or restricting any right or remedy in respect of the liability, or subjecting a person to any prejudice in consequence of his pursuing any such right or remedy; (c) excluding or restricting rules of evidence or procedure; and (to that extent) sections 2 and 5 to 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.'

Businesses are protected by this Act when they contract on the other party's *written standard terms* (section 3).¹⁷³ In this case interventions may be justified by the fact that parties usually are unable to freely negotiate terms which are drafted in advance and imposed on the weaker party. Nonetheless as UCTA does not define 'standard form contract' courts were left with the onerous task of interpreting its meaning and determining its application.¹⁷⁴ Lord Dunpark in *McCrone v Boots Farm Sales Ltd*¹⁷⁵ maintained that this phrase referred to 'a number of fixed terms or conditions invariably incorporated in contracts'.¹⁷⁶ Similarly in line with *British Fermentation Products Ltd v Compair Reavell Ltd*¹⁷⁷ the application of UCTA to a standard form contract 'would be proof that the model form is invariably or at least usually used by the party in question'.¹⁷⁸

In *Salvage Association v CAP Financial Services Ltd*¹⁷⁹ the court concluded that section 3 was not applicable to a contract that involved a certain degree of negotiation; as compared to *St Albans City & District Council v International Computers Ltd*¹⁸⁰ where the application of this provision was not ruled out when the amendments were not related to relevant exempting terms. *Watford Electronics Limited v Sanderson CFL Limited*¹⁸¹ in its turn added that in order to evaluate whether or not the alterations were substantial, any amendment of terms should be considered against the totality of the standard conditions.¹⁸²

More recently Edwards-Stuart J in *Yuanda (UK) Co Ltd v WW Gear Construction Ltd*¹⁸³ contended that the existence of negotiations is not 'itself a relevant consideration' and concluded that 'if there is any significant difference between the terms proffered and the terms of the contract actually made, then the contract will not have been made on one party's written standard terms of business'.¹⁸⁴

¹⁷³ Steve Wilson and Sheila Bone, 'Businesses, Standard Terms and the Unfair Contract Terms Act 1977' (2002) 1 JO & R 29, 36.

¹⁷⁴ While it is claimed that the phrase 'other party's written standard terms' is considered 'well known' it creates unnecessary uncertainty. See *Ibid.* 38.

¹⁷⁵ 1981 SC 68, 1981 SLT 103.

¹⁷⁶ *McCrone v Boots Farm Sales Ltd* 1981 SC 68, 1981 SLT 103, 74.

¹⁷⁷ [1999] 2 All ER (Comm) 389, [1999] BLR 352.

¹⁷⁸ *British Fermentation Products Ltd v Compair Reavell Ltd* [1999] 2 All ER (Comm) 389, [1999] BLR 352.

¹⁷⁹ *Salvage Association v CAP Financial Services Ltd* [1995] FSR 654.

¹⁸⁰ *St Albans City & District Council v International Computers Ltd* [1996] 4 All ER 481 (CA), [1995] FSR 686.

¹⁸¹ *Watford Electronics Ltd v Sanderson CFL Ltd* [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696.

¹⁸² *Ibid.* [63].

¹⁸³ [2010] EWHC 720 (TCC), [2011] Bus LR 360, [2011] 1 All ER (Comm) 550.

¹⁸⁴ *Yuanda (UK) Co Ltd v WW Gear Construction Ltd* [2010] EWHC 720 (TCC), [2011] Bus LR 360, [2011] 1 All ER (Comm) 550 [26]. In [21] Edwards-Stuart J maintained that 'the conditions have to be standard in that they are terms which the company in question uses for all, or nearly all, of its contracts of a particular type without alteration'.

2.2.1. Exemption clauses

In England the Supply of Goods (Implied Terms) Act 1973 already prescribed that unreasonable exemption clauses could be overridden in the context of implied terms in the sale of goods.¹⁸⁵ Subsequently the Unfair Contract Terms Act 1977 prescribed more general controls on the use of exclusion and limitation clauses that can be applied to a wider range of types of contracts.¹⁸⁶

Presently it is UCTA which offers the main protection against unfairness in the context of B2B contracts.¹⁸⁷ However, as mentioned previously, this Act deals only with *exemption clauses* which are terms which may exclude or limit liability or remedies that 'otherwise would be available for the breach' of a contract by one of the parties.¹⁸⁸

In business contracts those exemption clauses may be employed to assist the allocation of risks between parties; but their application is not free of legislative controls as their misuse may cause an imbalance between parties' rights and obligations. Macdonald suggested that those clauses provide a point in which the 'tension' between freedom of contract and the control of unfairness meet,¹⁸⁹ but 'it is still the case that individually negotiated contracts containing exemption clauses are generally assumed not to be harmful'.¹⁹⁰

Those clauses used to be treated as any other term of contract that defines the parties' obligations¹⁹¹ 'stating the area in which there is no liability and so no obligation'.¹⁹² Nowadays the prevailing approach is that they operate as a *defence to liability*.¹⁹³ The party who purports to rely on the exemption clause has to establish that the clause was

¹⁸⁵ Poole, *Textbook on Contract Law* (n 78) 241.

¹⁸⁶ *Ibid.*

¹⁸⁷ The UTCCR is limited to B2C contracts.

¹⁸⁸ Poole, *Textbook on Contract Law* (n 78) 229.

¹⁸⁹ Elizabeth Macdonald, *Exemption Clauses and Unfair Terms* (2nd edn, Tottel 2006) v.

¹⁹⁰ Poole, *Textbook on Contract Law* (n 78) 232.

¹⁹¹ See Lord Diplock in *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827 (HL), 850.

¹⁹² Macdonald, *Exemption Clauses and Unfair Terms* (n 189) 1.

¹⁹³ Howells and Brownsword suggested that an exclusion clause can have a definitional or exclusionary nature. It is definitional when it assists the specification of the scope of the contractual obligation and exclusionary when there is the derogation from rules (mandatory or default) or from other party's reasonable expectations. Courts have treated exclusion clauses as exclusionary in line with UCTA (See *Phillips Products Ltd v Hyland* [1987] 1 WLR 659) and have rejected the definitional argument 'as an attempted evasion of desirable legal control over unfair terms'. See Geraint G. Howells and Roger Brownsword, 'The Implementation of the EC Directive on Unfair Terms in Consumer Contracts - Some Unresolved Questions' [1995] JBL 243, 248-249.

incorporated as a term of the contract; that on its natural and ordinary meaning it covers the events that have occurred and that the clause was not rendered unenforceable by statutory provisions (UCTA and the Regulations).

The provisions of UCTA do not subject all exemption clauses to review, but only those which purport to exclude or restrict business liability and 'which fall within the compass of ones of its "active sections"'.¹⁹⁴ *Business liability* is the liability for breach of obligations or duties arising 'from things done or to be done by a person in the *course of a business*' or 'from the occupation of premises used for *business purposes* of the occupier' (s. 1(3)). The definition of 'business' here is fairly broad and includes professions and activities of government departments or local or public authority (s. 14).¹⁹⁵

UCTA also does not cover exemption clauses of certain types of contracts which are excluded from its scope, such as: contract of insurance; contracts relating to interest in land, intellectual property, companies or interest in securities; contract for the carriage of goods by ship or hovercraft; contract of employment (except in favour of the employee) and international supply contracts (as is described in s. 26).¹⁹⁶

2.2.1.1. Assessing the reasonableness requirement

UCTA renders certain exemption clauses automatically ineffective whereas other clauses are considered effective only if they satisfy the requirement of 'reasonableness'.¹⁹⁷ Such requirement therefore is not applicable to all sections of the Act, but only where the section prescribes its application (e.g., ss. 3 and 6). The determination of the reasonableness of a term should take into account the circumstances which were known or which could be foreseen by parties when the contract was made (s. 11(1))¹⁹⁸ and the

¹⁹⁴ Macdonald, 'Unifying Unfair Terms Legislation' (n 5) 70. According to Koffman and Macdonald, UCTA has two important types of section. The first one includes the 'active sections' (e.g., ss. 2, 3, 6 and 7) which 'state that a clause is totally ineffective or effective only if it satisfies the requirement of reasonableness'. The second type is the 'definition sections' 'which help to explain the meaning of the terms used within the "active sections" and s. 11'. See Koffman and Macdonald (n 1) 200-201.

¹⁹⁵ For instance, in *St Albans City & District Council v International Computers Ltd* [1995] FSR 686 (QBD), [1996] 4 All ER 481 (CA) a local authority was considered to be a 'business' under the definition of section 14.

¹⁹⁶ See Schedule 1 and s. 26.

¹⁹⁷ Macdonald, 'Unifying Unfair Terms Legislation' (n 5) 70.

¹⁹⁸ Courts should not consider posterior events even in the occurrence of change of circumstances. See Poole, *Textbook on Contract Law* (n 78) 252.

burden of proving the fulfilment of this requirement lies on the party who wants to rely on the exemption (s. 11(5)), which is normally a business.¹⁹⁹

Lord Bridge argued in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd*²⁰⁰ that the reasonableness assessment made by courts is not an 'exercise of discretion',²⁰¹ but the result of a *balancing test* in which a 'whole range of considerations' are weighted in a pair of scales.²⁰² Judges shall therefore take into account factors identified by the *legislation* and *courts*.²⁰³

The factors identified by *legislation* include the provisions of section 11(4) of UCTA which prescribe that in the determination of whether or not a limitation clause satisfies the requirement of reasonableness, courts should consider the resources that the person who wants to rely on the clause could expect to have to meet the liability should it arise and whether that party could have covered himself by insurance for such liability.

Furthermore Schedule 2 provides guidelines for the application of the reasonableness test that encompass:²⁰⁴ the strength of the bargaining power between parties (whether it would be possible to make the contract without the clause); inducement to agree to the clause (e.g., lower price), whether the customer knew or ought to have known the extent of the clause (reality of the consent to the term);²⁰⁵ whether it was reasonable and practicable to expect the compliance of a condition without which the liability would be excluded or limited; and whether goods were made to the customer's special order.

The scope of this Schedule 2 was in principle limited to the context of implied terms in sale and supply contracts (ss. 6 and 7).²⁰⁶ However those guidelines have been extended

¹⁹⁹ By comparison according to the UTCCR 1999 the burden of proof the unfairness normally rests on the consumer (as it will be examined in chapter 3).

²⁰⁰ [1983] 2 AC 803, [1983] QB 284.

²⁰¹ *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803, 815.

²⁰² *Ibid.* 816. Nonetheless as the decisions take into consideration the particularities of each contract, they should not 'be treated as a binding precedent in other cases'. See *Phillips Products Ltd v Hyland* [1987] 1 WLR 659, 668.

²⁰³ Poole, *Textbook on Contract Law* (n 78) 252-260.

²⁰⁴ *Ibid.* 254.

²⁰⁵ 'What the Unfair Contract Terms Act is concerned with, and in particular Sch. 2, para. (a) and (c), is, among other aspects of reasonableness, the actuality or the reality of the consent of the party that it is sought to bind by the particular clause'. See *AEG (UK) Ltd v Logic Resource Ltd* [1996] CLC 265 (CA), 279.

²⁰⁶ See section 11(2). Sections 6 and 7 of UCTA control exemptions in contracts of sale and supply of goods. Although they purport to protect mainly consumers, their provisions can also be applied to businesses. For instance, ss. 6(3) and 7(3) provide that the liability of sellers or suppliers for breaches of implied terms related to the quality of goods cannot be excluded by a contractual term against non-consumers unless the exemption satisfies the requirement of reasonableness. See Chen-Wishart (n 3) 472.

by courts to the assessment of reasonableness of exemption clauses in general.²⁰⁷ From the analysis of their provisions it is possible to argue that if a party was able to freely negotiate terms in equal conditions with the other party, is most likely that the contractual terms will be considered to be reasonable; hence UCTA will be compatible with the freedom of contract as long as the party could give a free and informed consent.

In addition to the above factors determined by legislation in the assessment of reasonableness, there are also factors identified by *courts*. Most case law under UCTA is concerned with B2B contracts rather than B2C agreements.²⁰⁸ Among those cases there are two House of Lords' decisions which used to illustrate different frameworks to the application of *reasonableness* in business contracts.²⁰⁹

In *Photo Production Ltd v Securicor Transport Ltd*²¹⁰ a defendant's employee started a fire while patrolling a factory which resulted in the destruction of the premises, but Securicor was exempted from liability for damages as the House of Lords held effective its exclusion clause. By contrast in *George Mitchell (Chesterhall) Ltd. v Finney Lock Seeds Ltd*²¹¹ the same court concluded that it would not be 'fair and reasonable' to allow a supplier of defective seeds to rely on a limitation clause which limited his liability to the 'replacement or refund of the price' when the whole production was lost.²¹²

The framework adopted in *George Mitchell* can be considered more interventionist as it left the decision regarding the reasonableness of the exemption clause 'entirely to the discretion of the trial judge'.²¹³ Conversely, in *Photo Production* the House of Lords adopted a non-interventionist approach that 'discourages judges from interfering with

²⁰⁷ In the words of Stuart-Smith L.J.: 'section 11(2) of the Act requires the court which is determining the question of reasonableness for the purpose of sections 6 and 7 to have regard in particular to the matters specified in Schedule 2. Although Schedule 2 does not apply in the present case, the considerations there set out are usually regarded as being of general application to the question of reasonableness'. See *Stewart Gill Ltd v Horatio Myer and Co Ltd* [1992] 1 QB 600, 608.

²⁰⁸ Nicky Hartwell, 'The Application of the Reasonableness Test under the UCTA 1977: A Schism between Certainty and Fairness' HLJ <http://www.herts.ac.uk/fms/documents/schools/law/HLJ_V3I2_Hartwell.pdf> accessed 28 May 2011, 55.

²⁰⁹ Roger Brownsword and John N. Adams, 'The Unfair Contract Terms Act: A Decade of Discretion' (1988) 104 LQR 94, 113. See also Brownsword and Adams, *Understanding Contract Law* (n 127) 147-151.

²¹⁰ [1980] AC 827 (HL).

²¹¹ *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803.

²¹² *Ibid.* 816-817.

²¹³ Brownsword and Adams, 'The Unfair Contract Terms Act: A Decade of Discretion' (n 209) 113. Nonetheless Lord Bridge proposed guidelines on the approach to reasonableness in the commercial context: the relative bargaining strength; whether the clause is generally accepted in a particular industry; whether it was negotiated by trade bodies and the availability of insurance cover to the parties. The negligence of the guilty party was also a relevant factor on this case. See *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803, 816-817.

commercial exemptions'.²¹⁴ This latter approach 'has gained prominence in more recent decisions'²¹⁵ such as *Monarch Airlines Ltd v London Luton Airport Ltd*²¹⁶ and *Watford Electronics v Sanderson*²¹⁷ which favoured the freedom of contract between business parties on the grounds that they have equal bargaining power and are able to negotiate terms, allocate risks and opt for an insurance cover.²¹⁸ In other words businessmen were considered to be the 'best judge of the commercial fairness of the agreement'.²¹⁹

Such non-interventionist approach is currently the prevailing one in commercial cases; hence parties who share an equivalent bargaining power may distribute risks through the use of exemption clauses without courts' intervention. Consequently courts will interfere only in cases where unreasonable terms were included in B2B contracts in virtue of the inequality of the bargaining strength (e.g., *Motours Ltd v Euroball (West Kent) Ltd*).²²⁰

2.2.2. Good faith

In line with the non-interventionist approach adopted by English law, there is no general duty of good faith in the context of business contracts,²²¹ because it would be inconsistent with the need of certainty and predictability that those agreements require. Moreover, Bridge contended that this concept is too vague as opposed to other rules of contracts that could serve the same purpose and address more precisely a particular problem taking into account the diversity of commercial contracting.²²²

²¹⁴ Ibid. 95.

²¹⁵ Poole, *Textbook on Contract Law* (n 78) 255.

²¹⁶ [1997] CLC 698.

²¹⁷ [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696.

²¹⁸ Elizabeth Macdonald, 'Watford v Sanderson: The Requirement of Reasonableness in System Supply Contracts and More Generally' Web JCLI <<http://webjcli.ncl.ac.uk/2001/issue4/macdonald4.html>> accessed 25 July 2012.

²¹⁹ In the words of Chadwick LJ in *Watford Electronics Ltd v Sanderson CFL Ltd* [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696 [55]: 'where experienced businessmen representing substantial companies of equal bargaining power negotiate an agreement, they may be taken to have had regard to the matters known to them. They should, in my view be taken to be the best judge of the commercial fairness of the agreement which they have made; including the fairness of each of the terms in that agreement. They should be taken to be the best judge on the question whether the terms of the agreement are reasonable. The court should not assume that either is likely to commit his company to an agreement which he thinks is unfair, or which he thinks includes unreasonable terms., Unless satisfied that one party has, in effect, taken unfair advantage of the other — or that a term is so unreasonable that it cannot properly have been understood or considered — the court should not interfere.'

²²⁰ [2003] EWHC 614 (QB), [2003] All ER (D) 165.

²²¹ Giuditta Cordero Moss, 'Contracts between Consumer Protection and Trade Usages: Some Observations on the Importance of State Contract Law' in R Schulze (ed) *Common Frame of Reference and Existing EC Contract Law* (Sellier 2008) 70.

²²² Bridge contended that a general standard of good faith deflects the attention from the need to deal with different problematic areas of commercial law. See MG Bridge, 'Good Faith in Commercial Contracts' in R Brownsword, N Hird and G Howells (eds), *Good Faith in Contract: Concept and Context* (Ashgate and Dartmouth 1999) (n 221) 140-150. Bridge cited 'commodities contracts' as example of bargains where the

Not surprisingly the traditional view in England is that good faith is also not applicable at negotiation stage in B2B and B2C contracts.²²³ According to common law, parties should not be liable before they are bound by a contract; otherwise it would undermine the parties' freedom to change their minds before the conclusion of the contract. Consequently negotiations in bad faith usually do not give rise to any liability to pay compensation.²²⁴

In accordance with this position the House of Lords in *Walford and Miles*²²⁵ decided that an 'agreement to agree' was unenforceable because 'it lacks the necessary certainty'.²²⁶ This court rejected the argument that there was an *implied* duty to negotiate in good faith for a reasonable period of time.²²⁷ In this case it was neither possible to subjectively determine the existence of 'proper reasons' to terminate the negotiations nor the defendant's bad faith.²²⁸ Lord Ackner stated that:

The concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest (...).²²⁹

His opinion reflected a concern that the 'adoption of a broad duty of good faith would unsettle the commercial bargaining process.'²³⁰ Similarly in *Regalian Properties Plc v London Docklands Development Corp*²³¹ it was held that any expenses incurred in an agreement 'subject to contract' are at a party's own risk because parties should be free to withdraw from negotiations.²³² It therefore rejected the argument of the Australian case

application of good faith would be inappropriate. Parties have to act opportunistically and the participants of the trade should be able to define their own rights and duties. 'There is no room for a co-operative search for a jointly maximised profit'. Ibid. 152.

²²³ See Poole, *Textbook on Contract Law* (n 78) 19. See also Carter and Furmston (n 94) 1.

²²⁴ J Carter and M Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part II' (1995) 8 JCL 93, 117-118.

²²⁵ [1992] 2 AC 128.

²²⁶ *Walford v Miles* [1992] 2 AC 128, 138.

²²⁷ Poole, *Casebook on Contract Law* (n 150) 69-70.

²²⁸ Ibid.

²²⁹ According to Lord Ackner 'a duty to negotiate in good faith is as unworkable in practice as it is inherently inconsistent with the position of a negotiating party. It is here that the uncertainty lies. In my judgment, while negotiations are in existence either party is entitled to withdraw from those negotiations, at any time and for any reason'. See *Walford v Miles* [1992] 2 AC 128 [138].

²³⁰ Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part I' (n 94) 2.

²³¹ [1995] 1 WLR 212. Similarly according to *Stephen Donald Architects Ltd v King* [2003] EWHC 1867 (TCC) and *Carlton Communications Plc v Football League* [2002] EWHC 1650 (Comm) when negotiations are 'subject to contract' parties are not liable in case of withdrawal.

²³² *Regalian Properties Plc v London Docklands Development Corp* [1995] 1 WLR 212, 231.

*Sabemo Pty Ltd v North Sydney Municipal Mutual Council*²³³ which maintained that a party should be protected during negotiations 'if the other party unilaterally decides to abandon the project, not for any reason associated with *bona fide* disagreement concerning the terms of the contract to be entered into (...)'.²³⁴

It may be possible to contend that *Sabemo's* position was in agreement with the *dynamic* market-individualism ideology which takes into account the expectations of the commercial community about legitimate or illegitimate reasons for withdrawal.²³⁵ On the other hand *Walford* and *Regalian* were more in line with the *static* market-individualism ideology; hence they rejected the application of a general duty of good faith in negotiations on the grounds that the latter is contrary to the adversarial ethic. According to them, parties should be able to protect their own interests and prior to the conclusion of the contract they are free to pursue agreements with other people or to break off negotiations at their convenience.

Nonetheless in *Petromec Inc v Petroleo Brasileiro SA Petrobras*²³⁶ the Court of Appeal admitted the application of an *express* provision to negotiate in good faith concerning certain extra costs.²³⁷ In this case there was already a contract in place between two companies and the mentioned provision was considered legally enforceable in order to not frustrate the reasonable expectations of the parties. The good faith obligation here was 'limited in scope, as opposed to an abstract good faith obligation'²³⁸ which was repudiated in *Walford*; consequently the decision in *Petromec* did not recognise a general duty to negotiate in good faith.²³⁹

²³³ [1977] 2 NSWLR 880.

²³⁴ *Sabemo Pty Ltd v North Sydney Municipal Mutual Council* [1977] 2 NSWLR 880, 900-903.

²³⁵ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 151. In line with the dynamic market-individualism the 'reasonableness' of the parties' expectations in B2B contracts can be also determined by the market and not only by law or by terms of contract. In other words 'practice-based expectations are now in head-to-head competition with legal rule-based competition'. See Roger Brownsword, 'Maps, Methodologies, and Critiques: Confessions of a Contract Lawyer' in MV Hoecke (ed) *Methodologies of Legal Research: Which Kind of Method for What Kind of Discipline?* (Hart Publishing 2011) 146-147.

²³⁶ [2005] EWCA Civ 891, [2006] 1 Lloyd's Rep 121.

²³⁷ *Petromec Inc v Petroleo Brasileiro SA Petrobras (No.3)* [2005] EWCA Civ 891, [2006] 1 Lloyd's Rep 121. 'Express terms may, even in the context of contractual negotiations, create a duty to act both honestly and reasonably'. See Michael Furmston and G.J. Tolhurst, *Contract Formation: Law and Practice* (Oxford University Press 2010) 373.

²³⁸ Poole, *Casebook on Contract Law* (n 150) 72.

²³⁹ *Ibid.* 71. The fact that one of the parties was a Brazilian company may have influenced the inclusion of such clause because good faith is commonly applied in agreements in Brazil, including B2B contracts.

The position adopted by *Walford and Miles*²⁴⁰ is still the prevailing one and has influenced subsequent cases such as *BBC Worldwide Ltd v Bee Load Ltd (t/a Archangel Ltd)*.²⁴¹ For this reason, provisions of the *Principles of International Commercial Contracts* (PICC), *Principles of European Contract Law* (PECL) and *Draft Common Frame of Reference* (DCFR) which prescribe the application of good faith and the imposition of liability in pre-contractual dealings appear inconsistent with the English perspective.²⁴² According to the latter, prior to the conclusion of the contract 'expecting that a party also takes into consideration the needs and expectations of the other party runs counter to the very essence of a negotiation'.²⁴³ At this stage parties should be allowed to look for better bargains even if they end up frustrating the other party's expectations.

Notwithstanding English law does not accept good faith in negotiations, it has expressly incorporated this concept in the performance of the contracts through the implementation of Directive 93/13/EEC;²⁴⁴ however the application of this directive is limited to consumer agreements. In the context of B2B contracts the Court of Appeal in *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd*²⁴⁵ was willing to 'imply a term that BSB should act with good faith in the performance of this contract',²⁴⁶ but Brownsword observed that 'it was not in fact material to imply such term' because only terms that represent 'parties' unstated intentions' may be implied and the latter are generally underlined by an 'adversarial model'.²⁴⁷

The influence of European law over the English law is indeed more prominent in the context of consumer protection than in business contracts.²⁴⁸ Brownsword suggested that the above Directive 93/13/EEC 'in line with much EC regulation, serves to underline the bifurcation in English contract law between consumer contracting and commercial contracting'.²⁴⁹ He added that 'the danger here is that English contract lawyers, unfamiliar

²⁴⁰ [1992] 2 AC 128.

²⁴¹ According to *BBC Worldwide Ltd v Bee Load Ltd* [2007] EWHC 134 (Comm) [93] 'the agreement to consider in good faith any request [by the defendant] to extend the scope of the agreement was (...) unenforceable as a matter of English law on the principle of *Walford v Mile*'.

²⁴² See articles 1.7 and 2.1.15 of PICC, articles 1:201 and 2:301 of PECL and article II.-3:301 of the DCFR.

²⁴³ Moss (n 221) 71.

²⁴⁴ See reg. 5(1) of Unfair Terms in Consumer Contracts Regulations 1999.

²⁴⁵ [1995] EMLR 472 (CA).

²⁴⁶ *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd* [1995] EMLR 472 (CA), 484.

²⁴⁷ See Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 148. See also Brownsword, 'Good Faith in Contracts Revisited' (n 86) 122-123.

²⁴⁸ See Poole, *Textbook on Contract Law* (n 78) 16.

²⁴⁹ See Brownsword, 'Two Concepts of Good Faith' (n 160) 243.

with the concept of good faith, treat it as a doctrine belonging exclusively on the consumer side of the line'.²⁵⁰

2.3. Legislative control on unfairness in business contracts in Brazil

In Brazil following the unification of the rules of private law, contracts between businesses²⁵¹ and non-businesses have been governed by provisions of the Civil Code which regulate obligations.²⁵² They include the general rules of contracts in articles 421 to 426 that are applicable to all contracts including consumer agreements.²⁵³

Although the systematization of the legislation through the use of Codes purports to provide a greater degree of transparency and consistency, their inflexibility may prevent an easy adaptation of the rules to social and economic transformations.²⁵⁴ Such inflexibility may be particularly problematic in the context of commercial dealings which require constant changes; hence the Civil Code has been unable to cover all contractual relationships of the marketplace which have become increasingly complex.²⁵⁵

In order to compensate for such inability to offer solutions to all conflicts, the social state developed a new legislative technique consistent with a more interventionist approach. It is the adoption of vague concepts and principles (e.g., social function, good faith, public interest) which can be applied by judges in different situations.²⁵⁶

However part of the legal literature contended that the application of general and abstract concepts and rules may not meet the needs of a complex society, because different

²⁵⁰ Ibid.

²⁵¹ Article 966 defines 'business proprietor' as 'anyone who engages, on a professional basis, in organised economic activity for the production or trade of goods or services'. See Leslie Rose, *O Código Civil Brasileiro em Inglês/ The Brazilian Civil Code in English* (Renovar 2008) 188.

²⁵² Special Part, Book I, 'The Law of Obligations' (articles 233 to 965).

²⁵³ However in the consumer context those general provisions are only subsidiary to the special rules provided by the Consumer Protection Code. B2C contracts are subject to more restrictions than other civil contracts because the Consumer Protection Code imposes more limitations to the sellers and suppliers in order to protect the vulnerable consumers. See chapter 3.

²⁵⁴ Edil Batista Júnior, 'O Ilógico Necessário: Considerações Acerca da Crise da Codificação Jusracionalista' ano 5, n. 48, 1, dez. 2000 <<http://jus.uol.com.br/revista/texto/517>> accessed 20 August 2011.

²⁵⁵ Gondinho observed that nowadays the private relationships have been directly influenced by the Federal Constitution and other statutes that form important legal micro-systems (e.g., Consumer Protection Code, Statute of the Child and Adolescent) which have diminished the importance of the Civil Code. See André Osório Gondinho, 'Codificação e Cláusulas Gerais' (2000) Rio de Janeiro: Padma, n. 2 Revista Trimestral de Direito Civil 3.

²⁵⁶ See Paula Castello Miguel, *Contratos entre Empresas* (Revista dos Tribunais 2006) 86-93 and Antonio Junqueira de Azevedo, 'O Direito Pós-Moderno e a Codificação' (2000) São Paulo, jan-mar, v. 33 Revista de Direito do Consumidor 123, 124.

relationships require distinct regulations.²⁵⁷ This argument is applicable especially to B2B contracts which due to their peculiarities need specific and clear rules to provide more certainty and enable companies to calculate risks.²⁵⁸

Despite the Civil Code containing special provisions in addition to general provisions to govern contracts of businesses or enterprises,²⁵⁹ the immutability and rigidity of those special rules have not allowed them to adapt to the dynamism of the market. Furthermore the above rules (which include open provisions) are not sufficient to address important institutions of commercial law (e.g., bankruptcy, debt instrument and business corporation) which made necessary the enactment of sparse statutes to fill the gap left by the codified law.²⁶⁰

Brownsword recently pointed out that the dilemma that contract law currently faces in the context of B2B contracts is regarding the balance between rigidly prescribing rules for the market and adapting to the practices that give particular markets their 'distinctive normative identity'.²⁶¹ The law should be flexible enough to adapt to different marketplaces and to different attitudes of the parties towards each other.²⁶²

2.3.1. Limits to the freedom of contract

The contemporary legislation has faced the onerous task of establishing a balance between the rights of business parties to pursue their self-interests and the need to protect the weak party against abuses. The freedom of contract is no longer an absolute value²⁶³ as it cannot contradict other constitutional values such as the social justice that purports to prevent imbalances in relationships.²⁶⁴ In other words contractual terms in B2B contracts are not immune to judicial interferences, but interventions should only be

²⁵⁷ See Castello Miguel (n 256) 94-95 and Gondinho (n 255) 3.

²⁵⁸ Bulgarelli noted that 'the general rules of obligations are related to the relationships of peoples and goods; whereas the business contracts are concerned to the production activity and circulation of wealth'. See Waldírio Bulgarelli, *Direito Comercial* (16th edn, Atlas 2001) 59.

²⁵⁹ See Special Part, Book I, 'The Law of Obligations' (articles 233 to 965) and Book II, 'The Law of Enterprises' (articles 966 to 1195) of the Civil Code.

²⁶⁰ Bankruptcy is regulated by Act 11101/2005 and Business Corporations by Act 6404/1976. Debt instruments are regulated by Decrees 2044/1908 and 57663/1966 (regulate Bills of Exchange and Promissory Notes) as well as by the Trade Acceptance Act (Act 5474/1968) and Check Act (Act 7357/1985).

²⁶¹ Brownsword, 'Maps, Methodologies, and Critiques: Confessions of a Contract Lawyer' (n 235) 136.

²⁶² *Ibid.* 142-143.

²⁶³ The contemporary Brazilian private law stipulates that parties no longer possess 'absolute rights' which depend only on their sole discretion and are free of any interference. See Flávio Tartuce, *Função Social dos Contratos: do Código de Defesa do Consumidor ao Código Civil de 2002* (2nd edn, Coleção Prof. Rubens Limongi França, Método 2007) 175.

²⁶⁴ Castello Miguel (n 256) 124-125.

made on an exceptional basis when it is ascertained that there has been the transgression of other values.

Theodoro Júnior contended that such '*contractual interventionism*' is a guarantee that the stronger party will not use his dominant position to exploit the other party.²⁶⁵ Moreover it implies that some legal provisions of public order (that impose certain limits on the individual will) cannot be revoked or modified by the parties.²⁶⁶

Castello Miguel classified those interventions in two types:²⁶⁷ the first one aims to protect interests that are external to the contracting parties and are related to collectivity (e.g., social function of the contract and the environment). The second type aims to protect the interests of the parties of the contract and its application is justified only when there is an inequality of bargaining power between parties. If there is a balance between them, they are presumably able to protect their own interests and avoid the violation of social values such as the principle of equality.²⁶⁸ Consequently it is possible to contend that interventions in B2B contracts are generally of the first type; whereas the second type may be more relevant to small businesses contracts.

Arguably one of the most important limitations to the freedom of contract in Brazil is the principle of the *social function of the contracts*. The Civil Code expressly stipulates that the former 'shall be exercised by virtue, and within the limits' of the latter;²⁶⁹ thus the individualist ethic that normally permeates B2B contracts is delimited by the social interest.²⁷⁰

Such a principle of the social function of contracts is also implied in the provisions of the Federal Constitution which prescribe that the social values of the free enterprise (one of the cornerstones of the Federative Republic of Brazil) have to be compatible with the fundamental objectives of Brazil that include the 'creation of a free society, just and with

²⁶⁵ Humberto Theodoro Júnior, *O Contrato e seus Princípios* (3rd edn, Aides 2001) 17.

²⁶⁶ *Ibid.*

²⁶⁷ Castello Miguel (n 256) 124-125.

²⁶⁸ *Ibid.*

²⁶⁹ See article 421 of the Civil Code. Although the Civil Code prescribes limitations to the freedom of contract, it does not reject its application. For instance, parties are allowed to conclude atypical contracts (art. 425), which means that they can establish any terms that suit their needs as long as they are consistent with the legislation.

²⁷⁰ Additionally judges have to take into account the *social ends* of the legislation and the requirements of the *common good* when applying the law. See article 5 of the Law of Introduction to the Brazilian Civil Code. Rose (n 251) 2.

solidarity'.²⁷¹ This constitutional principle of solidarity therefore imposes some boundaries to the free enterprise spirit that could give rise to unjust situations and abuses.²⁷²

The Federal Constitution prescribes other principles which govern economic activity.²⁷³ Although some of them also have an interventionist nature; others are considered non-interventionist. These apparent discrepancies result from the fact that the Constitution incorporated provisions typical of the liberal state as well as of the social state.²⁷⁴ For instance on one hand they include the promotion of the free enterprise and protection of the private property and free competition; but on the other hand the objectives of the economic order also purports to ensure everyone a life with dignity, in accordance with the precepts of social justice and the social function of property.

2.3.2. Contracts of adhesion

In Brazil businesses make use of '*general contractual conditions*' in B2B agreements which are unilaterally stipulated by one of the parties with the purpose of governing their commercial operations and negotiations in a more uniform way.²⁷⁵ Those conditions therefore facilitate their dealings and allow them to conclude large amounts of contracts. They become '*contracts of adhesion*' once accepted by the other party.²⁷⁶

The Brazilian legal system however recognises that the party (including businesses) who was unable to negotiate terms in those *contracts of adhesion* is susceptible to abuses; for this reason the Civil Code expressly prescribes protections to the adhering party. In those contracts the interpretation most favourable to the adhering party shall be adopted when clauses are ambiguous or contradictory. Additionally clauses that stipulate that the adhering party has waived in advance rights arising out of the nature of the transaction are deemed void.²⁷⁷ Those provisions clearly aim to protect the party who has not drafted the terms either through a more beneficial interpretation or through the prevention of the renouncement of rights.

²⁷¹ See articles 1, IV and 3, I of the Brazilian Federal Constitution.

²⁷² Fábio V. Figueiredo and Simone D. C. Figueiredo, *Código de Defesa do Consumidor Anotado* (Rideel 2009) 283.

²⁷³ See article 170 of the Brazilian Federal Constitution.

²⁷⁴ See José Afonso da Silva, *Curso de Direito Constitucional Positivo* (20th edn, Malheiros 2002) 763.

²⁷⁵ Grinover and others (n 34) 530-533.

²⁷⁶ Ibid. 531.

²⁷⁷ See articles 423 and 424 of the Civil Code. See also Rose (n 251) 88.

Ferreira suggested that judicial precedents corroborate the opinion that in the absence of a governmental intervention, contracts of adhesions would be far more damaging to parties who simply adhere to them.²⁷⁸

Although businesses in general are more likely to have some bargaining power to negotiate better terms than consumers, they may be compelled to accept imposed terms in certain situations. For instance in occasional contracts or in contracts with larger companies the dominant party may consider it not worth changing terms for an individual agreement, especially if he has a high demand for his products or services in which case the weaker business may be subject to a 'take it or leave it' situation.

As will be examined in chapter 4, the bargaining strength of a business is not always related to its size. There are some sectors (e.g., financial) where although businesses may be considered relatively small, are often in a strong position to negotiate. Therefore courts have to examine the circumstances of each individual agreement to determine whether one party abused its advantageous position to impose harmful terms on the adhering party.

2.3.3. Good faith

In Brazil good faith is not limited to B2C contracts, but it is also applied to business contracts as a general clause. The generalised application of this principle in contracts reflects the influence of the social state on the Brazilian legal system.²⁷⁹ Nonetheless ironically the revoked article 131 of the Commercial Code of 1850 was the first provision in this jurisdiction which expressly referred to good faith in an objective sense;²⁸⁰ even though such Code was enacted under a liberal state which advocated minimal government interventions in the economy.²⁸¹ For that reason this provision was virtually

²⁷⁸ Daniela Moura Ferreira, 'O Contrato de Consumo e o Princípios Informadores no Novo Código Civil' (2004) São Paulo, jan/mar, v. 13, f. 49 Revista de Direito do Consumidor 177, 179.

²⁷⁹ Leonardo Cacao Santos La Bradbury, 'Estados Liberal, Social e Democrático de Direito' ano 11, n. 1252, 5 dez. 2006 <<http://jus.uol.com.br/revista/texto/9241>> accessed 25 August 2011.

²⁸⁰ Article 131, item 1 of the Commercial Code applied good faith as a general rule of interpretation according to which this principle and 'the true spirit and nature of the contract shall prevail over the strict and narrow meaning of the words'. This article was among the provisions revoked by the new Civil Code (Act 10406/2002).

²⁸¹ La Bradbury (n 279).

ignored at that time and there were only a few isolated cases that made reference to good faith in the context of B2B contracts.²⁸²

Currently good faith can be found in various provisions of the new Civil Code that are relevant to all contractual relationships in Brazil. Nevertheless the operation and function of this concept will vary according to the type and peculiarities of the contract.²⁸³ Article 422 prescribes a general clause according to which parties are bound to observe the principle of good faith in the *conclusion* and *performance* of a contract.²⁸⁴

Legal literature and courts have also extended this principle to the *negotiation stage* through the application of the *culpa in contrahendo* doctrine in the absence of an express provision.²⁸⁵ This doctrine was proposed by Jhering and prescribes that 'damages should be recoverable against the party whose blameworthy conduct during negotiations for a contract brought about its invalidity or prevented perfection'.²⁸⁶ Therefore parties have to behave reasonably and loyally towards each other at this stage on pain of giving rise to pre-contractual liability, but for that 'the negotiations must at least have reached the stage of establishing a relation between the parties in which one may legitimately rely on the conduct of the other'.²⁸⁷

The duty to negotiate in good faith protects the reasonable expectations created by the behaviour of the parties and the trust between them. It is compatible with the freedom of contract that prevails in B2B contracts as parties are not compelled to conclude the contract.²⁸⁸ By the end of the negotiations, parties may opt to not contract according to

²⁸² Lívio Goellner Goron, 'Anotações sobre a Boa-Fé no Direito Comercial' (2003) São Paulo, jan./mar, v. 4, f. 13 Revista de Direito Privado 143, 153.

²⁸³ Andréa Carvalho Brito, 'A Função Restritiva do Princípio da Boa-Fé Objetiva: Uma Limitação ao Exercício Irregular dos Direitos Subjetivos' <<http://www.bahianoticias.com.br/justica/artigo/38,a-funcao-restritiva-do-principio-da-boa-fe-objetiva-uma-limitacao-ao-exercicio-irregular-dos-direito.html>> accessed 25 February 2011.

²⁸⁴ See Rose (n 251) 88.

²⁸⁵ In this context Brazilian law was particularly influenced by the German law. According to Quagliato 'although the Brazilian Legal System does not expressly require a negotiation procedure to be just, there is already a well defined tendency in admitting the "fair dealing" as an element of bargaining'. See Quagliato (n 82) 217.

²⁸⁶ Friedrich Kessler and Edith Fine, 'Culpa in Contrahendo, Bargaining in Good Faith, and Freedom of Contract: A Comparative Study' (1963-1964) 77 Harv L Rev 401, 401. This doctrine was expressly included in section 241(2) of the German Civil Code (BGB) which prescribes duties arising from an obligation such as 'to take account of the rights, legal interests and other interests of the other party'.

²⁸⁷ Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part II' (n 224) 119.

²⁸⁸ Quagliato (n 82) 216.

their own interests as long as they were transparent in relation to their intentions and made the other party aware of the risk of desistance.²⁸⁹

In some circumstances however the exercise of this right may be considered abusive. If a party breaks off the negotiations in bad faith and harms the other party, he will be liable for his wrongful behaviour. For instance if one party who never intended to conclude a contract induces the other party not to contract with a third party or to incur unnecessary expenses, he may be held accountable for his deceitful behaviour.²⁹⁰ Moreover according to the Civil Code if parties concluded a 'preliminary contract' which contains all the requirements of the contract to be entered to, then either of them has the right to demand the conclusion of the definitive contract, unless there is a clause allowing the parties to recede.²⁹¹

In other stages of B2B contracts good faith may be applied to prevent the '*abuse of rights*';²⁹² hence an act of a business may be formally legal but it will not be accepted by the legal system if it is contrary to this principle.²⁹³ As a result large companies which can afford staff with expertise to find loopholes in agreements or the law may have their behaviour limited by good faith. Similarly such principle can be employed to prevent any 'abuse of power' by the controlling shareholder in corporations as well as any disloyal behaviour among shareholders or partners who misuse their rights.²⁹⁴

2.3.3.1. Application of good faith by interpreters

Courts used to extend the application of the principle of good faith prescribed by the Consumer Protection Code to relationships between non-consumers by analogy.²⁹⁵ This

²⁸⁹ Ibid.

²⁹⁰ Dário Manuel Lentz Moura Vicente, 'A Responsabilidade Pré-Contratual no Código Civil Brasileiro de 2002' (abr./jun. 2004) R. CEJ 34, 37.

²⁹¹ Articles 462 and 463 of the Civil Code. See Rose (n 251) 95.

²⁹² Article 187 of the Civil Code considers illicit the exercise of a right that manifestly exceeds the limits imposed by its economic or social purpose, good conduct or good faith. See Ibid. 47. Good faith is also applied to prevent the abuse of rights. According to the Superior Court of Justice a lawful exercise of a right will become illicit at the moment that it goes beyond what it was reasonably expected in accordance with the objective good faith. See REsp 250523/SP (18/12/2000) and REsp 735168/RJ (26/03/2008).

²⁹³ Teresa Negreiros, *Teoria Geral do Contrato: Novos Paradigmas* (2nd edn, Renovar 2006) 141.

²⁹⁴ See article 117 of the Business Corporation Act (6404/1976).

²⁹⁵ See Ester Lopes Peixoto, 'O Princípio da Boa-Fé no Direito Civil Brasileiro' (2003) São Paulo, jan./mar, v. 12, f. 45 *Revista de Direito do Consumidor* 140, 160. Article 4 of the Law of Introduction to the Brazilian Civil Code authorises the use of analogy by judges.

analogical interpretation is no longer required following the enactment of the new Civil Code that expressly prescribes the use of good faith between private parties.²⁹⁶

Article 113 of the Civil Code prescribes that 'juridical transactions shall be interpreted in conformity with good faith and the practice of the place in which they are made'.²⁹⁷ This provision has therefore two implications for B2B contracts. First of all the legal effects of contracts will be guided by the principle of good faith. Secondly, business contracts should be interpreted in accordance with commercial practices common to a specific sector, commercial branches or professional categories,²⁹⁸ which is in line with a *dynamic market-individualism* approach.

The antecedent provision²⁹⁹ in its turn stipulates that more heed should be given to the intention of the parties than to the literal meaning of the language; but if it is not possible to infer the actual parties' intention or if the declaration of will is ambiguous, judges should interpret terms according to good faith and reject the ones that are abusive or unreasonable.³⁰⁰ Consequently this principle will attribute to a contractual term the meaning that parties would confer if they were behaving honestly and reasonably.

2.4. Analysing the differences and similarities of the legislative controls on unfairness in business contracts in England and Brazil

The English and Brazilian legal systems consider that when parties are both businesses and have equal resources and bargaining power, usually they do not need special protection so that freedom of contract should prevail in their agreements. As a consequence they should observe the agreed terms because they had the opportunity to negotiate them as well as to protect their own interests; hence 'the contract is law between equal parties'.³⁰¹ Otherwise agreements would not provide enough certainty to business parties.³⁰²

²⁹⁶ See REsp 1217951/PR (10/03/2011).

²⁹⁷ Rose (n 251) 34.

²⁹⁸ Judith Martins-Costa, 'Os Campos Normativos da Boa-Fé Objetiva: As Três Perspectivas do Direito Privado Brasileiro' (2005) Rio de Janeiro, nov./dez, v. 101, f. 382 Revista Forense 119, 139-140.

²⁹⁹ See article 112 of the Brazilian Civil Code.

³⁰⁰ In this context good faith should be applied in accordance with article 47 of the Consumer Protection Code. See Nobre Júnior (n 89) 79. In line with this interpretation see REsp 246562/SE (13/08/2001).

³⁰¹ Ulhoa Coelho (n 31) 20.

³⁰² Hoffman LJ observed that 'in many forms of transaction it is of great importance that if something happens for which the contract has made express provision, the parties should know with certainty that the terms of the contract will be enforced. The existence of an undefined discretion to refuse to enforce the contract on

Nonetheless England and Brazil recognise that there are situations in which business are not able to negotiate terms (such as in standard form contracts) or that they are in no position to have them changed (e.g., asymmetric relationships).³⁰³ Consequently both legislatures prescribe some controls on unfairness in the context of B2B contracts to prevent abuses in those circumstances. As seen above, general provisions of the Brazilian Civil Code can be used to protect businesses against disadvantageous terms that are included in contracts of adhesion.³⁰⁴ Section 3 of UCTA provides a similar protection to businesses (re: 'standard terms of business').

Therefore courts are allowed to interfere in business contracts to a certain extent and they may relieve parties from harsh terms; however they should limit such interferences only when the latter are strictly necessary to re-establish the contractual balance. Nonetheless while English courts have adopted a clear non-interventionist approach, the Brazilian courts have been given more flexibility to intervene in commercial agreements through the application of the principle of good faith.

2.4.1. Good faith in negotiations

There are fundamental differences between the approach adopted by the Brazilian legal system (and other civil law jurisdictions) and the English legal system concerning the application of good faith in negotiations. Those distinctions reflect the differences in the prevailing legal values in each legal system.³⁰⁵

Presently there is a tension between the *freedom of contract* and the need to limit such freedom in deference to the *common good*. On one hand, parties should be able to negotiate and conclude contracts according to their will and own interests. On the other hand, they should respect the legitimate expectations of the other party.³⁰⁶ In other words, in order to make life in society viable there is the need for some degree of

the ground that this would be 'unconscionable' is sufficient to create uncertainty'. See *Union Eagle Ltd v Golden Achievement Ltd* [1997] AC 514 , 519.

³⁰³ E.g., small businesses.

³⁰⁴ Articles 423 and 424 of the Civil Code.

³⁰⁵ Moura Vicente (n 290) 35.

³⁰⁶ *Ibid.*

sacrifice of individual interests in favour of the interests of the collectivity. However the 'extent of this sacrifice will vary considerably in time and space'.³⁰⁷

The recognition of a duty to negotiate in good faith by the Brazilian legal system reflects the influence of the *culpa in contrahendo* doctrine as well as the importance of the principle of the social function of the contracts.³⁰⁸ Therefore in Brazil there is a clear concern with the protection of the mutual trust and *equilibrium* between parties, even if this means interfering in their actions.

By comparison in the common law the main objective of the law of contracts is to provide the essential conditions for the operation of the market and the economy through the observance of freedom of contract and the sanctity of contract.³⁰⁹ In this context parties are free to conclude or not a contract; hence they should not be liable before its conclusion.³¹⁰

Although the English law of contract does not prescribe a duty to negotiate in good faith, it may be influenced by European initiatives such as PECL and DCFR which make reference to this duty as part of the common core of European contract law and which reflect the civilian position.³¹¹

Article 2:301 of the PECL (that inspired article II.-3:301 of the DCFR)³¹² tackles negotiations contrary to good faith and fair dealing. Under its paragraph (1) 'a party is free to negotiate and is not liable for failure to reach an agreement'. This is consistent with the English law position according to which there is no liability at negotiation stage.

However, paragraph (2) provides 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'. This provision is incompatible with the *Walford*³¹³ position as it prescribes the 'pre-contractual liability role' of good faith in the context of negotiations.³¹⁴ According to

³⁰⁷ Ibid. 35-36.

³⁰⁸ This principle can be expressly found in article 421 of the Civil Code.

³⁰⁹ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 50-53.

³¹⁰ Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part I' (n 94) 1.

³¹¹ Both PECL and DCFR are a result of discussions and studies of eminent jurists and academics from various European countries which led to the inclusion of concepts and principles typical of civil law.

³¹² Art. II.-3:301 DCFR (on negotiations contrary to good faith and fair dealing).

³¹³ *Walford v Miles* [1992] 2 AC 128.

³¹⁴ According to Carter and Furmston the 'pre-contractual liability' provides a basis for relief when one the parties withdraw from negotiations and it includes: remedial consequences for the breach of a contractual or

this role the defaulting party has to pay damages to the other party in order to compensate for the loss incurred.³¹⁵

Finally, paragraph (3) prescribes that 'it is contrary to good faith and fair dealing, in particular, for a party to enter into or continue negotiations with no real intention of reaching an agreement with the other party'. If the termination of the negotiations was caused by bad faith, parties should be obliged to continue such negotiations in accordance with the 'preservation role' of good faith.³¹⁶ Nevertheless if parties were acting in good faith they should be allowed to withdraw from the negotiations even if expenses were already incurred in reliance that the contract would be agreed.³¹⁷

2.5. Conclusion

In general business parties should be free to pursue their own interests; however agreements and other types of relationships have inevitably 'the capacity to affect adversely the interests of the other. Expectations can be thwarted, obligations ignored, vulnerability exploited, legitimate interests disregarded, powers exercised harshly, and so on.'³¹⁸ It is difficult to draw a line when the law should interfere.

Finn proposed that the idea of 'basic fairness' should limit a party's decision or action which directly affects the interests of the other.³¹⁹ Similarly Adams and Brownsword suggested that the 'pursuit of self-interest is permissible only so long as it is compatible with the legitimate interests of others'.³²⁰

non-contractual duty of good faith and invocation of promissory estoppels. It also includes claims for restitution based of the lack of good faith (when one party has conferred benefits to the other during negotiations). See Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part I' (n 94) 8. In England promissory estoppel promotes good faith and has been applied in non-contractual promises in the context of an existing contractual relation. See Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part II' (n 224) 100. In *Jorden v Money* (1854) 5 HL Cas 185 , 881 Lord Cranworth LC observed that there is 'a principle well known in the law, founded upon good faith and equity'.

³¹⁵ Quagliato (n 82) 215.

³¹⁶ Furmston, Norisada and Poole, *Contract Formation and Letters of Intent: A Comparative Assessment* (n 84) 275. Additionally Furmston and Tolhurst suggested that in *Hillas (WN) & Co Ltd v Arcos Ltd* (1932) 147 LT 503 (HL) the House of Lords decided that judges may imply terms into a contract based on the past dealings of the parties rather than consider the agreement void; thus it preferred an interpretation that allowed the preservation of the bargain rather than a strict interpretation of the terms. However this position was rejected in *Walford v Miles*. See Furmston and Tolhurst, *Contract Formation: Law and Practice* (n 237) 378.

³¹⁷ Parties are aware that negotiations always imply costs, but they intend to recoup expenses 'from contracts which result from successful negotiation'. See Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part I' (n 94) 8.

³¹⁸ Paul Finn, 'Commerce, the Common Law and Morality' (1989-1990) 17 MULR 87, 95.

³¹⁹ Ibid.

³²⁰ Brownsword, 'Two Concepts of Good Faith' (n 160) 215.

Therefore the English and Brazilian legal systems interfere in the freedom of contract in B2B agreements when they deem it necessary to prevent one party from harming the interests of the other. Among the tools employed in such intervention are the *reasonableness test* of UCTA and the concept of *good faith* of the Brazilian Civil Code. Bridge contended that the application of *undefined standards* however, may not be appropriate to regulate commercial relationships.³²¹ He argued that their vagueness gives too much leeway to judges who can interpret them according to their own convictions and beliefs, rendering their decisions unpredictable.³²²

Nonetheless 'where the parties are free and equal, they make little use of contract law',³²³ because a legal action implies high costs and may not provide the remedy that parties were expecting. For this reason the latter may prefer to settle eventual disputes 'in their own way' or through the use of 'customs of trade'.³²⁴ Even in the case of breach of contract they may opt for *non-legal sanctions* in the first instance (e.g., 'informal blacklisting') because a legal action 'often results in a "divorce" ending the "marriage" between the two businesses'.³²⁵ Therefore in order to preserve long-term relationships a business may avoid litigation or may adjust agreements in the case of the emergence of unexpected contingencies that impose an extra burden to the other party.³²⁶

Moreover more recently businesses have considered it more advantageous to behave according to a *cooperativist ethic* which takes into account the other party's interests with a view to 'obtaining mutual profits'.³²⁷ A cooperative relationship is conducted by a general norm of fairness and the individual self-interest is replaced by a 'common interest' attitude to contracts.³²⁸ Such *rationale of cooperation* has been also applied in the context of

³²¹ Bridge (n 221) 140.

³²² Ibid.

³²³ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 37. Similarly Lewis observed that 'there is also work which shows businesses to be reluctant to use the law in their relationships'. See P. Lewis, 'Small Firms and Their Difficulties with Contractual Relationships: Implications for Legal Policy' (2004) 33 *Comm L World Rev* 81, 83.

³²⁴ Macaulay (n 164) 61.

³²⁵ Ibid. 65.

³²⁶ Robert A Hillman, 'Court Adjustment of Long-Term Contracts: An Analysis under Modern Contract Law' (1987) 1987 *Duke LJ* 1, 5.

³²⁷ Quagliato (n 82) 213. According to Axelrod 'ordinary business transactions are also based upon the idea that a continuing relationship allows cooperation to develop without the assistance of a central authority. Even though the courts do provide a central authority for the resolution of business disputes, this authority is usually not invoked (...). The fairness of the transaction is guaranteed not by the threat of a legal suit, but rather by the anticipation of mutually rewarding transactions in the future'. See Robert Axelrod, *The Evolution of Co-operation* (Penguin 1990) 178-179. See Carvajal-Arenas and Maniruzzaman (n 83).

³²⁸ David Campbell and Donald Harris, 'Flexibility in Long-Term Contractual Relationships: The Role of Co-operation' (1993) 20 *J Law & Soc* 166, 167-168.

international business contracts and parties have 'voluntarily incorporated good faith'³²⁹ in their agreements for the sake of their long-term relationships.³³⁰

Such position is consistent with the current legislation that imposes controls on the adversarial ethic in bargains and prescribes that parties should act with loyalty and not obstruct or prevent the faithful compliance of the contract.³³¹ For instance a *duty to cooperate* is expressly prescribed by the *Principles of International Commercial Contracts* (PICC) and *Principles of European Contract Law* (PECL).³³² Additionally according to recital 31 of the *Proposal for a Regulation on a Common European Sales Law* (CESL) 'the principle of good faith and fair dealing should provide guidance on the way parties have to cooperate'.

Therefore in contractual relationships an environment of trust may be more fruitful to both parties as it involves fewer risks and protect legitimate expectations. It also ensures that businesses will mutually benefit from the agreement. For this reason the legislative controls on unfairness may contribute to the balance and stability of contractual relationships which many businesses aspire to.

³²⁹ Lord Justice Rix observed that 'commercial contracts assume such good faith, which is why express language requiring it is so rare'. See *Socimer International Bank Ltd (In Liquidation) v Standard Bank London Ltd (No.2)* [2008] EWCA Civ 116 , 116.

³³⁰ According to Carvajal-Arenas and Maniruzzaman 'good faith should be considered a framework of relationship between the parties to a contract and cooperation is the vehicle to maintain it'. See Carvajal-Arenas and Maniruzzaman (n 83).

³³¹ See Balbino (n 93) 115. In Brazil good faith is expressly applied in B2B contracts and it entails a duty of cooperation between contractual parties. Although in England there is no provision of the application of good faith in the context of B2B contracts, more recently it has been accepted that parties should act in cooperation. See Rawls (n 69) 10-13.

³³² In the words of article 1:202 of PECL: 'each party owes to the other a duty to co-operate in order to give full effect to the contract'. In addition article 1:301(4) of the same principles stipulates that the meaning of 'non-performance' includes the 'failure to co-operate in order to give full effect to the contract'. Article 5.3 of PICC prescribes that 'each party shall cooperate with the other party when such co-operation may reasonably be expected for the performance of that party's obligations'.

CHAPTER 3. ANALYSIS OF THE LEGISLATIVE CONTROLS ON UNFAIRNESS IN CONSUMER CONTRACTS IN ENGLAND AND BRAZIL

3.1. Context

As was seen in the previous chapter, freedom of contract prevails in agreements where parties are in a relatively equal position, thus it is still applicable in the context of business contracts when parties have equivalent bargaining strength. However the reality of consumer contracts is usually different.

Beale observed that often consumers do not fully understand the meaning of contractual terms and may consider it not worth the time and cost to achieve a greater comprehension of such terms. They may prefer to evaluate other qualities of the product that can be readily assessed such as appearance and price.³³³ For most consumers, the price is particularly influential to their decision and sellers and suppliers are well aware of that.³³⁴ For this reason in order to offer competitive prices and reduce costs, sellers and suppliers may shift risks to consumers through the inclusion of harsh terms and exemption clauses which are frequently overlooked.³³⁵

Moreover even when consumers are able to understand the content of the terms, they 'lack the power to have the contract changed'.³³⁶ Suppliers generally are not willing to alter a standard form contract for individual consumers, because it is impractical and involves extra costs; hence consumers are usually faced with a 'take it or leave it' situation.³³⁷

Those circumstances have led to the need for state intervention to restore the balance in consumer agreements. As a result, domestic legislatures (such as England and Brazil) and regional trade agreements (e.g., European Union and Mercosul) have enacted legislation

³³³ Hugh Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' in J Beatson and D Friedman (eds), *Good Faith and Fault in Contract Law* (Clarendon Press 1997) 232.

³³⁴ As it will be analysed later the Law Commission recently proposed that the price should be '*transparent* and *prominent*' because consumers 'should know what they have to pay and what they will receive in return'. See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) para 8.26.

³³⁵ Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 232.

³³⁶ Nebbia (n 120) 103.

³³⁷ See *Suisse Atlantique Société d'Armement Maritime S.A. Appellants v N.V. Rotterdamsche Kolen Centrale Respondents* [1967] 1 AC 361, 406.

whose primary objective is the protection of consumers against unfairness in contracts and the re-establishment of the contractual balance.

Marques remarked that this interventionist approach reflected the introduction of a social conception of the contract which takes into account not only the agreement between parties but also its effects on the society. For this reason the law has protected certain social interests such as the trust between parties, legitimate expectations and good faith.³³⁸

3.2. Legislative control on unfairness in consumer contracts in England

English law has been exposed to the influence of the European law in particular in the area of consumer protection.³³⁹ Consequently a considerable amount of legislation in this area results from the implementation of EU directives (e.g., *Unfair Terms in Consumer Contracts Regulations 1999* and the *Consumer Protection from Unfair Trading Regulations 2008*). It is therefore essential to analyse the consumer *acquis* prior to the examination of B2C contracts in the context of the English legal system.

3.2.1. The influence of European law

'Consumer *acquis*' may be defined as the cumulative body of European legislation and case law in the area of consumer protection. Since 1985 the EU has adopted various directives to regulate different aspects of consumer relationships that include: Doorstep Selling Directive (85/577/EEC); Consumer Credit Directive (87/102/EEC); Package Travel Directive (90/314/EEC); Unfair Terms in Consumer Contracts Directive (93/13/EEC); Distance Selling Directive (97/7/EC); Price Indication Directive (98/6/EC); Injunctions Directive (98/27/EC) and Consumer Sales Directive (99/44/EC).³⁴⁰

Directive 93/13/EEC is certainly the most relevant one for the purpose of the present study because it regulates terms on the basis of their 'unfairness' and has introduced the

³³⁸ Claudia Lima Marques, *Contratos no Código de Defesa do Consumidor* (6th edn, Revista dos Tribunais 2011) 210.

³³⁹ Poole, *Textbook on Contract Law* (n 78) 16.

³⁴⁰ 'The existing European consumer *acquis* is based on art. 3(t), 153 and 95 of the EC Treaty. According to these provisions, "the contribution to the strengthening of consumer protection falls among the activities of the European Community", which has the right to take measures for the accomplishment of this objective.' Zabia Vernadakis, 'Consumer Protection and the Reform of the European Consumer *Acquis*' (2010) 21(9) ICCLR 316, 317.

concept of good faith in this context.³⁴¹ In addition to this type of directive which contains a broader regulation of terms; other directives are limited to specific sectors or selling methods (e.g., Directive on Distance Selling) or provide enforcement mechanisms (Directive on Injunctions).³⁴²

These assorted types of directives however did not cover all key areas of consumer protection and the way they interacted with each other was far from straightforward.³⁴³ In order to address such fragmentation of the regulations of B2C contracts within the EU, in 2001 the European Commission issued the *Green Paper on European Consumer Protection* in which it suggested the development of a 'framework directive for fair commercial practices' to improve the consistency of the rules.³⁴⁴

As a result, the *Unfair Commercial Practices Directive* (UCPD)³⁴⁵ was adopted in 2005 and it was transposed into English law via the '*Consumer Protection from Unfair Trading Regulations 2008* (CPRs).³⁴⁶ The CPRs prohibit unfair commercial practices (activities related to the promotion, sale or supply of a product to consumers) in consumer contracts. Those practices are categorised as misleading actions or omissions³⁴⁷ and aggressive practices³⁴⁸ which are assessed according to the effect that they may have on the behaviour of the 'average consumer'.³⁴⁹

³⁴¹ The concept of "good faith" can be found in many *acquis* provisions. This is not surprising, because it is a notion found in most EU jurisdictions, although the common law continues to resist the adoption of a broad general "good faith" principle'. See Christian Twigg-Flesner, 'Pre-Contractual Duties – From the *Acquis* to the Common Frame of Reference' in R Schulze (ed) *Common Frame of Reference and Existing EC Contract Law* (Sellier, European law 2008) 101. 'Arguably the most significant contribution to general English contractual principles resulting from European directives and influence has been the introduction of the concept of "good faith"'. See Poole, *Textbook on Contract Law* (n 78) 19 and 267.

³⁴² See Commission, 'Green Paper on European Union Consumer Protection' COM (2001) 531 final para 2.2.

³⁴³ *Ibid.*

³⁴⁴ *Ibid.* para 4.1.

³⁴⁵ European Parliament and Council Directive 2005/29/EC of 11 May 2005 on Unfair Commercial Practices Directive [2005] OJ L149/22.

³⁴⁶ (SI 2008/1277).

³⁴⁷ In Case C-453/10 *Jana Pereničová and Vladislav Perenič v SOS Financ Spol. s r.o.* [2012] OJ C133/7 para 48 the EU Court of Justice observed that 'a commercial practice such as (...) indicating in a credit agreement an annual percentage rate of charge lower than the real rate must be regarded as "misleading" within the meaning of Article 6(1) of UCPD (...) in so far as it causes or is likely to cause the average consumer to take a transactional decision that he would not have taken otherwise. It is for the national court to ascertain whether that is the case in the main proceedings'.

³⁴⁸ In February 2011 a consumer (John Wigmore) won a court judgment against Safestyle (UK) which ignored his request of not being disturbed at his home by frequently visits of salesmen ('cold-callers') who were dealing on behalf of the defendant. The company was fined £4,000, ordered to pay £18,013 costs and a £15 victims' surcharge. It has been considered a landmark ruling as it is the first case in which a company has been convicted under the Consumer Protection from Unfair Trading Regulations 2008 and it represents an important step for consumer protection against harassment and other unfair commercial practices.

³⁴⁹ According to reg. 2(2) of the CPRs an 'average consumer' is 'reasonably well informed, reasonably observant and circumspect'.

A practice that is not considered misleading or aggressive may still be regarded as *unfair* under the general clause of reg. 3, provided that it fulfils two cumulative criteria: be contrary to the requirement of professional diligence *and* materially distorts (or be likely to) the average consumer's economic behaviour.³⁵⁰ There are also 31 practices prescribed in Schedule 1 that are banned outright under the CPRs (e.g. falsely stating limited offers, pyramid schemes, direct exhortation to children).³⁵¹

Moreover the CPRs prescribe in its part 3 that most breaches of the prohibition on unfair commercial practices are *criminal offences* punishable by fine or imprisonment. Therefore certain unfair terms that can mislead consumers 'are not only unfair but potentially criminally unfair'³⁵² and as a consequence 'such terms could give rise to enforcement action under the CPRs as well as, or instead of, the Regulations.'³⁵³

The UCPD adopts a *maximum* harmonisation clause that prohibits Member States to apply measures more protective of consumers than the one prescribed by the directive to ensure more consistency among EU regulations.³⁵⁴ Prior to UCPD, directives used to adopt a *minimum* harmonisation approach which allowed Member States to provide greater protection to consumers; thus they did not promote the 'uniformity of solutions for similar situations that the internal market would require'.³⁵⁵ The minimum harmonisation clauses were therefore another factor that contributed to the lack of harmony among the consumer protection legislation of the Member States.

Those inconsistencies within the consumer *acquis* have led to its undergoing review.³⁵⁶ As part of this review, the European Commission issued a *Proposal for a Directive on*

³⁵⁰ Health and Consumer Protection Directorate-General of the European Commission, *The Unfair Commercial Practices Directive: New Laws to Stop Unfair Behaviour Towards Consumers* (2006) 14-15.

³⁵¹ *Ibid.* 20-25.

³⁵² Oliver Bray and Lisa-Jayne Pickford, 'The UTCCRs: Coming to Terms with a Grey Area' (2009) 15(2) *CTLR* 26, 26.

³⁵³ Office of Fair Trading, *Unfair Contract Terms Guidance* (September 2008) 12.

³⁵⁴ Department for Business Innovation & Skills (BIS), *Review of the Eight EU Consumer Acquis Minimum Harmonisation Directives and their Implementation in the UK and Analysis of the Scope for Simplification* (URN 05/1951, 2005).

³⁵⁵ Commission, 'Communication from the Commission to the European Parliament and the Council: A More Coherent European Contract Law: An Action Plan' COM (2003) 68 final para 24.

³⁵⁶ In 2004 the Commission launched the review of the consumer *acquis* in its 'Communication from the Commission to the European Parliament and the Council: European Contract Law and the Revision of the Acquis: the Way Forward' COM (2004) 651 final paras 3-5. Such review is part of a plan to increase the coherence of the European contract law. In 2006 the Commission published a 'Green Paper on the Review of the Consumer Acquis' COM (2006) 744 final to collect views about the review.

Consumer Rights in 2008³⁵⁷ which intended to merge four existing EU consumer directives³⁵⁸ that adopt minimum harmonisation clauses and put forward a measure of maximum harmonisation. Such measure was criticised by consumer lawyers on the basis that Member States should be able to adopt higher standards of consumer protection according to the public interest of their country.³⁵⁹

Nonetheless the *Directive on Consumer Rights* (2011/83/EU)³⁶⁰ was adopted in October 2011 by the EU's Council of Ministers³⁶¹ and although its draft in principle proposed to repeal and replace the Directive 93/13/EEC, in practice it made only a minimal amendment to its article 8 which requires Member States to inform the European Commission about the adoption of more stringent provisions that ensure a higher degree of consumer protection.³⁶² This Directive has to be transposed into the national legislation of the Member States before the end of 2013.

In parallel to those developments the European Commission launched a *review of the European contract law* through the publication of a *Communication on European Contract Law* in 2001³⁶³ which suggested possible solutions to problems that result from divergences between the contract law of Member States. The suggestions varied from one extreme of leaving problems to be dealt by the market to the other of adopting an EU Contract Code.

There are also intermediate solutions that may be considered less controversial. The first one is the development of common non-binding contract law principles which may be satisfied by the UNIDROIT *Principles on International Commercial Contracts* (PICC)³⁶⁴ as

³⁵⁷ Commission, 'Proposal for a Directive on Consumer Rights' COM (2008) 614 final. In 2009 the Government published a response to this proposal through the White Paper 'Department for Business, Innovation and Skills (BIS), *A Better Deal for Consumers: Delivering Real Help Now and Change for the Future* (Cm 7669, 2009), which focused on four key themes: real help now for vulnerable consumers; a new approach to consumer credit; empowering consumers through better enforcement and information and modernising consumer law.

³⁵⁸ Consumer Sales and Guarantees (99/44/EC); Unfair Terms in Consumer Contract Terms (93/13/EEC); Distance Selling (97/7/EC); Doorstep Selling (85/577/EEC). As the review included the Directive 93/13/EEC the Law Commission Proposal on Unfair Terms in Contracts is on hold.

³⁵⁹ See Brownsword, 'Maps, Methodologies, and Critiques: Confessions of a Contract Lawyer' (n 235) 151-152.

³⁶⁰ Directive 2011/83/EU of the European Parliament and of the Council of 25 October 2011 on consumer rights [2011] OJ L304/64.

³⁶¹ The Directive on Consumer Rights (2011/83/EU) amended the Directives 93/13/EEC and 99/44/EC and repealed the Directives 85/577/EEC and 97/7/EC.

³⁶² Which ultimately allows the adoption of a minimum harmonisation clause. See article 32 of the Directive on Consumer Rights (2011/83/EU).

³⁶³ Commission, 'Communication from the Commission to the Council and the European Parliament on European Contract Law' COM (2001) 398 final.

³⁶⁴ UNIDROIT (International Institute for the Unification of Private Law) published in 1994 the *Principles of International Commercial Contracts* which aim to establish a set of rules for international commercial contracts

well as by the *Principles of European Contract Law* (PECL) which were already underway when the Communication was issued.³⁶⁵ The latter were produced by the Commission on European Contract Law ('Lando Commission') and 'are intended to be applied as general rules of contract law in the European Union'.³⁶⁶ Picat and Soccio observed that although those principles are not legally enforceable ('soft law'),³⁶⁷ they 'are an excellent instrument for information on the fundamental concepts and common principles prevailing in contract law in Member States'; but 'as a whole, these Principles remain too incomplete and abstract to provide solutions'.³⁶⁸

The other intermediate suggested solution is to review and improve existing EU legislation in the area of contract law to make it more coherent. The '*Action Plan*' issued by the European Commission in 2003 was in line with this solution and it proposed the creation of a *Common Frame of Reference* (CFR).³⁶⁹ This 2003 Communication noted that 'the reform of the European legislation on consumer' should be 'a priority policy area (...) for the update and simplification of the Community *acquis*'.³⁷⁰

Following the '*Action Plan*', the Commission released a second Communication in 2004 ('*The Way Forward*')³⁷¹ which outlined the development of the CFR. The purpose of the *Common Frame of Reference* is to improve the quality of legislation and the coherence of the current and future European contract law through the establishment of principles, terminologies and model rules.³⁷² In other words, 'the principal goal for the CFR--it is to serve as a terminological model in the drafting and revision of European legislation, in this way improving the functioning of the internal market by way of the resulting benefits for

which can be applied in any jurisdiction irrespectively of its legal tradition. They were developed by jurists from different jurisdictions, including Professor Luiz Olavo Baptista from Brazil (University of São Paulo) and Professor Michael P. Furmston (University of Bristol).

³⁶⁵ PECL are composed by three parts and were published in three phases: part I in 1995, part II in 2000 and part III in 2003. 'These principles remain broadly inspired (i) by the CISG and (ii) by the UNIDROIT Principles on international commercial contracts'. See Marc Picat and Stessie Soccio, 'Harmonisation of European Contract Law: Fiction or Reality?' (2011) 4 IBLJ 371, 375.

³⁶⁶ Article 1:101(1) of PECL.

³⁶⁷ Article 1:101(2) of PECL: these principles will only bind parties when they 'have agreed to incorporate them into their contract or that their contract is to be governed by them'.

³⁶⁸ Picat and Soccio (n 365) 375.

³⁶⁹ Commission, 'Communication from the Commission to the European Parliament and the Council: A More Coherent European Contract Law: An Action Plan' COM (2003) 68 final.

³⁷⁰ Vernadak (n 340) 318.

³⁷¹ Commission, 'Communication from the Commission to the European Parliament and the Council: European Contract Law and the Revision of the Acquis: the Way Forward' COM (2004) 651 final.

³⁷² Study Group on a European Civil Code and Research Group on EC Private Law (Acquis Group), *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR) - Outline Edition* (2009).

consistency'.³⁷³ It may also be used as 'basis for possible optional instruments of European contract law' or even to its unification.³⁷⁴

In 2009 a *Draft of the Common Frame of Reference* (DCFR) was published and it was based in part on the PECL.³⁷⁵ The DCFR 'is intended to be an amalgam of best solutions taken from both national law and the *acquis*;³⁷⁶ but the House of Lords is still sceptical about its application as well as the creation of an EU Contract Code and remarked that:

How far the DCFR will be used as the basis for a European Union instrument, and what form such an instrument might take, is still undecided. The development of a harmonised code of European contract law (to which we remain opposed) appears to be off any foreseeable agenda.³⁷⁷

Nevertheless, England cannot ignore the growing influence of the European law over its domestic law of contract. The latter will be increasingly exposed to concepts and principles typical of civil law which is the legal system that prevails among Member States. For the purpose of this work, the incorporation of 'good faith' into English law was used as a prominent example of such influence.³⁷⁸³⁷⁹

In 2010 the European Commission launched a Green Paper to consult relevant stakeholders about 'policy options for progress towards a European Contract Law for consumers and businesses'.³⁸⁰ This Commission proposed a range of options for a European Contract Law instrument,³⁸¹ which included the set up of an Expert Group 'to

³⁷³ See Lucinda Miller, 'The Common Frame of Reference and the Feasibility of a Common Contract Law in Europe' (2007) *Jun JBL* 378, 381.

³⁷⁴ Dirk Staudenmayer, 'European Contract Law – What Does It Mean and What Does It Not Mean?' in S Vogenauer and S Weatherill (eds), *The Harmonisation of European Contract Law: Implications for European Private Laws, Business and Legal Practice* (Hart 2006) 242.

³⁷⁵ The DCFR has an 'almost identical structure as the Principles of European Contract Law (PECL)', but the latter 'have been elaborated with a clear objective in mind--the first step towards use as "a basis for a European Code of Contracts'. See Miller (n 373) 382.

³⁷⁶ Twigg-Flesner (n 341) 99.

³⁷⁷ European Union Committee, *European Contract Law: the Draft Common Frame of Reference (Report with Evidence)* (HL 2008-09, 95).

³⁷⁸ 'In many laws the principle [good faith] is accepted as fundamental, but it is not accorded the same recognition in the laws of all the Member States'. See *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR) - Outline Edition* (n 372) [72]. 'Some see these frequent references to good faith and fair dealing as the Achilles' heel of the Draft, making it difficult to accept especially for lawyers in England'. See Carvajal-Arenas and Maniruzzaman (n 83).

³⁷⁹ Such concept is expressly prescribed by PECL and DCFR as a general clause applicable in the formation, performance and enforcement of the contract. See articles 1:102, 1:201, 1:305, 2:301, 4:110 of the PECL and articles I. – 1:103 and II. – 1:102 of the DCFR.

³⁸⁰ Commission, 'Green Paper on policy options for progress towards a European Contract Law for consumers and businesses' COM (2010) 348 final.

³⁸¹ The proposed options were: Option 1: Publication of the results of the Expert Group; Option 2: An official 'toolbox' for the legislator; Option 3: Commission Recommendation on European Contract Law; Option 4:

study the feasibility of a user-friendly instrument of European Contract Law' which would benefit consumers and businesses.³⁸² The results of this study were published in May 2011 but they were received with 'a lot of scepticism amongst stakeholders'.³⁸³ The suggested implementation of a European Contract Law or a European Civil Code was rejected; hence 'real harmonisation is excluded'.³⁸⁴ Consequently the proposals which may have a higher probability of being adopted are: an official 'toolbox' for the legislator, which may be satisfied by the adoption of the 'Common Frame of Reference' and/or an optional instrument of European Contract Law.³⁸⁵

The latter option in its turn may be fulfilled by the *Regulation on a Common European Sales Law* (CESL)³⁸⁶ which was proposed by the European Commission in October 2011. This regulation prescribes *optional* common rules of contract law that parties 'may choose to use to govern their cross-border sales and supply contracts' which would work as a *28th regime of contract law* alongside the contract law of the 27 EU Member States.³⁸⁷ It contains provisions that expressly tackle unfair terms in 'contracts between a trader and a consumer' which resemble articles 3 and 4 of the Directive 93/13/EEC³⁸⁸ but they make express reference to the duty of *transparency*. It also prescribes a *black list* of 'contract terms which are always unfair' and a *grey list* of 'contract terms which are presumed to be unfair' that include provisions already prescribed in the annex of Directive 93/13/EEC (Schedule 2 of the Regulations) and a few others.³⁸⁹

Regulation setting up an optional instrument of European Contract Law; Option 5: Directive on European Contract Law; Option 6: Regulation establishing a European Contract Law; Option 7: Regulation establishing a European Civil Code. See *Ibid.* para 4.1.

³⁸² *Ibid.* para 2.

³⁸³ Carvajal-Arenas and Maniruzzaman (n 83).

³⁸⁴ *Ibid.*

³⁸⁵ *Ibid.* See Commission, 'Green Paper on policy options for progress towards a European Contract Law for consumers and businesses' COM (2010) 348 final para 4.1.

³⁸⁶ Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final.

³⁸⁷ Poole, *Textbook on Contract Law* (n 78) 15. The CESL covers sale of goods, supply of digital content and provision of related services. See article 1 of the Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final.

³⁸⁸ Art. 83 of CESL: 1. 'In a contract between a trader and a consumer, a contract term supplied by the trader which has not been individually negotiated within the meaning of Article 7 is unfair for the purposes of this Section if it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer, contrary to good faith and fair dealing. 2. When assessing the unfairness of a contract term for the purposes of this Section, regard is to be had to: (a) whether the trader complied with the duty of *transparency* set out in Article 82; (b) the nature of what is to be provided under the contract; (c) the circumstances prevailing during the conclusion of the contract; (d) to the other contract terms; and (e) to the terms of any other contract on which the contract depends'.

³⁸⁹ For instance they considered unfair contract terms which 'oblige the consumer to pay for goods, digital content or related services not actually delivered, supplied or rendered' or 'inappropriately exclude or limit the right to set-off claims that the consumer may have against the trader against what the consumer may owe to the trader'. Article 84 (j) and 85 (c) of the *Regulation on a Common European Sales Law* respectively.

Nonetheless Picat and Soccio argued that a 'non-binding instrument would have no direct effect on national contract laws' thus they 'do not enable the ambitious project of the European Commission to standardise or harmonise contract law to be realised'.³⁹⁰

3.2.2. The English law on unfairness in B2C contracts

As seen in chapter 2 the controls prescribed by the *Unfair Contract Terms Act 1977* are mainly limited to exemption clauses. The Directive 93/13/EEC later introduced further controls on unfairness applicable more generally to 'unfair terms' in the context of consumer contracts. This directive was transposed into English law by the *Unfair Terms in Consumer Contracts Regulations 1994* which was replaced by the *UTCCR 1999*.³⁹¹ As will be analysed in chapter 5, there are numerous issues arising from overlapping and inconsistencies between UCTA and the UTCCR. For this reason in 2005 the Law Commission published recommendations which aim to unify the regimes of those unfair terms legislation to provide more coherence to the law. In view of the case law developed since then, in July 2012 the Law Commission proposed a review and update of these recommendations. This review was open for consultation until 25 October 2012 and it 'will be followed by an Advice to the Department for Business Innovation and Skills in spring 2013'.³⁹² The consultation involves discussions such as whether the list of Schedule 2 of the Regulations should be re-written and whether new legislation should cover non-negotiated and negotiated terms in B2C contracts.³⁹³

In addition to the Law Commission's recommendations, the Department for Business, Innovation and Skills (BIS) proposed a *Consumer Bill of Rights* in September 2011 which purports to reform the current pieces of consumer legislation in the UK because they are 'fragmented, overlapping and often expressed in complex language that is difficult for consumers and business to understand'.³⁹⁴ The first steps towards such reform include:

³⁹⁰ See Picat and Soccio (n 365) 395.

³⁹¹ The *Directive on Certain Aspects of the Sale of Consumer Goods and Associated Guarantees*, SCGD (99/44/EC) which was implemented by the Sale and Supply of Goods to Consumers Regulations 2002 'also requires Member States to ensure that certain types of limitation and exclusion clauses in consumer contracts are invalid'. See Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 1.4.

³⁹² See <http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm> accessed 26 July 2012.

³⁹³ See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) paras 9.36, 9.53, 10.15 and 10.17.

³⁹⁴ See <<http://www.bis.gov.uk/policies/consumer-issues/consumer-rights>> accessed 10 October 2011. This *Consumer Bill of Rights* will affect *secondary legislation* (Unfair Terms in Consumer Contracts Regulations 1999, Unfair Terms in Consumer Contracts (Amendment) Regulations 2001 and Sale and Supply of Goods to Consumers Regulations 2002) and *primary legislation* (Supply of Goods (Implied Terms) Act 1973, Unfair Contract Terms Act 1977, Sale of Goods Act 1979, Supply of Goods and Services Act 1982 and Sale and Supply of Goods and Services Act 1994). See Department for Business, Innovation and Skills (BIS), *Enhancing*

the consultation on the consolidation and modernisation of consumer law enforcement powers *and* the Law Commission's consultation and report on Misleading and Aggressive Practices. The latter resulted in the publication of the *Report on Consumer Redress*³⁹⁵ by the Law Commission in March 2012 which recommended the enactment of 'new legislation to provide redress to consumers who experience misleading and aggressive practices in their dealings with traders' in order to 'clarify and simplify the current law on misleading practices, and to improve the law on aggressive practices by filling the gaps in the current law'.³⁹⁶

Furthermore in July 2012 the government launched a new consultation '*Enhancing Consumer Confidence by Clarifying Consumer Law*' concerning the *Consumer Bill of Rights*, seeking 'views on strengthening and modernising consumer law' in particular 'on rights and remedies for goods and services and digital content supplied under a contract'.³⁹⁷ Due to the ongoing consultations it is still unclear how the new recommendations of the Law Commission (which may follow the consultation process) and the proposed *Consumer Bill of Rights* will interact with each other. Although the latter partly share a similar objective with the former, i.e. the enactment of a more coherent and clearer legislation to govern B2C contracts, the Law Commission recommendations also include provisions which cover B2B and small business contracts and the 'primary legislation that apply to business to business transactions' is outside the scope of the *Consumer Bill of Rights*.³⁹⁸

Nonetheless in its response to the Law Commission consultation, the Law Society contended that the proposed reform to unfair terms in contracts legislation 'should be focused solely on consumer contracts' due to existing doctrinal distinctions between rules which govern B2C and B2B contracts; hence they 'urge that the business relevant clauses of the Law Commissions draft bill be left out of this reform to the UTCCRs'.³⁹⁹

Consumer Confidence by Clarifying Consumer Law: Consultation on the Supply of Goods, Services and Digital Content (July 2012) 225.

³⁹⁵ Law Commission, *Consumer Redress for Misleading and Aggressive Practices* (Law Com No 332, 2012).

³⁹⁶ *Ibid.* para 22.

³⁹⁷ See <<http://www.bis.gov.uk/news/topstories/2012/Jul/consumer-bill-of-rights>> accessed 08 August 2012. This consultation is open until 05 of October 2012. See also Department for Business, Innovation and Skills (BIS), *Enhancing Consumer Confidence by Clarifying Consumer Law: Consultation on the Supply of Goods, Services and Digital Content* (July 2012).

³⁹⁸ See *Ibid.* 225.

³⁹⁹ Response by the Law Society to Law Commission, *Unfair Terms in Consumer Contracts: A New Approach? Issues Paper* (Law Com No 292, 2012) para 9.

3.2.2.1. Defining consumer

In the context of UCTA, in order to determine who *deals as a consumer* it is necessary to establish who makes a contract *in the course of a business* as both definitions are intrinsically correlated. In the words of section 12(1) a party 'deals as consumer' if he does not make the contract in the course of a business or holds him out as doing so; the other party does make the contract in the course of a business; and if the consumer is not an individual the goods should be of a type ordinarily supplied for private use or consumption.⁴⁰⁰ Therefore under UCTA a company can deal as a consumer as long as it does *not* make the contract in the course of a business.

The meaning of 'in the course of a business' however is not unequivocal; hence it has been subject of judicial consideration. According to *R&B Customs Brokers Co Ltd v United Dominions Trust Ltd*⁴⁰¹ a degree of regularity is needed for an activity be considered an integral part of the business for the purpose of section 12 of UCTA.⁴⁰² Similarly, *Davies v Sumner*⁴⁰³ 'overlooks the width of the phrase at issue and appears to revert to a narrow definition of business as only applicable to the actual business in dispute and to the goods normally dealt with in that business'.⁴⁰⁴ In line with this view a company will not make a contract 'in the course of a business' in transactions merely incidental to the business; in which case it may 'deal as a consumer' and protected accordingly.

Nevertheless, the Court of Appeal adopted a broader approach for this phrase in *Stevenson v Rogers*.⁴⁰⁵ It concluded that in the context of section 14(2) of the Sale of Goods Act 1979 a sale is made in the course of a seller's business except when it is made 'outside the confines of the business'.⁴⁰⁶ Therefore even transactions ancillary to the scope of a business are also considered to be made 'in the course of a business'; thus there is no need to determine the regularity of the activity. Macdonald suggested that this approach is more appropriate than the narrow approach adopted in *R&B Customs*

⁴⁰⁰ There are exceptions in public auctions (s. 12(2)). However, is the person who claims that a party does not deal as consumer who has the burden of proof (s. 12(3)).

⁴⁰¹ [1988] 1 WLR 321 (CA).

⁴⁰² *R&B Customs Brokers Co Ltd v United Dominions Trust Ltd* [1988] 1 WLR 321 (CA) 331.

⁴⁰³ [1984] 1 WLR 1301 (HL).

⁴⁰⁴ Ian Brown, 'Business and Consumer Contracts' [1988] JBL 386, 391.

⁴⁰⁵ [1999] QB 1028.

⁴⁰⁶ *Stevenson v Rogers* [1999] QB 1028, 1039.

*Brokers*⁴⁰⁷ because otherwise it would allow 'merely incidental, and not regularly occurring, business purchases' to be protected as consumers.⁴⁰⁸

However, in *Feldarol Foundry Plc v Hermes Leasing (London) Ltd*⁴⁰⁹ the Court of Appeal preferred to apply the *R&B Customs Brokers* test instead of the *Stevenson v Rogers* approach in the context of UCTA. Notwithstanding the above decision, the Law Commission recommended the adoption of the broader approach that is currently applied in the Regulations (reg. 3).⁴¹⁰ It proposed that a 'person who makes a contract to obtain goods or services "related to", even if not "in the course of", his business should be treated as dealing as a business and not as a consumer'.⁴¹¹

By comparison with UCTA, the UTCCR 1999 regard as consumers only *natural* persons who in a contract act for purposes which are outside their trade, business or profession (reg. 3(1)); consequently for the purposes of the Regulations under no circumstances will businesses be deemed consumers. The Law Commission adopted a similar definition of 'consumer' who is described by the 'Unfair Contract Terms Bill' as an *individual* (hence a 'natural person') 'who enters into a contract wholly or mainly for purposes unrelated to a business of his' (clause 26).⁴¹² Furthermore the Consumer Protection from Unfair Trading Regulations 2008 (CPRs) also define consumer as an *individual* 'who in relation to a commercial practice is acting for purposes which are outside his business' (reg. 2(1)).⁴¹³

3.2.2.2. Assessment of reasonableness

The determination of the meaning of *in the course of business* as seen previously will enable the conclusion to be made as to whether a person is *dealing as a consumer*, which in its turn is essential to determine the application of section 3 of UCTA. This provision is

⁴⁰⁷ [1988] 1 WLR 321 (CA).

⁴⁰⁸ See Elizabeth Macdonald, 'In the Course of a Business - A Fresh Examination' Web JCLI <<http://webjcli.ncl.ac.uk/1999/issue3/macdonald3.html>> accessed 08 April 2010.

⁴⁰⁹ [2004] EWCA Civ 747.

⁴¹⁰ According to reg. 3(1) "seller or supplier" means any natural or legal person who, in contracts covered by these Regulations, is acting for purposes *relating* to his trade, business or profession (...).'

⁴¹¹ Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) paras 3.94 and 5.12. See also para. 4.44 of Law Commission's Report (Law Com No 292, 2005) and clause 26 of the respective draft Bill.

⁴¹² In the words of the clause 26 (draft Bill) a "consumer contract" means a contract (other than one of employment) between— (a) an individual ("the consumer") who enters into it wholly or mainly for purposes unrelated to a business of his, and (b) a person ("the business") who enters into it wholly or mainly for purposes related to his business.

⁴¹³ Law Society contended 'that the definition of consumer should be uniform across all consumer legislation' and 'this should be the EU definition'. See Response by the Law Society to Law Commission, *Unfair Terms in Consumer Contracts: A New Approach? Issues Paper* (Law Com No 292, 2012) paras 47 and 48.

applicable to attempts to limit or exclude strict contractual liability⁴¹⁴ in the occurrence of one of the qualifying conditions: when one of the contracting parties *deals as consumer*, or one business *deals on the other's written standard terms* in a B2B contract.⁴¹⁵

Section 3 prescribes restrictions on the party who is in breach of contract to exclude or restrict his own liability; or claim to be entitled to provide performance substantially different from what is reasonably expected or to render no performance at all.⁴¹⁶ Such restrictions are particularly important in B2C contracts to prevent sellers or suppliers from evading obligations. Those terms however will be valid if they satisfy the requirement of *reasonableness* which was examined in chapter 2.

In the assessment of the reasonableness requirement courts tend to be more protective in contracts involving consumers. In *Smith v Eric Bush*⁴¹⁷ the House of Lords held that a disclaimer of liability for the accuracy of the valuation report of a house for mortgage purposes was unreasonable because parties did not share equivalent bargaining strength. Similarly in *St Albans City & District Council v International Computers Ltd*,⁴¹⁸ a 'quasi-consumer' case, the Court of Appeal also adopted an interventionist approach due to the lack of bargaining power of a local authority in relation to a supplier of computer software. For that reason the limitation clause that purported to restrict the loss caused by an error of the software supplied by the defendant was held unreasonable.

3.2.2.3. Assessment of fairness

By comparison with UCTA, the test applied by UTCCR 1999 is of '*fairness*' not '*reasonableness*'. The application of the Regulations however is limited to *non-individually negotiated terms* in contracts between consumers and sellers or suppliers; whereas the provisions of UCTA also cover business contracts and negotiated terms. For this reason

⁴¹⁴ *Strict contractual obligations* 'must be performed completely and precisely to an absolute standard', differently from *qualified obligations* that require only that the party 'takes reasonable care or exercise reasonable skill in the performance of the contract'. See Poole, *Textbook on Contract Law* (n 78) 244. For the purpose of exemption clauses, qualified obligations are equate to negligence liability that is regulated by section 2 of the UCTA.

⁴¹⁵ If the breach of strict contractual obligations is related to sale and supply of goods, then sections 6 and 7 of UCTA should be applied instead s. 3. According to s. 6(2) if a person is dealing as a consumer (in line with s. 12) then such obligations cannot be excluded or restricted; whereas under s. 6(3) in case of non-consumers such obligations can be excluded or restricted if the clause is considered reasonable.

⁴¹⁶ According to Brownsword, the standards of reasonable expectation vary in different sectors, thus they need to be analysed case-by-case, what can be unpredictable. See Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 10.

⁴¹⁷ [1990] 1 AC 831, 858.

⁴¹⁸ [1996] 4 All ER 481 (CA), [1995] FSR 686.

the Law Commission proposed that the consumer regime should cover terms individually negotiated *and* non-individually negotiated so that the protection currently offered to consumers by the UCTA is not reduced.⁴¹⁹ This recommendation is a positive step to increase the level of consumer protection because the weaker party can be influenced or persuaded to agree with an unjust term which may be regarded as negotiated.

For the purpose of the Regulations a term is considered *not individually negotiated* where it has been drafted in advance and the consumer has therefore not been able to influence the substance of the term'.⁴²⁰ Even if the consumer was able to influence a specific term or certain aspects of it, the Regulations will be still applicable to the rest of the contract if an overall assessment indicates that it is a pre-formulated standard contract.⁴²¹ Otherwise sellers and suppliers would be able to easily circumvent the provisions of the UTCCR by negotiating an insignificant term and imposing harsh conditions on the remaining non-negotiated terms. In other words this provision 'is seeking to close a possible loophole whereby standard forms are deemed to be negotiated contracts (...) simply on the strength of one term in the contract being open to negotiation'.⁴²²

As in practice B2C contracts are frequently drafted beforehand, they may usually be regarded as standard form contracts and subjected to the controls of the Regulations. Nonetheless consumers may consider that the pre-drafted terms suit their needs and can freely accept them, in which case they should not be considered unfair. Directive 93/13/EEC and its respective Regulations' 'primary target is not [the] standard form as such, but *unfair* standard form dealing in the mass consumer market'.⁴²³

Negotiated terms in their turn are not subject to the 'fairness test'. Similarly *core terms* will not have their fairness assessed as long as they fulfil the *transparency requirement*,⁴²⁴ which means to be written in *plain and intelligible language* in order to enable consumers

⁴¹⁹ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 3.55.

⁴²⁰ See reg. 5(2).

⁴²¹ See reg. 5(3).

⁴²² Howells and Brownsword (n 193) 247.

⁴²³ Brownsword, Howells and Wilhelmsson, 'Between Market and Welfare: Some Reflections on Article 3 of the EC Directive on Unfair Terms in Consumer Contracts' (n 77) 27.

⁴²⁴ Christian Twigg-Flesner, 'The Implementation of the Unfair Contract Terms Directive in the United Kingdom' (2006/7) CIL 235, 255. Schillig observed that a term which violates the principle of transparency is not automatically cancelled; instead under reg. 7(2) it can 'be retained' if interpreted in favour of the consumer. He added that 'to interpret an ambiguous term in the most favourable way to the other party seems to set a powerful incentive for the seller or supplier to draft his terms in a clear and transparent fashion'. See Michael Schillig, 'Inequality of Bargaining Power Versus Market for Lemons: Legal Paradigm Change and the Court of Justice's Jurisprudence on Directive 93/13 on Unfair Contract Terms' (2008) 33 EL Rev 336, 351-352.

to understand their contents before agreeing with them.⁴²⁵ In *Director General of Fair Trading v First National Bank plc*⁴²⁶ this provision was used as a bank's argument to avoid the application of the Regulations over a term which prescribed that interest was chargeable before and after the judgment on repayment in case of customer's default; however the House of Lords considered that the term was *incidental* being 'acutely aware of the need to adopt a restrictive approach to the notion of core term'.⁴²⁷ Although this court determined that UTCCR were applicable to the term in question, it also held that such term was not unfair as it was neither unbalanced nor detrimental to the consumer.

In agreement with the above case and *Bairstow Eves London Central v Smith*,⁴²⁸ the interpretation of reg. 6(2) should be restrictive to avoid precluding the assessment of the unfairness of terms that are not strictly related to the subject matter of the contract. 'We would expect a court minded to protect consumers to confine the main subject matter of the contract within the narrowest of bounds' to allow the application of the fairness test over a greater number of terms.⁴²⁹ Otherwise this provision would be rendered inept for its protective purpose.

More recently in *Office of Fair Trading v Abbey National plc and Others*⁴³⁰ it was discussed whether the OFT could assess the fairness of bank charges levied on customers' personal accounts for unauthorised overdrafts under the Regulations. Although the Court of Appeal held that these charges could be subject to assessment for fairness, the Supreme Court reversed this decision based on reg. 6(2) of the UTCCR 1999. According to the latter, if overdraft fees constitute part of the price or bank's remuneration, then they should be regarded as core terms and cannot be challenged.

The decision in the above case gave rise to considerable uncertainty concerning the interpretation of reg. 6(2). As a result on 25 July 2012 the Law Commission published the issues paper '*Unfair Terms in Consumer Contracts: A New Approach?*' containing new recommendations 'on how the price and main subject matter exemption should be

⁴²⁵ Core terms are related to the definition of the main subject matter of the contract (goods or services) or to the adequacy of the price or remuneration. See reg. 6(2). The Directive 93/13/EEC purports to ensure that consumers have 'access to all the information needed to arrive at his decision in full knowledge of the facts'. See Schillig (n 424) 351.

⁴²⁶ [2001] UKHL 52, [2002] 1 AC 481 (HL).

⁴²⁷ Twigg-Flesner, 'The Implementation of the Unfair Contract Terms Directive in the United Kingdom', 246.

⁴²⁸ [2004] EWHC 263 QB [25].

⁴²⁹ Howells and Brownsword (n 193) 251.

⁴³⁰ [2009] UKSC 6, [2010] 1 AC 696, [2009] EWCA Civ 116.

interpreted'.⁴³¹ For instance it was suggested that the exclusion of a *price term* from the fairness test should be made only if such term is '*transparent and prominent*' and that it would be helpful to have statutory guidelines to clarify the meaning of both expressions.⁴³²

3.2.2.4. Unfair terms

The objective of the *fairness test* is to identify contractual terms which shall be regarded as unfair in order to declare them invalid. Reg. 5(1) defines *unfair term* as 'a contractual term which has not been individually negotiated' and '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*'.

Although it would be expected that an express definition of 'unfair term' would allow a clear understanding of its meaning, in practice the use of vague expressions such as 'good faith' and 'significant imbalance' has caused a considerable degree of perplexity among interpreters. It is unclear whether those expressions complement each other or whether the imbalance may be considered an 'evidence of lack of good faith'.⁴³³ Furthermore, despite it being widely accepted that 'significant imbalance' is concerned with substantive fairness,⁴³⁴ there are questions whether 'good faith' is related to substantive and/or procedural fairness.⁴³⁵

⁴³¹ See <http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm> accessed 26 July 2012. For instance the Law Commission suggested that the legislation should state 'in clear terms that the exemption [from the fairness test] does not apply to' 'price escalation clauses, early termination charges and default charges'. See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) para 8.4.

⁴³² According to the Law Commission *transparent* term is the one written in 'plain, intelligible language, legible and readily available to the consumer' and a *prominent* term is the one 'that it is presented during the sales process in such a way that a reasonable consumer would be aware of the term even if they did not read the full contractual document'. See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) paras 8.16 to 8.34. According to the Law Society 'the new rules should make it unambiguously clear which terms and conditions are core and which are not'. See Response by the Law Society to Law Commission, *Unfair Terms in Consumer Contracts: A New Approach? Issues Paper* (Law Com No 292, 2012) para 18.

⁴³³ Poole, *Textbook on Contract Law* (n 78) 267.

⁴³⁴ According to Bright it is generally accepted that if a term causes significant imbalance in a contract, this term will be automatically contrary to good faith and substantively unfair, independently of the procedure. See Susan Bright, 'Winning the Battle against Unfair Contract Terms' (2000) 20(3) LS 331, 348. On the other hand the content of a term can be fair, but procedural issues, such as lack of transparency and bargaining defects can cause a significant imbalance to the detriment of the consumer. See Susan Bright, 'Unfairness and the Consumer Contract Regulations' in A Burrows and E Peel (eds), *Contract Terms* (Oxford-Norton Rose Law Colloquium Oxford University Press 2007) 184.

⁴³⁵ Collins, 'Good Faith in European Contract Law' (n 109) 249.

The House of Lords suggested in *Director General of Fair Trading v First National Bank plc*⁴³⁶ that 'good faith' in the context of the Regulations is an overarching concept of 'fair and open dealing'.⁴³⁷ At first sight Lord Bingham circumscribed this concept to procedural aspects; however he also made references to examples of substantive unfairness in the definition of fair dealing.⁴³⁸ Furthermore Lord Steyn in the same judgment observed that 'any purely procedural or even predominantly procedural interpretation of the requirement of good faith must be rejected' because there are overlaps between the requirements of 'good faith' and 'significant imbalance' and both are related to substantive issues.⁴³⁹

Similarly Collins and Beale contended that good faith has not only a *procedural* aspect but also a *substantive* one.⁴⁴⁰ The former is related to the disclosure of information to prevent unfair surprises on terms and products; whereas the latter recognises that there are terms that should always be considered unfair due to the imbalance that they may cause between parties, hence 'the term itself must be contrary to good faith'.⁴⁴¹

There is more recent case law which also examined the unfairness of terms and whether it was related to procedural or substantive matters. For instance, in *Office of Fair Trading v Foxtons Ltd*⁴⁴² Mann J assessed the existence of a significant imbalance of terms (pertinent to commissions which a consumer landlord had to pay for a letting agent services) as well as procedural issues related to the lack of openness that could become 'a trap, or a time bomb'.⁴⁴³ Similarly in *Mylcrist Builders Ltd v Buck*⁴⁴⁴ Ramsey J held that an arbitration clause in a B2C contract was unfair because the consumer was not aware of the significance of such clause, thus the requirement of 'fair and open dealing' was not fulfilled.⁴⁴⁵

⁴³⁶ *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 AC 481 .

⁴³⁷ *Ibid.* [17].

⁴³⁸ 'Fair dealing required that a supplier should not, whether deliberately or unconsciously, take advantage of the consumer's necessity, indigence, lack of experience, unfamiliarity with the subject matter of the contract, weak bargaining position (...)'. See *Ibid.*

⁴³⁹ *Ibid.* [36].

⁴⁴⁰ Collins, 'Good Faith in European Contract Law' (n 109) 250 and Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 245.

⁴⁴¹ According to Collins 'the Directive does not state that the significant imbalance of the obligations must be caused by actions contrary to the requirement of good faith, as one would expect if the requirement of good faith referred solely to procedural matters such as pressure and deception'. Collins, 'Good Faith in European Contract Law' (n 109) 250. See also Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 245.

⁴⁴² [2009] EWHC 1681 (Ch).

⁴⁴³ *Office of Fair Trading v Foxtons Ltd* [2009] EWHC 1681 (Ch) [91]. In the words of Mann J 'the typical consumer landlord may well be familiar with the concept of commission, but the real question is: commission on what?'

⁴⁴⁴ [2008] EWHC 2172 (TCC); [2009] 2 All ER (Comm) 259; [2008] BLR 611.

⁴⁴⁵ *Mylcrist Builders Ltd v Buck* [2008] EWHC 2172 (TCC), [2009] 2 All ER (Comm) 259, [2008] BLR 611 [56].

On the other hand, in *Bryen & Langley Ltd v Boston*⁴⁴⁶ the Court of Appeal concluded that there was no procedural unfairness because the term, although potentially unfair, was included by the consumer's own agent and not by the supplier; thus in this case the consumer 'had the opportunity to influence the terms'.⁴⁴⁷

Notwithstanding the controversy surrounding the definition of 'unfair terms' in reg. 5(1); reg. 6(1) stipulates that the assessment of the unfairness of a contractual term should take into account the nature of the goods or services for which the contract was concluded, all circumstances attending the conclusion of the contract and all other terms of the contract.

In addition, Schedule 2 provides an indicative list of terms that may be regarded as unfair, also known as 'grey list'.⁴⁴⁸ The examples provided refer mainly to the substance of the contract rather than the contracting process, with exception of para 'i' which considers unfair a term that 'irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract' ('unfair surprise').⁴⁴⁹

Furthermore, in 2008 the Office of Fair Trading (OFT) published an *Unfair Contract Terms Guidance* 'which taken with the decision of the House of Lords in *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 AC 481 and subsequent case law, constitutes some guidance on the interpretation of unfairness under the regulations'.⁴⁵⁰

⁴⁴⁶ [2005] EWCA Civ 973, [2005] BLR 508.

⁴⁴⁷ *Bryen & Langley Ltd v Boston* [2005] EWCA Civ 973, [2005] BLR 508 [46]. Similarly according to *Westminster Building Co. Ltd v Beckingham* [2004] EWHC 138 (TCC), 94 Con LR 107 [31] 'the terms in this case were not individually negotiated but were couched in plain and intelligible language' and 'the terms of the contract were decided upon by [the consumer's] agent'.

⁴⁴⁸ The 'grey list' differs from the 'black list' provided by UCTA 1977 that makes certain exclusions or restrictions absolutely invalid.

⁴⁴⁹ Howells and Brownsword (n 193) 256.

⁴⁵⁰ Poole, *Textbook on Contract Law* (n 78) 273.

3.2.2.4.1. Good faith

One of the most controversial aspects of the 'unfair term' definition is the use of the *good faith* expression. This concept was only introduced into English law by the Regulations and its application is still limited to the *performance of consumer* contracts.⁴⁵¹

In England good faith is not expressly defined but as observed above it may be related to procedural and substantive matters. In the absence of a definition, interpreters may refer to the provisions of the American *Uniform Commercial Code* (UCC)⁴⁵² which defines the obligation of good faith in the performance or enforcement of a contract⁴⁵³ as 'honesty in fact in the conduct or transaction concerned'.⁴⁵⁴ Good faith is therefore opposed to 'bad faith' and is based on the '*community standards*' of reasonableness, honesty and fairness;⁴⁵⁵ according to which parties have to behave with loyalty towards a common purpose that was agreed between them in order to not frustrate the legitimate expectations of the other party.

As a result of the uncertainty which surround the meaning and interpretation of good faith, the Law Commission proposed in its Report on Unfair Terms in Contracts a '*fair and reasonable*' test which does not make reference to this concept.⁴⁵⁶⁴⁵⁷ In chapter 6 the advantages and disadvantages of the application of good faith in English law will be discussed in more depth.

⁴⁵¹ See Ibid. 19. As seems previously the English law rejects the duty of good faith in negotiations for the reasons discussed in chapter 2.

⁴⁵² The law of the United States may be applied by English comparatists due the fact that it represents other major common law jurisdiction. Moreover good faith 'had already become established in American law'. See Bridge (n 221) 142.

⁴⁵³ In the words of the Uniform Commercial Code § 1-203 'every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement'. Similarly the Restatement (Second) of Contracts prescribes in its §205 that 'every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement'.

⁴⁵⁴ § 1-201 (19).

⁴⁵⁵ According to Brownsword and Reiter good faith is not determined by judges' discretion, but is based on the community standards. See Brownsword, 'Good Faith in Contracts Revisited' (n 86) 120 and B. J. Reiter, 'Good Faith in Contracts' (1983) 17 Val U L Rev 705, 716. Summers defined good faith as the opposite of bad faith. He contended that 'it is a phrase without general meaning (or meanings) of its own and serves to exclude a wide range of heterogeneous forms of bad faith'. Robert S. Summers, 'Good Faith in General Contract Law and the Sales Provisions of the Uniform Commercial Code' (1968) 54 Va L Rev 195, 201.

⁴⁵⁶ 'It will be easier for UK lawyers to apply than a more "European" test which makes express reference to good faith. Therefore we still recommend that the test should be one of "fairness and reasonableness"'. Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 3.85 and 3.91.

⁴⁵⁷ The proposed test shall be applied to consumer and small businesses contracts as well as to B2B contracts where UCTA provisions are still applicable. According to the draft clause 14(1) the 'fair and reasonable' test of a term will take into account (a) the extent to which the term is transparent, and (b) the substance and effect of the term, and all the circumstances existing at the time it was agreed. The matters concerning the substance include: the balance of the parties' interests and the strength of the parties' bargaining positions (clause 14(4)).

3.3. Legislative control on unfairness in consumer contracts in Brazil

Under the provisions of the Brazilian Federal Constitution 'consumer protection' has the status of a *fundamental right* and a *general principle of the economic activity*.⁴⁵⁸ The constitutional protection of consumers also included the stipulation of the creation of the Consumer Protection Code⁴⁵⁹ which contains the main controls on abusive clauses and exemption clauses in the context of B2C contracts. This Code has represented a powerful tool in the prevention of abuses of consumers' rights and has contributed to the growth of the consumer consciousness in Brazil. Furthermore the importance of its provisions has been widely recognised and applied by the higher courts of this country.⁴⁶⁰

In addition to the Federal Constitution and the Consumer Protection Code, the new Civil Code also contains provisions relevant to the protection of consumers against unfair terms; however its general rules have only a subsidiary application to the special rules of the Consumer Protection Code. Furthermore key principles of this Code, such as good faith and the social function of the contracts, could already be found in the consumer legislation.⁴⁶¹

3.3.1. Defining consumer

The Brazilian Consumer Protection Code expressly defines *consumer* in its article 2 as 'every *natural* or *legal* person who acquires or uses any product or service as a final recipient'. This article's sole paragraph adds that 'any group of people, even if indeterminate, who have participated in consumer relations shall be equated to consumers'.

In agreement with this definition, businesses may contract as consumers as long as they are the *final recipients* of goods and services and do not resell products with the purpose

⁴⁵⁸ See article 5, XXXII and article 170, V of the Federal Constitution. This article 5 contains a list of rights that cannot be revoked by amendments to the Constitution (article 60 §4, IV).

⁴⁵⁹ According to article 48 of the Constitution's Transitional Provisions the National Congress had to draw up the Consumer Protection Code within 120 days of the Constitution's promulgation.

⁴⁶⁰ E.g., REsp 827833/MG (16/05/2012).

⁴⁶¹ Tartuce (n 263) 106.

of making profit.⁴⁶² This provision does not discriminate between different sizes or types of legal persons, thus it covers 'small businesses, multinationals, foundations and even legal entities of public law'.⁴⁶³

The protection afforded by this Code can be also extended to *third parties* who are equated to consumers *stricto sensu* such as the victims of damages caused by defective products or services as a result of the supplier's fault (art. 17).⁴⁶⁴ They are termed as 'bystanders' by legal literature because although they are not part of the consumer relation, their health and safety are affected 'by intrinsic and extrinsic defects of the product or service'.⁴⁶⁵

Furthermore any person (determinable or not) *exposed* to abusive commercial practices is also protected under the Consumer Protection Code (art. 29). The mere exposure to those practices is sufficient to allow the application of preventive and abstract controls by courts and public prosecutors.⁴⁶⁶ The legal ties involving those third parties 'are determined by law and not by their will' and it represents a major change to the traditional idea that the effects of contracts should be limited to its actual parties (*inter partes* effect).⁴⁶⁷

This wide consumer definition clearly indicates the adoption of an interventionist approach in the context of B2C contracts as it covers any person who may be directly or indirectly harmed in a consumer relationship. This is in line with one of the principles of the National Policy for Consumer Relations which prescribes that the 'efficient prevention and suppression of all abuses in the consumer market' should be observed.⁴⁶⁸

⁴⁶² Nevertheless the Superior Court of Justice has extended the consumer protection to vulnerable small businesses even when they employ goods or services as part of their economic activity. See REsp 1010834/GO (13/10/2010).

⁴⁶³ Figueiredo and Figueiredo (n 272) 284.

⁴⁶⁴ The Superior Court of Justice applied this provision to make liable an establishment (which stocked and sold fireworks) for the damages caused to people who were injured or perished in an explosion caused by the firework's poor storage condition, even though did not have a consumer relationship with the business. See REsp 181580/SP (22/03/2004).

⁴⁶⁵ Grinover and others (n 34) 216.

⁴⁶⁶ Ibid. 271-272.

⁴⁶⁷ Marques, 'Notas sobre o Sistema de Proibição de Cláusulas Abusivas no Código Brasileiro de Defesa Do Consumidor: Entre a Tradicional Permeabilidade da Ordem Jurídica e o Futuro Pós-Moderno do Direito Comparado' (n 125) 59.

⁴⁶⁸ Article 4, VI of the Consumer Protection Code.

3.3.2. Unfair terms or abusive clauses

The Consumer Protection Code expressly addresses 'unfair terms' in B2C contracts; however as is the case for other countries that adopt the civil law tradition, it refers to such terms as '*abusive clauses*'.⁴⁶⁹ Although they are usually found in standard form contracts, the controls on unfairness cover both negotiated and non-negotiated terms either written or verbal.⁴⁷⁰

According to the aforementioned Code the protection against abusive clauses is regarded as one of the *basic consumer rights*.⁴⁷¹ Furthermore its article 51 contains examples of terms which shall be considered abusive and declared void. They can be classified in three groups:⁴⁷² clauses that limit rights of the consumer;⁴⁷³ clauses that offer advantages only to the supplier⁴⁷⁴ and clauses that may represent an 'unfair surprise' to the consumer.⁴⁷⁵ This list however is *indicative* and *non-exhaustive*,⁴⁷⁶ which means that judges may also consider other terms 'unfair' in accordance with the circumstances of each individual case.⁴⁷⁷

The most significant subsection of the list contains a general rule which regard as 'abusive' all terms which 'establish obligations considered inequitable or abusive which put the consumer at an unreasonable disadvantage'⁴⁷⁸ or that are inconsistent with good faith

⁴⁶⁹ 'The denomination given to "abusive clause" varies depending on the jurisdiction. For instance, in England it is called "unfair terms" and in the United States "unconscionable contract or clause"'. See Edilson Pereira Nobre Júnior, 'A Proteção Contratual no Código do Consumidor e o Âmbito de sua Aplicação' (1998) Bauru, ago./nov, f. 23 Revista do Instituto de Pesquisas e Estudos 275, 286.

⁴⁷⁰ Grinover and others (n 34) 535 and 570. As the Consumer Protection Code purports to cover also negotiated terms, the protection against abusive clauses is not prescribed under the section which regulates 'contracts of adhesion'.

⁴⁷¹ See article 6, IV of the Consumer Protection Code.

⁴⁷² Marques, 'Notas sobre o Sistema de Proibição de Cláusulas Abusivas no Código Brasileiro de Defesa Do Consumidor: Entre a Tradicional Permeabilidade da Ordem Jurídica e o Futuro Pós-Moderno do Direito Comparado' (n 125) 65.

⁴⁷³ Subsections I, II, III, VI, XV and XVI.

⁴⁷⁴ Subsections IX, X, XI, XII and XIII.

⁴⁷⁵ Subsections VII and VIII.

⁴⁷⁶ Article 51 provides a list of abusive clauses, but it expressly says that the examples provided are void 'among others'.

⁴⁷⁷ Grinover and others (n 34) 533-534. In addition subsection XV of article 51 allows judges to deem as void clauses which are in disagreement with the consumer protection system.

⁴⁷⁸ It is considered 'unreasonable' the advantage that: offends the fundamental principles of the legal system to which it belongs; restricts fundamental rights and obligations inherent to the nature of the contract in a manner which jeopardise its purpose or the contractual balance; and proves excessively onerous to the consumer considering the nature and content of the contract, the interests of the parties and other circumstances peculiar to the case. These provisions purport to protect the reasonable expectations of the parties and the balance of their rights and obligations. See article 51, first paragraph of the Consumer Protection Code.

or equity'.⁴⁷⁹ The considerable broadness and subjectivity of the expressions '*good faith*' and '*equity*'⁴⁸⁰ confer judges with ample flexibility to interpret them. This provision 'represents one of the most important innovations introduced by the Consumer Protection Code into the Brazilian contractual law', because it allows courts to examine the contents of consumer contracts and consequently exercise a substantive control on unfairness.⁴⁸¹

The Consumer Protection Code also entrusts Public Prosecutors with extensive power in the battle against unfair terms.⁴⁸² This body can propose on request of any consumer (or legal entity that represents the consumer) a legal action aimed at invalidating the terms that are contrary to the provisions of this Code or which are opposed to a fair balance between the rights and obligations of the parties.⁴⁸³

3.3.3. Good faith

Marques suggested that the Consumer Protection Code encompasses three fundamental principles that aim to prevent unfairness in B2C contracts: *good faith*, *vulnerability* and *equity* (the latter in the sense of contractual balance).⁴⁸⁴

Those principles are interrelated and complement each other. The principle of *vulnerability* recognises that consumers are particularly susceptible to harsh contractual terms due to their lack of bargaining strength.⁴⁸⁵ For this reason they need a special regime to protect them against economic abuses that may result from the suppliers' dominant position. This intervention is justified by the principle of *equity* which stipulates the need for a balance between the rights and obligations of the contracting parties.⁴⁸⁶

⁴⁷⁹ See subsection IV of article 51 of the Consumer Protection Code. See REsp 158728/RJ (17/05/1999) that considered abusive a term imposed by a health insurance company which limited the time of hospitalisation of the insured as it violated this article 51, IV. See also judicial precedent (Súmula) 307 (22/11/2004) of the Superior Court of Justice.

⁴⁸⁰ Equity here in the sense of contractual balance and not as a system of justice typical of common law jurisdictions which allow the supplement of unsatisfactory law in favour of a fair judgment.

⁴⁸¹ Marques, 'Notas sobre o Sistema de Proibição de Cláusulas Abusivas no Código Brasileiro de Defesa Do Consumidor: Entre a Tradicional Permeabilidade da Ordem Jurídica e o Futuro Pós-Moderno do Direito Comparado' (n 125) 69.

⁴⁸² The Public Prosecutors have played an important role in the control on abusive clauses especially in cases involving banks, health insurance, credit cards and so forth. Ibid. 55.

⁴⁸³ Article 51 §4 allows Public Prosecutors to control abstractly the unfairness of terms which were included in a contract during its formation stage. Ibid.

⁴⁸⁴ Ibid. 45-54.

⁴⁸⁵ Article 4, I of the Consumer Protection Code.

⁴⁸⁶ Article 51, IV of the Consumer Protection Code. The principle of equity can also be found in article 4, III which emphasises the importance of the 'balance in the relationship between consumers and suppliers'. The principle of equity is directly related with the constitutional principle of equality (art. 5, *caput* of the Federal

Ultimately these two principles are based on the idea that consumer contracts should be guided by the principle of *good faith* which aims to promote the fairness and harmony between parties.

As seen in chapter 1, the Brazilian law adopts the *objective* good faith that is a 'standard' according to which parties should respect the interests and expectations of the other party and cooperate for the fulfilment of the contract.⁴⁸⁷ Parties therefore have to act loyally and avoid abuses so that they do not harm or cause excessive disadvantage to the other party.

This principle of good faith governs all consumer relationships in Brazil and any clause which violates this principle shall be regarded as 'abusive'. As seen above under article 51, IV terms which are not consistent with good faith are unfair. In addition article 4, III prescribes that 'good faith and the balance in the consumers and suppliers' relationships' is one of the principles of the National Policy for Consumer Relations and article 51, XV stipulates that any clause in disagreement with the consumer protection system is also deemed abusive. Consequently it is possible to argue that all B2C contracts contain an *implied* general clause of good faith.⁴⁸⁸

The application of good faith is also expressly prescribed by the Civil Code which stipulates that courts shall interpret contractual terms according to this principle and to the 'practice of the place in which they are made'.⁴⁸⁹⁴⁹⁰ Furthermore in line with this

Constitution) because the latter prescribes the need for legislative intervention to restore the balance between consumers and suppliers. See Nunes Júnior and De Matos (n 75) 36.

⁴⁸⁷ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 215-216.

⁴⁸⁸ The good faith prescribed by article 4, III is considered a general clause which gives some leeway to judges and allows them to go beyond the literal meaning of the law; whereas the good faith of article 51, IV is an indefinite legal concept which is related to the judges' interpretative and evaluative activity when they declare a clause abusive and void. See Grinover and others (n 34) 534-535 and Nobre Júnior, 'O Princípio da Boa-Fé e o Novo Código Civil' (n 89) 76.

⁴⁸⁹ See article 113 of the Civil Code. Therefore courts should take into account the context of the contract and its social ends. See article 5 of the *Law of Introduction to the Brazilian Civil Code* which stipulates that 'in applying the legislation the judge shall attend the social ends to which it is direct and to the requirements of the common good'. See Rose (n 251) 2.

⁴⁹⁰ The Brazilian higher courts have extensively applied good faith in the interpretation of consumer contracts. For instance, the Superior Court of Justice has applied this principle to deal with unfair terms in health insurance contracts, such as terms which determine that pre-existing illnesses are not covered in the absence of previous health examination (AgRg no Ag 973265/SP - 17/03/2008) or terms which limit the length of stay in intensive care unit (REsp 249423/SP - 05/03/2001). The Supreme Federal Court has also made reference to good faith in various cases such as the discussion of the constitutionality of the transfer of the tax burden to the final consumer. See RE 370682/SC (25/06/2007).

principle as well as the principles of vulnerability and equity, terms shall be interpreted more favourably to consumers and to the adhering party in contracts of adhesion.⁴⁹¹

3.3.3.1. Good faith at performance stage

The Civil Code establishes in its article 422 that 'contracting parties are bound to observe the principles of probity and good faith, both in entering into the contract and in its *performance*'.⁴⁹² This provision prescribes a model of conduct that is 'operative and with a real practical value'.⁴⁹³

There are secondary duties that can be derived from good faith at this contractual stage such as the duty of *cooperation*.⁴⁹⁴ According to the latter parties should cooperate with each other and not prevent or interfere with the fulfilment of the contractual obligations by the other party. The Superior Court of Justice observed that such duty of cooperation has been underlined by the modern conception of contracts and presupposes a reciprocal loyalty between parties.⁴⁹⁵ It also requires proactive behaviour from sellers and suppliers through compliance with their obligations (e.g., providing information or performing a service).⁴⁹⁶

This duty to cooperate also implies the possibility of renegotiation or revision of clauses and obligations which become excessively onerous or disproportionate as a result of supervening facts.⁴⁹⁷⁴⁹⁸ Filomeno suggested that the possibility of modification of terms in the occurrence of fundamental and unpredictable changes of circumstances after the conclusion of a contract is in line with the so-called *clausula rebus sic standibus* (Latin for

⁴⁹¹ Article 423 of the Civil Code and article 47 of the Consumer Protection Code.

⁴⁹² See Rose (n 251) 88.

⁴⁹³ Judith Martins-Costa, *A Boa-Fé no Direito Privado* (Revista dos Tribunais 1999) 436. In addition as seen above the Consumer Protection Code prescribes that in the performance of the contract clauses that are inconsistent with good faith or equity shall be declared void (article 51, IV).

⁴⁹⁴ This duty of cooperation can be derived from articles 39, 40, 51, 52, 53 and 54 of the Consumer Protection Code.

⁴⁹⁵ See REsp 927457/SP (01/02/2012) and REsp 595631/SC (02/08/2004).

⁴⁹⁶ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 232.

⁴⁹⁷ *Ibid.* 233.

⁴⁹⁸ This argument was used as ground for the revision of contracts of *leasing* which instalments were linked to the exchange rate variation. In January 1999 there was an exchange rate overvaluation of the *US dollar* in relation to the *Brazilian real* and contracts of *leasing* became excessively onerous to consumers in Brazil. The understanding of the Superior Court of Justice has been in favour of the revision of the contracts; however this court has decided that the differences resulting from the devaluation of the 'real' (Brazilian currency) should be split equally between the parties what can be unfair to consumers as they normally have less financial resources than *leasing* companies. See AgRg no REsp 627674/SP (22/05/2009).

'things thus standing').⁴⁹⁹ The latter is an exception to the principle *pacta sunt servanda* (Latin for 'agreements must be kept') which establishes that agreements freely made should be strictly observed. Nonetheless both principles aim at the fulfilment of the contract either through the performance of its original terms or through the revision of the terms if necessary.⁵⁰⁰ Tartuce contended that in the consumer context there is no need to prove the above unpredictability but only that terms became highly onerous to the vulnerable party as a result of supervening events.⁵⁰¹

Another important secondary duty that can be derived from good faith at this contractual stage is the *duty of care*. According to this duty parties should be careful to not cause damage (physical, moral or economic) to the integrity of any person.⁵⁰² For instance the Superior Court of Justice concluded that a financial institution which registered an innocent consumer as a defaulter due to its lack of care should pay compensation for moral damages.⁵⁰³

3.3.3.2. Good faith at the negotiation and post-contractual stage

In the context of consumer contracts, Marques contended that parties not only have a 'duty to provide' but also a 'duty to behave'.⁵⁰⁴ Parties should therefore consistently behave honestly and faithfully towards each other to make their relationship more stable and trustworthy. In other words parties have to act in good faith in all contractual stages not only during the performance of the contract, but also in its negotiations (pre-contractual stage) and in a posterior stage (post-contractual).⁵⁰⁵

⁴⁹⁹ Grinover and others (n 34) 155-156. See also article 6, V of the Consumer Protection Code and article 317 of the Civil Code. According to the latter the revision of terms is justified in the occurrence of unforeseen circumstances.

⁵⁰⁰ In Brazil the *clausula rebus sic standibus* is also applied to business contracts. Articles 478 to 480 of the Civil Code prescribe that contracts with continuing or deferred performance may be dissolved if the obligation of one of the parties becomes excessively onerous with extreme advantage for the other party due to unforeseeable events. The dissolution may be avoided by the modification of the conditions on an equitable basis. See Rose (n 251) 98.

⁵⁰¹ Tartuce (n 263) 127-129. See article 51 §1, III of the Consumer Protection Code which tackles the excessive onerousness of one party's obligations.

⁵⁰² See article 186 of the Civil Code and article 6, VI of the Consumer Protection Code.

⁵⁰³ See REsp 987483/RJ (02/02/2010).

⁵⁰⁴ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 217.

⁵⁰⁵ *Ibid.* Marques observed that if the protection was limited to the contracting parties, it would exclude from the special protection all pre-contractual relationships which are also extremely relevant to the consumer market context. See Cláudia Lima Marques, 'Novas Regras sobre Proteção do Consumidor nas Relações Contratuais' (1992) São Paulo, n 1, *Revista de Direito do Consumidor* 27, 33.

The application of good faith at the negotiation stage has been supported by the *culpa in contrahendo* doctrine (as seen in chapter 2) as well as by the stipulation of *extra-contractual liability* for damages (including moral) or for violation of rights caused by any voluntary act or omission, negligence or imprudence; which means that liability may be attributed despite the non-existence of a contract between parties.⁵⁰⁶ Furthermore the Consumer Protection Code protects any person exposed to unfair commercial practices even before he performs an act of consumption (e.g., when a potential consumer is exposed to a misleading advertisement).⁵⁰⁷

There are also provisions of the Civil Code which prescribe the application of pre-contractual liability that are in line with a duty to behave in good faith. For instance under article 430 'if, for unforeseen circumstances, acceptance becomes known to the offeror late, he must communicate that fact immediately to the accepting party, on pain of liability for losses and damages' and according to article 443 'if the alienor knows of the vice or defect in the thing, he shall restitute what he received with losses and damages'.⁵⁰⁸

Therefore parties in Brazil are expected to observe the principle of good faith and its secondary contractual duties, such as *transparency* and *information* during negotiations.⁵⁰⁹ Those duties are of paramount importance at the pre-contractual stage as they imply that contracts shall be written in an intelligible manner to allow consumers to fully understand their contents.⁵¹⁰ They also establish that sellers and suppliers have to offer and publicise their products and services in a clear and honest way to enable consumers to make an informed decision.⁵¹¹ For this reason the Superior Court of Justice has reiterated that the information provided by sellers to consumers must be 'correct,

⁵⁰⁶ Article 186 of the Civil Code. See Rose (n 251) 47. Interpreters can also apply general rules of civil liability prescribed in articles 389 and 927 of the Civil Code.

⁵⁰⁷ See article 29 of the Consumer Protection Code. See also Castello Miguel (n 256) 74.

⁵⁰⁸ See Moura Vicente (n 290) 35. Rose (n 251) 89 and 92.

⁵⁰⁹ Marques, 'Notas sobre o Sistema de Proibição de Cláusulas Abusivas no Código Brasileiro de Defesa Do Consumidor: Entre a Tradicional Permeabilidade da Ordem Jurídica e o Futuro Pós-Moderno do Direito Comparado' (n 125) 48-49.

⁵¹⁰ Peixoto (n 295) 163. See article 6, III of the Consumer Protection Code. In MS 5986/DF (13/10/1999) the Superior Court of Justice observed that suppliers have to provide appropriate and clear information about products and services including their price. The same court recently decided in REsp 1293006/SP (29/06/2012) that an insurance company cannot be exempted to cover damages caused by a 'larceny' on the basis that the contract covers only 'compound larceny' because there was a failure to provide adequate information about the insurance cover and the use of a legal and technical expression also indicates that the clause is abusive.

⁵¹¹ Consequently in line with good faith consumers have the right to withdraw from a contract in case of distance selling because they did not have the opportunity to examine the product (see article 49 of the Consumer Protection Code). See Nobre Júnior, 'A Proteção Contratual no Código do Consumidor e o Âmbito de sua Aplicação' (n 469) 285.

clear, accurate, noticeable and in Portuguese language'.⁵¹² Sellers will be bound by this information in the conclusion of the contract on pain of frustrating the consumer's legitimate expectations.⁵¹³

The non-compliance with the above duties may imply the invalidation of contractual terms⁵¹⁴ or the imposition of other *sanctions* (e.g., fine or imprisonment for the practise of misleading advertisement).⁵¹⁵ Furthermore the Consumer Protection Code expressly provides that suppliers are bound by 'declarations of will' given in *pre-contracts* and that judges may grant specific performance if necessary to ensure a practical result equivalent to the compliance of the obligations ('to do' or 'not to do') assumed in those declarations in case suppliers fail to fulfil them.⁵¹⁶

The application of the general clause of good faith is not only extended to the negotiation stage but it also covers the *post-contractual stage* because there are duties that should remain after the contractual performance, such as the duty of *confidentiality*. The latter provides that a seller is not allowed to share a buyer's personal information without his authorisation following the performance of the contract.⁵¹⁷ The *duty of care* also remains applicable at this stage. For instance there are risks that may be only identified after the performance of the contract, but suppliers are still liable for defects that can endanger the health and safety of the consumers (this is the basis for the 'recalls' of defective products).⁵¹⁸ Furthermore the Consumer Protection Code expressly prescribes that in the collection of debts the consumer in default shall not be exposed to ridicule or any type of embarrassment or threat (harassment of debtors).⁵¹⁹

⁵¹² See article 31 of the Consumer Protection Code. The Superior Court of Justice determined in REsp 586316/MG (19/03/2009) the application of such 'duty to inform' in the sale of products containing gluten ('allergy information').

⁵¹³ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 223 and 243. In REsp 590336/SC (21/02/2005) the Superior Court of Justice decided that an insurance company must pay the agreed indemnification in the occurrence of the insured event based on the trust between parties and the principle of good faith which protects the consumer expectations.

⁵¹⁴ According to article 46 of the Consumer Protection Code the contract will not bind the consumer if he was not given the opportunity to have prior knowledge of its contents or if it was drafted in a way to hinder the understanding of its meaning and scope.

⁵¹⁵ See articles 37 and 67 of the Consumer Protection Code

⁵¹⁶ See Nunes Júnior and De Matos (n 75) 221. See also articles 48 and 84 of the Consumer Protection Code.

⁵¹⁷ Nobre Júnior, 'O Princípio da Boa-Fé e o Novo Código Civil' (n 89) 83.

⁵¹⁸ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 233. For instance the manufacturer has a duty to *recall* defective cars in order to be repaired if they endanger the safety of the buyer. See REsp 1010392/RJ (13/05/2008) and articles 8 to 10 of the Consumer Protection Code.

⁵¹⁹ Article 42 of the Consumer Protection Code.

3.4. Analysing the differences and similarities of the legislative controls on unfairness in consumer contracts in England and Brazil

At first sight one of the most evident differences between the legislative controls on unfairness in B2C contracts in England and Brazil is that in the Brazilian legislation these controls are concentrated in Codes (e.g., Civil Code and Consumer Protection Code); whereas in English law the statutory controls can be found in different pieces of legislation, such as UCTA 1977 and the UTCCR 1999.

In principle this could lead to the conclusion that the Brazilian legal system is more coherent than the English legal system as the piecemeal solutions of the latter may be tainted by overlapping and inconsistencies. However the Brazilian law just like the English law also have conflicts among its internal provisions, as will be analysed in chapter 5.

3.4.1. Defining consumer

The first part of the consumer's definition in article 2 of the Brazilian Consumer Protection Code is compatible with the definition in reg. 3(1) of UTCCR 1999 as both regard consumers as *natural* persons.⁵²⁰ Furthermore, according to both provisions consumers should be at the end of the market chain and do not have the purpose of making profit.

However article 2 proceeds to include '*legal persons*' in its consumer definition. Therefore the Brazilian law, similarly to UCTA, may also regard a business as a consumer when it is not making the contract 'in the course of a business'. Such wider definition may be preferable when companies or legal persons are vulnerable in asymmetric contracts and exposed to harmful terms.⁵²¹

3.4.2. Burden of proof

In England the burden of proof of the unfairness of a term rests on the consumer or a qualifying body (reg. 12) because the UTCCR 1999 did not 'make any provision to displace

⁵²⁰ According to art. 2 of the Consumer Protection Code, consumer is 'every *natural* or *legal* person who acquires or uses products or services as a final recipient'; similarly in the words of reg. 3(1) of the UTCCR 1999 consumer is 'any *natural* person who is acting for purposes which are outside his trade, business or profession'.

⁵²¹ E.g., small businesses. See chapter 4.

the normal burden of proof resting on the claimant',⁵²² except from reg. 5(4) which stipulates that 'it shall be for any seller or supplier who claims that a term was individually negotiated to show that it was'. On the other hand, under UCTA it is the party claiming that the term satisfies the requirement of reasonableness (normally a business) who has to prove it. Similarly, the Law Commission recommended that the burden of showing the fairness of a term should fall on the business which will facilitate the access of consumers to the protection offered by the relevant legislation.⁵²³

By comparison in Brazil article 6, VIII of the Consumer Protection Code provides that if the judge considers that the claim is *verisimilar* or that the consumer is vulnerable, he can invert the burden of proof in favour of the consumer. In addition article 51, VI of the same Code considers a term abusive, hence void, when it establishes the inversion of the burden of proof to the detriment of the consumer. The latter provision is similar to paragraph 1(q) of Schedule 2 of the Regulations which regards as unfair a term that imposes on the consumer the burden of proof 'which, according to the applicable law, should lie with another party to the contract'.

3.4.3. Transparency and interpretation favourable to consumers

According to both legislatures, terms have to be written in an understandable way, because consumers should be aware of their contents to be able to make a conscious decision. For this reason suppliers have the obligation to provide all relevant information to consumers, which is in line with the principle of *transparency* in consumers' relationships.⁵²⁴ 'Transparency in consumer contracts has an important role to play in ensuring that markets operate effectively and that both parties in a business to consumer transaction can have an element of trust in each other'.⁵²⁵

Under article 46 of the Consumer Protection Code 'contracts which regulate consumer's relationships do not oblige consumers if they were not given the opportunity to have prior knowledge of their contents or if the respective documents are drafted in a way to hinder

⁵²² Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 3.79.

⁵²³ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 3.130.

⁵²⁴ Collins proposed that this duty to disclose information purports to 'assist the successful completion of the contracts by requiring a minimal and inexpensive mutual duty to safeguard the other contracting party's interests', which is directly related to an implied duty of *cooperation* between parties. See Hugh Collins, 'Implied Duty to Give Information during Performance of Contracts' (1992) 55(4) MLR 556, 556-557.

⁵²⁵ See Response by the Law Society to Law Commission, *Unfair Terms in Consumer Contracts: A New Approach? Issues Paper* (Law Com No 292, 2012) para 6.

the understanding of its meaning and scope.⁵²⁶ Similarly, according to Schedule 2 paragraph 1(i) of the UTCCR 1999 it may be regarded as unfair a term which has the object or effect of 'irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract'.

In addition, in Brazil under article 54 §3 of the Consumer Protection Code 'the terms of contracts of adhesion shall be clear and written in plain and legible font in order to facilitate their understanding by the consumer' and article 47 of the same Code states that 'contractual clauses shall be interpreted in favour of the consumer'. By comparison, reg. 7(1) of the UTCCR 1999 prescribes that 'a seller or supplier shall ensure that any written term of a contract is expressed in plain, intelligible language' and although there is no provision of sanction in case of its non-compliance, if the unintelligibility results in uncertainty about the meaning of the term, then 'the interpretation which is most favourable to the consumer shall prevail (reg. 7(2)).⁵²⁷

More recently the Law Commission proposed in the review of its 2005 recommendations that only terms which are *transparent* and *prominent* should be exempted from the fairness test.⁵²⁸⁵²⁹ Furthermore the *Proposal for a Regulation on a Common European Sales Law* (CESL) prescribed that the assessment of the unfairness of a contract term has to take into account whether the trader complied with the 'duty of transparency' which requires terms to be 'drafted and communicated in plain, intelligible language'. Terms that are regarded as unfair will not bind the parties.⁵³⁰

Marques suggested that this duty of transparency caused a shift from the *caveat emptor* rule ('let the buyer beware') to the *caveat venditor* rule ('let the seller beware') in B2C

⁵²⁶ See also article 4 of the Consumer Protection Code.

⁵²⁷ Additionally reg. 6(1)(c) of the CPRs prescribes that a commercial practice is a misleading omission if it provides material information in a manner which is unclear, unintelligible, ambiguous or untimely.

⁵²⁸ See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) paras 8.2 and 8.4. This concept of 'transparency' is also employed in the 'fair and reasonable test' of its proposed *Unfair Contract Terms Bill* (Law Com No 292, 2005). According to clause 14(1) 'whether a contract term is fair and reasonable is to be determined by taking into account: the extent to which the term is transparent' (...). Clause 14(3) defines 'transparent' as 'expressed in reasonably plain language, legible, presented clearly, and readily available to any person likely to be affected by the contract term or notice in question'.

⁵²⁹ 'The UK position on the role of transparency in legitimizing substantively unfair terms is uncertain and unstable'. According to Willet in England it is unclear whether consumers are 'protected from substantively unfair terms' if terms are clear or transparent. See Chris Willett, 'The Functions of Transparency in Regulating Contract Terms: UK and Australian Approaches' (2011) 60 ICLQ 355, 355-356.

⁵³⁰ See article 79, 82 and 83 of the CESL.

contracts.⁵³¹ This means that presently is the seller or supplier who has the duty to provide information about the products, services and terms of the contract; hence the consumer no longer has to actively look for the relevant information on pain of not being able to complain later.⁵³² In other words now the 'consumer protection ethic' prevails over the 'consumer self reliance ethic' as the latter provided that consumers had to protect their own interests.⁵³³

3.4.4. Consequences of the unfairness of a term

In Brazil the Consumer Protection Code (art. 51) prescribes that abusive clauses may be declared void *ex officio* by courts; hence judges can take action of their own accord (without the request of the parties).⁵³⁴ Similarly article 6(1) of Directive 93/13/EEC and reg. 8(1) provide that an unfair term in a B2C contract will not bind consumers and recently the EU Court of Justice in the case *Banco Español de Crédito SA v Joaquín Calderón Camino*⁵³⁵ maintained that article 6(1) should be interpreted:

'to mean that national courts are required to raise, of their own motion, the issue as to whether an unfair term is void and/or inapplicable, even where none of the parties to the contract has made an application to that effect'.⁵³⁶

In the same case, the Court of Justice determined that national courts should be limited to exclude the application of terms tainted by unfairness; therefore judges cannot revise their contents otherwise sellers and suppliers would be 'tempted to use those terms' with the knowledge that even if the latter were considered invalid they still could be modified by courts and applied.⁵³⁷

Article 51 §2 of the Consumer Protection Code in its turn prescribes that the invalidation of abusive clauses does not invalidate the contract as a whole unless it results in an

⁵³¹ Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 225-226.

⁵³² The Superior Court of Justice maintained that the duty to inform requires a proactive behaviour from sellers and suppliers because the Consumer Protection Code rejects the *caveat emptor* rule and the silence (total or partial) which may mislead the consumer. See REsp 586316/MG (19/03/2009) and article 31 of the Consumer Protection Code.

⁵³³ Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 413-414.

⁵³⁴ See Grinover and others (n 34) 571-572 and Marques, *Contratos no Código de Defesa do Consumidor* (n 338) 245. According to the Superior Court of Justice courts can review *ex officio* clauses considered abusive in line with article 51, IV. See AgRg no REsp 506650/RS (03/11/2003).

⁵³⁵ Case C-618/10 *Banco Español de Crédito SA v Joaquín Calderón Camino* [2012] OJ C227/5 .

⁵³⁶ Ibid. para 33.

⁵³⁷ Ibid. paras 65-69.

excessive burden for one of the parties.⁵³⁸ By comparison under reg. 8(2) the rest of the contract will continue binding the parties if it is capable of continuing in existence without the unfair term. Consequently in England the severance of offending parts of a contract may be employed in order to keep the rest of it enforceable.⁵³⁹

Therefore there is a tendency in both jurisdictions towards the preservation of contracts when possible; hence the English and Brazilian law are in agreement with a 'universal legislative trend that aims to limit the invalidation of terms in order to keep the legal transactions "alive".⁵⁴⁰

3.4.5. Strict and qualified obligations

In English law there are contractual obligations that are considered *strict*, which means that a party must achieve a certain result otherwise he will be in breach of contract.⁵⁴¹ Those strict obligations can be compared with the *qualified* obligations according to which a party will achieve the purpose of the contract if he takes reasonable care or exercise reasonable skill in its performance (e.g., s. 2 of UCTA).

In Brazil there is a similar dichotomy between the so-called '*obligation of means*' and the '*obligation of result*'. According to the first type of obligation, the party should employ his skills diligently and honestly towards an end, but he is not obliged to achieve the expected result; differently from the second type where the party must obtain a certain result otherwise he will be in breach of contract.⁵⁴² For instance, in an obligation of means, although a doctor cannot guarantee that he will cure a disease, he should do everything possible to heal the patient. On the other hand, in the Brazilian jurisdiction the

⁵³⁸ This is known as 'principle of preservation' (of the contracts) which is based on the idea that judges should derive a maximum utility from contractual terms and consider them valid always when possible in the context of consumer contracts (see also article 170 Civil Code). See Figueiredo and Figueiredo (n 272) 409.

⁵³⁹ Nonetheless 'severance is allowed only if it is consistent with the public policy which made the contract containing the offending part illegal. If the whole contract is tainted by the illegality, severance cannot save it'. See Poole, *Textbook on Contract Law* (n 78) 274 and 592.

⁵⁴⁰ Antonio Janyr Dall'agnol Júnior, 'Cláusulas Abusivas: A Opção Brasileira' (1994) Porto Alegre, mar, v. 21, f. 60 *Ajuris* 129, 140.

⁵⁴¹ See UCTA 1977 ss. 6 and 7 (specific provisions) and s. 3 (general provision). See also Poole, *Textbook on Contract Law* (n 78) 244.

⁵⁴² Luiz Roldão Freitas Gomes, 'Elementos de Responsabilidade Civil' in RP Lira (ed) *Curso de Direito Civil* (Renovar 2000) 347.

surgeon has to achieve the promised result in a purely aesthetic plastic surgery. This is the understanding of the Superior Court of Justice.⁵⁴³

In England, in its turn, the standard of performance required in *qualified* obligations 'has long been regarded as the appropriate standard for professional people such as doctors and lawyers, whose work make it impossible to guarantee a result.'⁵⁴⁴

3.4.6. Pre-emptive challenges

The Unfair Terms in Consumer Contracts Regulations 1994 followed by the UTCCR 1999, introduced a significant mechanism of consumer protection: the *preventive* action by the Office of Fair Trading (OFT),⁵⁴⁵ the Director General of Fair Trading and qualifying bodies (Schedule 1) who can request traders to remove or amend unfair terms. The fact that those bodies can apply for an injunction to prevent continued use of unfair terms (reg. 12) has been deemed very useful in the context of B2C contracts because 'ordinary consumers do not normally resort to the courts'.⁵⁴⁶ Such preventive protection however is not applicable to B2B contracts, in which disputes are analysed individually according UCTA.

The Brazilian Consumer Protection Code also prescribes preventive protection for consumers either individually or collectively;⁵⁴⁷ hence in Brazil the above protection is also limited to consumer contracts. The *consumers' basic rights* include the effective prevention and redress for material, moral, individual, collective and diffuse damages.⁵⁴⁸ In addition any type of legal action capable of providing adequate and effective protection to consumers' rights and interests, such as 'provisional remedies', is allowed (article 83).⁵⁴⁹

⁵⁴³ The Superior Court of Justice 'has understood that in the case of plastic surgery merely aesthetic, the obligation is of result not of means. Consequently the claimant does not need to prove that the defendant was at fault, but only that he did not achieve the promised result'. See REsp 236708/MG (10/02/2009).

⁵⁴⁴ Poole, *Textbook on Contract Law* (n 78) 281.

⁵⁴⁵ The OFT is a governmental department of the United Kingdom which aims to 'make markets work well' for consumers, enforcing the consumer protection and competition law. See <<http://www.offt.gov.uk/about-the-offt/>;jsessionid=746885F446EEFB86E20360BAF53F13AE> accessed 10 October 2010.

⁵⁴⁶ W.C.H. Ervine, 'The Unfair Terms in Consumer Contracts Regulations in Courts' (2004) SLT 127, 130.

⁵⁴⁷ See arts. 81 and 51 §4 of the Consumer Protection Code.

⁵⁴⁸ See article 6, VI and VII of the Consumer Protection Code.

⁵⁴⁹ See articles 796 to 889 of the Code of Civil Procedure (Act 5869/1973). See also Dall'agnol Júnior (n 540) 141.

Furthermore the Department of Justice and other bodies listed in article 82 (Public Prosecutors, Federal Government, States, Municipalities, the Federal District, governmental entities and agencies and consumers' associations) can exercise pre-emptive challenges through the use of a *public civil action*⁵⁵⁰ to protect collective rights which have not been affected yet.⁵⁵¹ Ferreira called such preventive powers as 'abstract controls' of unfairness which may be employed before the actual use of abusive clauses; as opposed to 'concrete controls' which aim to declare void unfair terms or clauses that are in fact contrary to the principles of consumer protection.⁵⁵²

3.4.7. Investigative powers

Under reg. 13 of the UTCCR 1999 the Director General and the public qualifying bodies can require copies of pre-formulated standard contracts and information about their use to facilitate the consideration of a complaint concerning the unfairness of a term; or to ascertain the compliance with an undertaking or court order. However a person cannot be compelled to supply any document or information that he could refuse to produce in civil proceedings before the court (reg. 13(5)).

In addition the *Consumer Protection from Unfair Trading Regulations 2008* give powers to the OFT and local weights and measures authorities to investigate a possible breach of the Regulations. These powers include: making test purchasers (reg. 20), inspecting any goods (reg. 21) and entering premises (reg. 22).

In Brazil the *Public Civil Action Act* (Act 7347/1985) provides that public bodies and consumer associations (art. 5) can commence a civil investigation and request from public or private bodies certificates, information, tests or expert evidence in order to establish whether there are grounds to propose a public civil action (art. 8 §1).⁵⁵³ Only when the law imposes confidentiality a person can refuse to supply a certificate or information, in which case judges can request it.

⁵⁵⁰ See Act 7347/1985.

⁵⁵¹ REsp 175645/RS (30/04/2001).

⁵⁵² See Ferreira (n 278) 190.

⁵⁵³ The refusal, delay or omission in the supply of documents and information are regarded as crime punishable by imprisonment from 1 to 3 years plus fine (art. 10 of the Act 7347/1985).

3.4.8. Enforcement

In line with reg. 10 to 12 of the UTCCR 1999 the Director General of Fair Trading (DGFT) has a duty to consider a complaint concerning the unfairness of a contract term drawn up for general use. The DGFT and qualifying bodies (Schedule 1) may apply for an *injunction* (including an interim injunction) in the High Court or county court to prevent the continued use of unfair terms or of a term having like effect in standard form contracts.

Similarly, according to part 4 of the *Consumer Protection from Unfair Trading Regulations 2008* (CPRs), the OFT and local weights and measures authorities have a duty to enforce the CPRs provisions when there are breaches of the prohibition on unfair commercial practices that may imply in criminal offences. 'The prohibitions will be enforceable through the procedure for the enforcement of Community infringements in Part 8 of the Enterprise Act 2002.'⁵⁵⁴

Part 8 of the *Enterprise Act 2002* (s. 210 onwards) provides that the Office of Fair Trading, every local weights and measures authority in Great Britain and other 'enforcers'⁵⁵⁵ can seek *enforcement orders* against businesses that are in breach of certain consumer legislation.⁵⁵⁶ Those enforcement actions can be taken against 'community infringements' that are breaches of UK legislation that give effect to specified EU Directives and which may harm the collective interests of consumers.⁵⁵⁷ Those Directives are listed in Schedule 13 of the Act that includes the *Directive on Unfair Terms in Consumer Contracts* (93/13/EEC) and the *Directive on Unfair Commercial Practices Directive* (2005/29/EC).

The court can order the cessation and non-repetition of the infringement or accept undertakings from the business that it will cease the infringing conduct. If the business fails to comply with the enforcement order or breach an undertaking to the court, it may

⁵⁵⁴ See recital 2 of the 'Explanatory note' of the CPRs.

⁵⁵⁵ The Secretary of State can designate sectoral regulators and consumer protection bodies as enforcers.

⁵⁵⁶ The enforcer must consult with the business before recourse to the court for the purpose of achieving the cessation of the infringement and ensuring that it will not be repeated (s. 214) through the acceptance of undertakings from the business that it will cease the infringing conduct.

⁵⁵⁷ Enforcement actions can also be taken against 'domestic infringements' that are breaches of UK laws or contracts of a type specified by the Secretary of State for Trade and Industry (SoS) which are committed in the course of a business and harm the collective interest of consumers. See Office of Fair Trading, *Overview of the Enterprise Act: The Competition and Consumer Provisions* (June 2003) 23.

be considered in contempt of court, which could lead to a fine or imprisonment for up to two years.⁵⁵⁸

By comparison, the Brazilian Consumer Protection Code expressly prescribes civil, penal and administrative mechanisms to prevent injustices and arbitrariness which may negatively affect consumers.⁵⁵⁹ As seen previously all types of legal actions capable of providing adequate and effective protection to consumers are permitted.⁵⁶⁰ In addition judges can determine measures that ensure a practical result equivalent to the performance of an obligation ('to do or not to do') which vary from the imposition of daily fines to the use of police intervention.⁵⁶¹

Furthermore articles 61 to 80 prescribe a list of criminal offences that are punishable by imprisonment for up to two years and fine.⁵⁶² For instance it is crime to omit information about the hazards of a product or mislead the consumer about the characteristics and quality of a product or service.

In addition, Act 8137/1990 defines 'crimes against the economic order and consumer relations', which include practices that are detrimental to the market competition and may limit the consumer choice and freedom of contract.⁵⁶³ Those crimes are punishable by fine or imprisonment for up to eight years.

3.4.9. Harmonisation of consumer protection (EU *versus* Mercosul)

As seen earlier, the consumer *acquis* is under review and there is a trend towards the harmonisation of consumer protection in the European Union. As a consequence English consumer legislation may be increasingly shaped by the European law.

⁵⁵⁸ See Office of Fair Trading, *Enforcement of Consumer Protection Legislation* (June 2003) [3.47] and [3.51].

⁵⁵⁹ Ferreira (n 278) 178. See articles 55 to 80 of the Consumer Protection Code.

⁵⁶⁰ See article 83 of the Consumer Protection Code.

⁵⁶¹ See article 84 of the Consumer Protection Code. Other measures include search and seizure, removal of things and persons, undoing construction works and prevention of harmful activities (§5).

⁵⁶² Other sanctions may be adopted cumulatively or alternately, such as: temporary suspension of rights, publication in the media about the conviction and community services (art. 78).

⁵⁶³ For instance according to article 4 'it constitutes crimes against the economic order (...) I – the abuse of economic power, through the domination of the market or elimination of all or part of the competition'. The crimes against the consumer relations include 'inducing the consumer or user in error through indication or false or misleading statement about the nature or quality of the goods or service, through any means, including advertising' (art. 7, VII).

Similarly in the Mercosul there was an attempt to harmonise the consumer law of its Member States through a *Consumer Protection Protocol of the Mercosul*.⁵⁶⁴ However, as examined earlier, the latter did not come into force because the protection offered by the protocol was inferior to the protection provided by the Brazilian Consumer Protection Code and any reduction of fundamental rights in Brazil is deemed unconstitutional.⁵⁶⁵ As a consequence until a common regulation to protect consumers within the Mercosul is approved, each Member State will keep applying its own legislation independently.⁵⁶⁶

Marques contended that such *uniform legislation* of consumer protection may not be viable in the context of the Mercosul because the latter does not have a 'supranational court of law which holds the monopoly of the interpretation of the common rules'.⁵⁶⁷ In addition the 'Consumer Protection Protocol' imposed clauses containing *maximum* levels of protection which did not suit the distinct realities of each Member State (e.g., different levels of industrialisation).⁵⁶⁸ By comparison, the European Union has its Court of Justice and most of its consumer directives (such as the Directive 93/13/EEC) used to contain *minimum harmonisation clauses* that respected higher levels of protection offered by Member States.⁵⁶⁹ Marques suggested that the Mercosul should adopt a similar technique as applied by the EU because such minimal regulation respects the individual characteristics of the Member States.⁵⁷⁰ However more recently the EU has changed its approach in favour of the adoption of *maximum harmonisation clauses* in a bid to improve the consistency among the regulations of its members.⁵⁷¹

Nonetheless any level of harmonisation of the consumer protection within the EU and the Mercosul is an important step to facilitate cross-border transactions and enhance the

⁵⁶⁴ The draft of the 'Consumer Protection Protocol in the Mercosul' was proposed by the Technical Committee number 7 (CT 7) of the Mercosul in 1997.

⁵⁶⁵ Fabrício Castagna Lunardi, 'A Defesa do Consumidor no Mercosul: Necessidade de Harmonização das Legislações' ano 11, n. 1024 <<http://jus.com.br/revista/texto/8268>> accessed 23 September 2011.

⁵⁶⁶ See article 2 of Resolution 126/94.

⁵⁶⁷ Cláudia Lima Marques, 'União Européia legisla sobre Cláusulas Abusivas: um Exemplo para o Mercosul' (1997) São Paulo, jan./mar., n. 21, *Direito do Consumidor* 300 (n 568) 301. See article 8 of the Directive 93/13/EEC.

⁵⁶⁸ At the time that the Protocol was proposed Uruguay and Paraguay did not have a systematic and comprehensive legislation in the context of consumer protection and the Argentine legislation did not offer the same level of protection as the Brazilian legislation. See *Ibid.* 301.

⁵⁶⁹ *Ibid.* See article 8 of the Directive 93/13/EEC. Similarly Gardini observed that 'contrary to what happens in Europe, no supranational organs, such as the European Commission or the European Court of Justice, exist in MERCOSUR. Therefore, integration has not been promoted as much by regional institutions as it has by member states and their leaders, upon whom the entire process has been highly dependent'. See Gardini (n 42) 685.

⁵⁷⁰ Marques, 'União Européia legisla sobre Cláusulas Abusivas: um Exemplo para o Mercosul' (n 567) 302.

⁵⁷¹ Department for Business Innovation & Skills (BIS), *Review of the Eight EU Consumer Acquis Minimum Harmonisation Directives and their Implementation in the UK and Analysis of the Scope for Simplification* (URN 05/1951, 2005).

consumer confidence in their common markets. The absence of a clear transnational protection may discourage consumers from entering transactions outside their own country, which may jeopardise the purpose behind the existence of a common market.

Presently the European Union through its consumer *acquis* is ahead of its Latin American counterpart in terms of offering effective ways to deal with conflicts in cross-border transactions.⁵⁷² Although the Mercosul proposed the *Protocol of Santa Maria* which purported to regulate consumer protection in disputes involving more than one Member State,⁵⁷³ this Protocol did not come into force because it was subjected to the approval of the 'Consumer Protection Protocol of the Mercosul' which did not happen.⁵⁷⁴

Despite the above differences between the EU and the Mercosul, there have been negotiations for a 'Bi-Regional Association Agreement' or 'EU-Mercosul Free-Trade Agreement'.⁵⁷⁵ However their different levels of consumer protection may be a hindrance to these negotiations; thus the Mercosul should consider implementing the aforementioned protocols or finding alternative ways to improve the protection of consumers in cross-border contracts in the forthcoming years.⁵⁷⁶

3.5. Conclusion

The numerous differences in cultural, social and economic aspects between England and Brazil have influenced the development of their legislation. Although one could expect that both legislatures would be completely distinct from each other, they have similar approaches in relation to the control on unfairness in B2C contracts. Zweigert and Kötz pointed out that often 'different legal systems give the same or similar solutions (...) to the same problems of life, despite the great differences in their historical development, conceptual structure, and style of operation'.⁵⁷⁷

⁵⁷² Klausner (n 38) 31. Differently from the EU, the Mercosul does not have a 'community law' but a 'law of integration' which is "in between" international law and community law'. See Belen Olmos Giupponi, 'International Law and Sources of Law in MERCOSUR: an Analysis of a 20-year Relationship' (2012) 25(3) LJIL 707, 732.

⁵⁷³ John A.E. Vervaele, 'Mercosur and Regional Integration in South America' (2005) ICLQ 387, 402.

⁵⁷⁴ See article 18 of the Protocol of Santa Maria.

⁵⁷⁵ Negotiations between the EU and the Mercosul were launched in 1999, suspended in October 2004 and re-launched in 2010. Recent rounds of negotiations involving delegations of both regions took place in March and July of 2012. See <<http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/regions/mercosur/>> accessed 17 July 2012. See also Foreign Affairs Committee, *UK-Brazil Relations: Ninth Report of Session 2010-12* (HC 2010-12, 949) and Foreign Affairs Committee, *UK-Brazil Relations: Response of the Secretary of State for Foreign and Commonwealth Affairs* (Cm 8237, 2011).

⁵⁷⁶ Klausner (n 38) 71.

⁵⁷⁷ Zweigert and Kötz (n 48) 39.

Similarities between legal solutions of both legal systems may result in part from the fact that over the centuries countries which adopt the *civil law* and *common law* systems have constantly interacted with each other, resulting in the approximation of their law to a certain extent.⁵⁷⁸ According to David those legal families have developed a '*shared vision of justice*' and consequently they 'have often produced very similar answers to common problems'⁵⁷⁹ as it can be observed from the solutions offered by England and Brazil to unfairness in consumer contracts.⁵⁸⁰

To begin with, the definition of 'unfair terms' in the English and Brazilian legislation share some remarkable similarities. According to article 51, IV of the Consumer Protection Code and reg. 5(1) of the UTCCR a term may be regarded as 'unfair' or 'abusive' if there is a *significant imbalance* between the rights and obligations of the parties or an *unreasonable disadvantage* to the *detriment of the consumer*. Additionally the *inconsistency with good faith* may also indicate a lack of fairness.

Furthermore Schedule 2 of the Regulations and article 51 of the Consumer Protection Code contain similar *indicative* and *non-exhaustive lists* of terms that are likely to be unfair or abusive. Most of the situations prescribed by Schedule 2 can find corresponding provisions in the Consumer Protection Code and the Civil Code. In addition the Brazilian Senator Antonio Valadares proposed a Bill (PLS 42/2007) which aims to include subsections in article 51 to cover cases that are prescribed by Schedule 2 but are nowhere to be found in the Brazilian law.⁵⁸¹

⁵⁷⁸ Due to their affinities it is possible to include them under a common 'western law' family. David and Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (n 16) 25.

⁵⁷⁹ Ibid.

⁵⁸⁰ Rawls observed that people who live in society recognise that they are bound by rules of conduct and that a *shared* conception of justice and fairness guides people's conduct to act in *cooperation* in order to achieve mutual benefits taking into account the needs of the less advantaged. See Rawls (n 69) 3-13. Indeed the Brazilian and English legal systems have converged on the adoption of a *cooperative ethic* in the context of consumer contracts. It is possible to argue that such cooperative ethic is also applicable to a certain extent in the context of business contracts. See *St Albans City & District Council v International Computers Ltd* [1995] [1996] 4 All ER 481 (CA), [1995] FSR 686 and CC 92519/SP (04/03/2009).

⁵⁸¹ In the justification for the Bill (PLS 42/2007), the aforementioned Senator contended that the proposed subsections already exist in the context of the European Union (i.e., Directive 93/13/EEC) and that a comparative analysis with the Brazilian Consumer Protection Code concluded that the above subsections were absent in the latter despite the fact that they can be perfectly adapted to the Brazilian context.

It is noteworthy that the existing similarities are not only a matter of coincidence. The list of article 51 was based on common problems which affect consumers in Brazil⁵⁸² and it was also considerably influenced by provisions of the *AGB-Gesetz*.⁵⁸³ Similarly the Directive 93/13/EEC (which introduced the list of unfair terms that can be found in the Regulations) also 'owed a considerable debt to German law' in particular to the same *AGB-Gesetz*.⁵⁸⁴ Therefore ultimately both lists were based on the same German piece of legislation which contained provisions that presumably satisfied the needs of Brazil and of the EU Member States.

The comparative table below demonstrate the existing equivalence between provisions of the Schedule 2(1) of the Regulations and provisions of article 51 of the Brazilian Consumer Protection Code, the Civil Code and the Bill PLS 42/2007:

Schedule 2(1) UTCCR 1999	Consumer Protection Code and others
(a) excluding or limiting the legal liability of a seller or supplier in the event of the death of a consumer or personal injury to the latter resulting from an act or omission of that seller or supplier.	Article 12: manufacturers, producers, constructors, and importers are liable, regardless the existence of culpability for the redress of damages caused to the health or safety of consumers (...)
(b) inappropriately excluding or limiting the legal rights of the consumer <i>vis-a-vis</i> the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him.	Article 51, I: prevent, exempt or reduces the suppliers' liability for defects of any nature in products and services or imply a renouncement or a waiver of rights.
(c) making an agreement binding on the consumer whereas provision of services by the seller or supplier is subject to a condition whose realisation depends on his own will alone.	Article 51, IX: leave to the supplier alone the option to conclude or not the contract, though obliging the consumer.
(d) permitting the seller or supplier to retain sums paid by the consumer where the latter decides not to conclude or perform the contract, without providing for	Article 51, II: take from the consumer the option for reimbursement of an amount already paid.

⁵⁸² In accordance with judicial precedents and bodies responsible for the consumer protection in Brazil, such as PROCONs (Consumer Protection Agencies) and Public Prosecutors. See Grinover and others (n 34) 535-536.

⁵⁸³ Gesetz zur Regelung des Rechts der Allgemeinen Geschäftsbedingungen (Act on Standard Contract Terms – AGBG) of 1976. See Ibid. 535-536 and 570.

⁵⁸⁴ See Youngs (n 110) 622-623. Annex of Directive 93/13/EEC which refers to its article 3(3) was introduced by Schedule 2 of the UTCCR 1999. See Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 3.60.

the consumer to receive compensation of an equivalent amount from the seller or supplier where the latter is the party cancelling the contract.	Article 51, XII: require from the consumer the reimbursement for expenses related to the collection of his debts, without giving the same right to the consumer against the supplier.
(e) requiring any consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation.	Bill (PLS 42/2007) proposes the inclusion of a new subsection in art. 51 which considers void terms which stipulate disproportionate penalties or damages to be paid by the consumer who fails to fulfil his obligations.
(f) authorising the seller or supplier to dissolve the contract on a discretionary basis where the same facility is not granted to the consumer, or permitting the seller or supplier to retain the sums paid for services not yet supplied by him where it is the seller or supplier himself who dissolves the contract.	Article 51, XI: authorise the supplier to unilaterally cancel the contract without giving the same right to the consumer. Article 51, II: take from the consumer the option for reimbursement of an amount already paid.
(g) enabling the seller or supplier to terminate a contract of indeterminate duration without reasonable notice except where there are serious grounds for doing so.	Article 720 (Civil Code): if the contract is of indeterminate duration, either of the parties may terminate it on 90 days' notice, provided that a period of time has passed that is compatible with the nature and size of the investment required from the agent.
(h) automatically extending a contract of fixed duration where the consumer does not indicate otherwise, when the deadline fixed for the consumer to express his desire not to extend the contract is unreasonably early.	Bill (PLS 42/2007) proposes the inclusion of a new subsection in art. 51 which considers void terms which authorise the automatic renewal of contracts of fixed duration, without the prior consent of the consumer.
(i) irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract.	Article 46: contracts governing consumer relations do not bind consumers when they have not been given the opportunity of being previously acquainted with their contents (...).
(j) enabling the seller or supplier to alter the terms of the contract unilaterally without a valid reason which is specified in the contract.	Article 51, XIII: authorise the supplier to unilaterally modify the contents or the quality of the contract after it has been entered into.
(k) enabling the seller or supplier to alter unilaterally without a valid reason any characteristics of the product or service to be provided.	Article 51, XIII: authorise the supplier to unilaterally modify the contents or the quality of the contract after it has been entered into.
(l) providing for the price of goods to be determined at the time of delivery or allowing a seller of goods or supplier of services to increase their price without in both cases giving the consumer the corresponding right to cancel the contract if the final price is too high in relation to the price agreed when the contract was	Article 51, X: allow the supplier to directly or indirectly change the price unilaterally.

concluded.	
(m) giving the seller or supplier the right to determine whether the goods or services supplied are in conformity with the contract, or giving him the exclusive right to interpret any term of the contract.	Bill (PLS 42/2007) proposes the inclusion of a new subsection in art. 51 which considers void terms which authorise exclusively the supplier to determine whether the contract has been fulfilled or to interpret it.
(n) limiting the seller's or supplier's obligation to respect commitments undertaken by his agents or making his commitments subject to compliance with a particular formality.	Article 932, III (Civil Code): employers and principals are liable for civil reparation for their employees, servants and agents in the performance of the work given to them, or by the reason of that work.
(o) obliging the consumer to fulfil all his obligations where the seller or supplier does not perform his.	Article 51, IX: leave to the supplier alone the option to conclude or not the contract, though obliging the consumer.
(p) giving the seller or supplier the possibility of transferring his rights and obligations under the contract, where this may serve to reduce the guarantees for the consumer, without the latter's agreement.	Bill (PLS 42/2007) proposes the inclusion of a new subsection in art. 51 which considers void terms which allow the assignment of the contract with the guarantees given by the consumer without his agreement.
(q) excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract.	Article 51, VII: determine a compulsory use of arbitration. Article 51, VI: establish the inversion of the burden of proof to the detriment of the consumer.

Despite the similarities between their legislation, the English and Brazilian legal systems may use different processes and concepts to limit harmful terms in B2C contracts which reflect the differences between their legal systems.⁵⁸⁵ Nonetheless 'in a shrinking world (...) there must be some virtue in uniformity of outcome whatever the diversity of approach in reaching that outcome'.⁵⁸⁶ Furthermore those distinctions may be mitigated by the growing influence of the European law over the English law. The ongoing movement towards the harmonisation of the consumer *acquis* and the European contract law may lead to the convergence of concepts and principles within the EU.⁵⁸⁷ This process may result in the approximation of the English law with the civilian Continental law. As a consequence it is possible to argue that the legislation which regulates B2C contracts in England and Brazil may become even more alike in the forthcoming years.

⁵⁸⁵ For instance although good faith is employed in both jurisdictions, its scope varies between them.

⁵⁸⁶ *Fairchild v Glenhaven Funeral Services Ltd* [2002] UKHL 22, [2003] 1 AC 32 [66].

⁵⁸⁷ According to Picat and Soccio *harmonisation* means 'a simple reconciliation between two or more legal systems in order to reduce or to remove certain contradictions'. See Picat and Soccio (n 365) 372.

CHAPTER 4. ANALYSIS OF THE LEGISLATIVE CONTROLS ON UNFAIRNESS IN SMALL BUSINESS CONTRACTS IN ENGLAND AND BRAZIL

4.1. Context

Following the analysis of the control on unfairness in the context of B2B contracts and B2C contracts, this chapter proceeds with the examination of the topic in small business contracts which as mentioned earlier are in a *grey area* between the other two categories of contracts.

The dichotomy between the above B2B contracts and B2C contracts was explicitly recognised in England by the Unfair Contract Terms Act 1977 and prior to that case law had already adopted different approaches to those contracts.⁵⁸⁸ By comparison the Brazilian law and its respective case law already recognised a differentiated regime to business transactions in its revoked Commercial Code of 1850 and subsequently it prescribed a special regime for consumers in its Consumer Protection Code of 1990.⁵⁸⁹

The recognition of differences between contracting parties implies the acknowledgement that parties are no longer presumably equals as they used to be considered in the classical model.⁵⁹⁰ The inequality and imbalance between parties may lead to distortions in the market relationships such as the imposition of exemptions clauses without a free consent of the weak party.⁵⁹¹

The need to protect the weak party justifies the state intervention in contracts, including B2B contracts where there is no actual equality between parties.⁵⁹² In principle small businesses are more likely to be affected by the imposition of unfair terms than large

⁵⁸⁸ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 43-44. See *Thornton v Shoe Lane Parking* [1971] 2 QB 163 (consumer case) and *British Crane Hire Corp Ltd v Ipswich Plant Hire Ltd* [1975] QB 303 (B2B contracts).

⁵⁸⁹ For example REsp 1447/RJ (19/02/1990) and REsp 9317/SP (07/10/1991) expressly applied provisions of the Commercial Code; whereas REsp 1230233/MG (03/05/2011) and REsp 59494/SP (01/07/1996) made express reference to provisions of the Consumer Protection Code.

⁵⁹⁰ It has become relevant to take into account whether the parties are consumers or businesses and whether they are vulnerable or not. See Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 44.

⁵⁹¹ According to Lord Denning the 'little man' in the face of a 'take it or leave it' situation would have no option but to take it and even if exemption clauses were written in clear words the 'little man' would never read or understand them. See *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] QB 284, 297.

⁵⁹² Castello Miguel (n 256) 124-125. See also *Phillips Hong Kong Ltd v Attorney General of Hong Kong* (1993) 61 BLR 41, 7. 'Except possibly in the case of situations where one of the parties to the contract is able to dominate the other as to the choice of the terms of a contract, it will normally be insufficient to establish that a provision is objectionably penal (...)'

businesses either because they normally do not have staff with legal expertise to fully understand the consequences of the clauses or they lack bargaining strength to negotiate terms with the other party.⁵⁹³

Nonetheless case law suggests that the imposition of harsh terms in B2B contracts is more concerned to the inequality of bargaining power than to the size of the business;⁵⁹⁴ hence the fact that a business is dealing on the other party's standard form of contract is more influential than whether the company is regarded as large or small.⁵⁹⁵ For instance a small supplier of an item which is essential to the production of a large firm is in a better position to negotiate terms than its larger counterpart.⁵⁹⁶

Therefore it may be more appropriate for the control over unfairness in SME contracts to be based on a more general '*vulnerability of the weak party*' criterion (resulting from the inequality of bargaining power) rather than on the classification of the weak party as 'small business' or 'consumer'.⁵⁹⁷

Only when demonstrated such asymmetry between parties that interventions may be considered legitimate in B2B contracts, because when parties are in an equal position they are able to protect their own interests⁵⁹⁸ and freedom of contract should prevail. As Dillon LJ observed 'courts would only interfere in exceptional cases where as a matter of common fairness it was not right that the strong should be allowed to push the weak to the wall'.⁵⁹⁹

⁵⁹³ Lewis concluded from an empirical research involving 40 small businesses in the UK that only a minority of them 'had a professional legal input into their contracts' and the ones which did not have such input considered 'themselves as contractually vulnerable'. Additionally their 'perceived legal problems' included the 'inadequacies in contractual arrangements including trading on others' unfavourable terms' and 'the high cost of legal advice and representation'. See Lewis (n 323) 84-93. See also Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 5.28.

⁵⁹⁴ The Law Commission identified 34 cases related to the use of standard terms in B2B contracts. In 19 of these cases courts have found clauses to be unreasonable under UCTA, but only 5 out these 19 cases 'specifically make reference to one party being a small business'. See Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 5.28.

⁵⁹⁵ *Ibid.* para 5.29.

⁵⁹⁶ Macaulay (n 164) 67.

⁵⁹⁷ Vincenzo Roppo, 'From Consumer Contracts to Asymmetric Contracts: A Trend in European Contract Law?' (2009) 5(3) ERCL 304, 346.

⁵⁹⁸ Castello Miguel (n 256) 124-125.

⁵⁹⁹ Dillon LJ also maintained that 'inequality of bargaining power must anyhow be a relative concept. It is seldom in any negotiation that the bargaining powers of the parties are absolutely equal (...). See *Alec Lobb Garages Ltd v Total Oil Great Britain Ltd* [1985] 1 WLR 173 (CA), 182-183.

4.2. Defining the 'small business'

The task of defining *small business* is not a straightforward one.⁶⁰⁰⁶⁰¹ Pieces of legislation that aim to regulate the relationships of this type of business may adopt different definitions according to their own purposes.⁶⁰² Furthermore one could say that SMEs have a 'hybrid' characteristic: although they are 'businesses' by nature they also share similarities with 'consumers' because often they are too weak to negotiate on an equal basis with large businesses.⁶⁰³

It may be an impossible task to propose a unanimous criterion for distinguishing the 'smallness' from the 'bigness' of a business 'because we don't know precisely where in the twilight to draw the line'.⁶⁰⁴ Nonetheless the application of differentiated regimes to those businesses has made necessary to define them, thus *qualitative* and *quantitative* criteria have been employed to this end. The Bolton Report of 1971⁶⁰⁵ was one of the first attempts to define small firms in the UK and applied both criteria. Its definition includes: independence from a larger business; personalised management and a relatively small share of the market.⁶⁰⁶

As will be observed later, various pieces of legislation are inclined to apply *quantitative criteria* such as the number of employees, turnover, balance sheet, production and gross revenue.⁶⁰⁷ This may result from the fact that those criteria can be objectively assessed;

⁶⁰⁰ 'Small business tends generally to be found among manufacturers of consumer products and retailers'. See D. G. Rice, 'Small Business and its Problems in the United Kingdom' (1959) 24(1) LCP 222, 234.

⁶⁰¹ The category of '*small businesses*' may also include '*medium and micro businesses*' depending on the legislation that regulates those enterprises in England and Brazil as well as in their respective common markets (EU and Mercosul). For instance the European Commission Recommendation 2003/361/EC and the Companies Act 2006 are applicable to micro, small and medium businesses. The same categories of businesses are covered by the Mercosul Resolution 59/98, whereas the Brazilian Declaratory Statute 123/2006 tackles only micro and small businesses.

⁶⁰² For example the Brazilian National Statute of Micro and Small Businesses (Declaratory Statute 123/2006) defines small businesses according to their *gross revenue* because its main concern is to simplify taxation of enterprises which need incentives due to their small revenue; whereas the Draft Bill of the Law Commission and the SEBRAE (Brazilian Support Service for Micro and Small Businesses) define those businesses based on their *number of employees* in order to facilitate their identification.

⁶⁰³ Larry T. Garvin, 'Small Business and the False Dichotomies of Contract Law' (2005) 40 Wake Forest L Rev 295, 297.

⁶⁰⁴ M.A. Adelman, 'Small Business - A Matter of Definition' (1960) 16 ABA Antitrust Section 18, 18. Similarly Rice observed that "'small," like "big," is a relative term. What is small in one context is large in another, and what is insignificant to one person appears immense to someone else.' Rice (n 600) 222.

⁶⁰⁵ Bolton Committee, *Report of the Committee of Enquiry on Small Firms* (Cmnd 4811, 1971).

⁶⁰⁶ The Report also adopted quantitative criteria based on the number of employees, turnover, production and so forth depending on the sector of the business. See Sara Carter and Dylan Jones-Evans, *Enterprise and Small Business: Principles, Practice and Policy* (2nd edn, Prentice Hall/Financial Times 2006) 8.

⁶⁰⁷ *Turnover* 'is the amount of sales of goods or services by a company'. *Balance sheet* 'is a statement of the financial position of a company at a particular time, such as the end of the financial year or the end of a quarter, showing the company's assets and liabilities'. *Gross revenue* is the 'total money received with no

hence they provide more certainty to commercial relationships. In order to calculate risks and avoid undesirable surprises, a party should be able to determine whether the other party is a SME because the latter may be subject to a different regime that can give rise to distinct legal consequences. In other words the other party while assessing the risks involved should be aware of the possibility that agreed terms may be susceptible to judicial interferences.

The Law Commission in its proposal for a unified regime to regulate unfair contract terms took into consideration this need 'to promote certainty and predictability' in business contracts.⁶⁰⁸ For this reason it defined small businesses by reference to the *number of employees* (nine or fewer)⁶⁰⁹ rather than the turnover as the former criterion is 'most likely to be accessible to the other contracting party'.⁶¹⁰ The proposed protection will cover the vast majority of businesses because companies with nine or fewer employees represent approximately 95% of the enterprises in the UK.⁶¹¹ In Brazil the SEBRAE (Brazilian Support Service for Micro and Small Businesses) also adopts the 'number of employees' criterion to classify the size of an enterprise because it can be easily identified by businesses which intend to apply for this institution's support.⁶¹²

However the criterion based on the number of employees in isolation may include some types of businesses (e.g., financial businesses) that can be considerably sophisticated. They may generate a substantial amount of money in spite of having few employees and

deductions'. See P. H. Collin, *Dictionary of Business* (4th edn, A & C Black 2006) 428 and 29. *Production* is the 'formal activity that adds value to goods and services (...) until used' or 'an organized process with specific goals'. See Friedman (n 114) 539.

⁶⁰⁸ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 2.26 and 5.76. Specialised categories of contracts that require a higher level of certainty (such as contracts relating to land and intellectual property) are excluded from the small business regime.

⁶⁰⁹ See clause 27 of the *Unfair Contract Terms Bill*. Schedule 4 of the Bill defines employee as 'an individual who works in the business under a contract of employment or a contract for services' (item 8) and stipulates how the number of employees in a business should be calculated.

⁶¹⁰ According to the Law Commission *turnover* may be not an accurate guide to the size of the business because depending on the sector it does not reflect its profit. Moreover it is difficult to be ascertained by the other party and it would need to be reassessed in each transaction. The turnover of a business can be also market-sensitive information that cannot be widely available. Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 5.36 to 5.38.

⁶¹¹ According to the 'Business Population Estimates for the UK and Regions 2012' at the start of 2012 there were approximately 4.8 million enterprises in the private sector: 74.16% with no employees and 20.84% with 1 to 9 employees. See <<http://www.bis.gov.uk/assets/BISCore/statistics/docs/B/12-92-bpe-2012-stats-release.pdf>> accessed 26 December 2012.

⁶¹² For instance in the sector of trade and services, micro enterprises are the ones with 9 or fewer employees and small enterprises the ones with 49 or fewer employees; whereas in the sector of industry those numbers double. See SEBRAE, *Anuário do Trabalho na Micro e Pequena Empresa: 2010-2011* (2011). SEBRAE is a non-profit private entity of public interest that aims to promote competitiveness and sustainable development of micro and small businesses in Brazil. It supports the opening and expansion of businesses that fulfil the above criteria. See <<http://www.sebrae.com.br/customizado/sebrae/institucional/quem-somos/sebrae-um-agente-de-desenvolvimento>> accessed 20 April 2011.

consequently do not require special protection.⁶¹³ In order to avoid potential unjust situations the *headcount criterion* may be complemented by another criterion that reflects the wealth of the company (e.g., turnover and gross revenue).⁶¹⁴

For instance *Recommendation 2003/361/EC* of the European Commission adopts *financial ceilings* (annual turnover and balance-sheet total) in addition to the headcount of the enterprises to define them as micro, small and medium-sized.⁶¹⁵ Those definitions entered into force in 2005 and have been applied by EU Member States, the European Investment Bank (EIB) and the European Investment Fund (EIF) 'without any notable difficulty'.⁶¹⁶ The European Commission was planning to open a consultation in 2012 to discuss whether such SME definitions need to be revised and any changes should be implemented in 2013, but so far this consultation has not materialised.⁶¹⁷

England has incorporated the Recommendation's definition into its domestic legislation such as the Community Investment Tax Relief (Accreditation of Community Development Finance Institutions) (Amendment) Regulations 2008, Payment Services Regulations 2009 and Taxation (International and Other Provisions) Act 2010.⁶¹⁸ The Corporation Tax Act 2009 also adopted this definition but excluded from the small businesses category companies which in any time of an accounting period were:⁶¹⁹ an open-ended investment company, an authorised unit trust scheme, an insurance company, or a friendly society because their dealings may involve high values.⁶²⁰ On the other hand the Companies Act

⁶¹³ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 2.32.

⁶¹⁴ The adoption of the mechanical test 'of number of employees and/or having a certain level of turnover' to specify the application of a special regime allows the 'relative bargaining positions of the parties become what it should be, a factor in assessing reasonableness.' See Wilson and Bone (n 173) 38.

⁶¹⁵ Under Title I of the Annex of the Recommendation: *medium-sized* enterprises employ fewer than 250 persons and have an annual turnover which does not exceed €50 million (approximately £42.5 million) or an annual balance-sheet total up to €43 million (approximately £36.5 million). A *small* enterprise employs up to 50 persons and has a turnover and/or annual balance sheet total up to €10 million (approximately £8.5 million). A *micro* enterprise employs fewer than 10 persons and has a turnover and/or annual balance sheet total that does not exceed €2 million (approximately £1.7 million). According to a European Commission's report of October 2009 the current headcount ceiling was still appropriate. Similarly the financial ceiling was kept the same because the inflation has been considered moderate. See Commission, 'Commission staff working document on the implementation of Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises' SEC (2009) 1350 final para 3.2.

⁶¹⁶ *Ibid.* para 4.

⁶¹⁷ See <<http://www.euractiv.com/innovation-enterprise/sme-commission-ask-news-506418>> accessed 10 February 2012.

⁶¹⁸ Section 9(2) of the Community Investment Tax Relief (Accreditation of Community Development Finance Institutions) (Amendment) Regulations 2008 (SI 2008/383); section 2(1) of the Payment Services Regulations 2009 (SI 2009/209); Taxation (International and Other Provisions) Act 2010 in section 172(1) provides exemptions from the basic rule of taxation for dormant companies and SMEs.

⁶¹⁹ Accounting period: a period of time at the end of which the firm's accounts are made up. See Collin (n 607) 4.

⁶²⁰ Corporation Tax Act 2009 (2009 c4) 931S (1).

2006 adopts the same number of the employees' criterion of the Recommendation but applies different criteria for turnover and balance sheet totals.⁶²¹

The Mercosul also adopts the *number of employees* and *turnover* criteria similar to Recommendation 2003/361/EC; however the protection offered by the European Commission covers businesses with a turnover almost four times higher than its South American equivalent.⁶²² One could suggest that SMEs in EU countries are more sophisticated or profitable. However this difference may result from the fact that the EU criterion includes businesses with a larger number of employees which presumably have transactions involving larger amounts of money and higher turnovers.

By comparison, the Brazilian National Statute of Micro and Small Businesses (Declaratory Statute 123/2006)⁶²³ adopted only the *gross revenue* as the criterion to classify a company as small or micro because this statute is mainly concerned with estimating and collecting taxes and contributions; consequently the number of employees is not essential for its purpose.⁶²⁴

⁶²¹ According to section 382 of this Act a company is classified as small if it has a turnover of not more than £6.5 million, a balance sheet total of not more than £3.26 million and not more than 50 employees. On the other hand, a company is classified as medium-sized if it has a turnover of not more than £25.9 million, a balance sheet total of not more than £12.9 million and not more than 250 employees. Nonetheless, those definitions are limited to the purpose of accounting and reporting requirements (section 465).

⁶²² In the context of the Mercosul, Resolution 59/98 applies a quantitative criterion that takes into account the number of employees and the turnover. In the sector of trade and services, a micro business has up to 5 employees and a turnover not higher than US\$200,000 (approximately £125,000) whereas a small business has up to 30 employees and a turnover under US\$1.5 million (approximately £945,000). In the sector of industry, a micro business has up to 10 employees and a turnover not higher than US\$400,000 (approximately £250,000) and a small business has up to 40 employees and a turnover under US\$3.5 million (approximately £2.2 million). There is also a qualitative criterion according to which small businesses should not be controlled by another company or belong to a business group which has a turnover that exceed the established values.

⁶²³ The Declaratory Statute 123/2006 was enacted in accordance with the constitutional amendment 42/2003, which introduced changes into the National Tax System including the provision that a Declaratory Statute should establish general rules for tax legislation, particularly regarding to the definition of a differentiated and favourable tax treatment to be given to micro and small businesses, including special or simplified tax regimes (article 146, III, 'd' of the Federal Constitution).

⁶²⁴ According to article 3 of the *National Statute of Micro and Small Businesses* small and micro businesses are the companies, societies and business proprietors properly registered in the Registry of Companies or the Civil Registry of Legal Entities, provided that I – in the case of micro businesses: the business proprietor, the legal person or its equivalent receives in each calendar year gross revenue of less than R\$240,000 (approximately £92,500); II – in the case of small businesses: the business proprietor, the legal person or its equivalent receives in each calendar year gross revenue higher than R\$240,000 and equal or less than R\$2.4 million (approximately £925,000).

4.3. Legislative control on unfairness in small businesses contracts in England and the EU

European contract law has been developed mainly in the area of B2C contracts and has left B2B transactions to be regulated by Member States.⁶²⁵ One could say that the EU recognises that consumers are particularly vulnerable in cross-border transactions within the common market thus it provides special protection at European level to the latter; whereas interferences in businesses transactions should be avoided in deference to freedom of contract. When such interferences are deemed strictly necessary they should be determined by the legislation of each Member State which can identify specific issues that have to be addressed.

In England the Unfair Contract Terms Act 1977 prescribes provisions that purport to protect businesses and non-businesses from exclusion and limitation clauses as seen in chapter 2. Its section 3 affords protection in the context of breaches of strict contractual obligations to consumers and those 'dealing on the other's written standard terms of business' in B2B contracts. This provision may be particularly significant to small businesses contracts as it may protect SMEs from unreasonable terms that are unlikely to be negotiated or modified due to the disparity of bargaining strength between the parties.

Notwithstanding the aforementioned provision the classical model still prevails in the context of business contracts in England. Such model is consistent with the *static market-individualist* ideology which is underpinned by an individualist ethic. According to this ideology each party can pursue his self-interest and courts should not interfere in contracts freely agreed.⁶²⁶

However this ideology may not prevent distortions created by market asymmetries such as the imposition of unfair terms in contracts where parties do not share equal bargaining power. Brownsword suggested that the so-called *dynamic market-individualist* ideology may adjust better to the market reality as it takes into account commercial expectations and prescribes limits to the pursuit of self-interest.⁶²⁷

⁶²⁵ Roppo (n 597) 306.

⁶²⁶ Brownsword and Adams, 'The Ideologies of Contract' (n 127) 208. See also *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827 (HL) which adopted a non-interventionist approach in a business contract. A similar position was adopted in *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361, [2009] 1 All ER (Comm) 586 because parties had an equivalent bargaining strength.

⁶²⁷ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 142-143.

Additionally Roppo contended that EU legislation should regulate B2B contracts where a dominant party takes advantage of a weak business, in particular of a small business. Therefore special protections should be no longer limited to consumer contracts and should also be applied to business agreements in those circumstances.⁶²⁸

According to the European Commission in its 'Green Paper on the Review of the Consumer Acquis' small businesses and individual entrepreneurs may be comparable to consumers 'when they buy certain goods or services', 'which raises the question whether they should benefit to a certain extent from the same protection provided to consumers.'⁶²⁹

In 2008 the same Commission enacted *A Small Business Act for Europe (SBA)*⁶³⁰ that prescribed principles and proposed policies and legislative actions aiming at the full development of SMEs (e.g., facilitate access to funding) and creation of jobs. At the heart of the SBA was the *think small first* principle which 'requires that legislation takes SMEs' interests into account at the very early stages of policy making in order to make legislation more SME friendly'.⁶³¹ This principle can be found in the domestic legislation of England such as the *Companies Act 2006* which took into account not only the interests of larger companies but also of SMEs. This Act prescribes a 'small companies regime'⁶³² which is a positive step for SMEs as the previous legislation 'was incomprehensible to many small businesses, bureaucratic and unsympathetic to the needs of small companies and clearly not user-friendly'.⁶³³

A review of SBA in 2011 expressly recognised that unfair commercial practices and unfair contractual clauses are often imposed on SMEs;⁶³⁴ for this reason the European Commission intends to carry out an analysis of such practices and clauses in B2B

⁶²⁸ Roppo (n 597) 311.

⁶²⁹ Commission, 'Green Paper on the Review of the Consumer Acquis' COM (2006) 744 final para 15.

⁶³⁰ Commission, 'Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - "Think Small First" - A "Small Business Act" for Europe' COM (2008) 394 final.

⁶³¹ See <<http://ec.europa.eu/enterprise/policies/sme/small-business-act/think-small-first/>> accessed 10 December 2011.

⁶³² The Act defines in its sections 381 to 384 the 'companies subject to the small companies' regime'. This regime includes: 'group accounts' if a small business is a 'parent company' ('a company which owns more than 50% of the shares of another company') (s. 398); distinct provisions for filing obligations (s. 444) and exemption from audit of accounts (s. 477). See Collin (n 607) 290.

⁶³³ According to Sheikh the CA 1985 'was opaque and inaccessible for small business users'. See Saleem Sheikh, *A Guide to the Companies Act 2006* (Routledge-Cavendish 2008) 47 and 126.

⁶³⁴ Commission, 'Review of the "Small Business Act" for Europe' COM (2011) 78 final.

contracts within the EU and recommend 'a legislative proposal if needed in order to protect businesses' against them.⁶³⁵ This proposition supports the idea that small businesses may need protections similar to consumers as the latter are already covered by the provisions of the *Unfair Commercial Practices Directive* (UCPD).⁶³⁶

Furthermore the *Principles of European Contract Law* (PECL) and the *Draft Common Frame of Reference* (DCFR) contain provisions which in spite of not referring to small businesses expressly may benefit them indirectly as they purport to protect the weaker party in asymmetric contracts.⁶³⁷

The PECL transposed rules from the Directive 93/13/EEC (that are limited to B2C contracts) to control any non-negotiated term, but they 'do not differentiate between possible legal entities'.⁶³⁸ Therefore, although there is no special treatment for small businesses, they may be favoured by provisions that used to be restricted to consumer contracts.

The DCFR in its turn deals with unfair terms more generally and does not confer privileged treatment on consumer contracts because 'other market players (especially small businesses) (...) suffer in the same way as consumers do an asymmetry of bargaining power in their relationships to stronger contract parties'.⁶³⁹ For this reason the DCFR regulates unfair terms in B2C contracts (article II - 9:404); C2C contracts (article II - 9:405) and also B2B contracts (article II - 9:406). Such provisions purport to protect parties who adhere to non-negotiated terms which significantly disadvantage them and that are contrary to good faith and fair dealing. Those controls are justified because in standard form contracts there is 'no free consent to the terms by one side'.⁶⁴⁰

⁶³⁵ Ibid. para 3.3.1.

⁶³⁶ European Parliament and Council Directive 2005/29/EC.

⁶³⁷ See Roppo (n 597) 331-336. Additionally the Directive 2011/7/EU on *Combating Late Payment in Commercial Transactions* made reference to SBA in its recital 6 which prescribes the facilitation of the SMEs' access to finance and the development of 'a legal and business environment supportive of timely payments in commercial transactions' because late payments aggravate the weak position of those businesses. This provision implicitly recognises an asymmetric position of SMEs in B2B contracts.

⁶³⁸ The PECL 'proceed on the basis of the equality of all potential legal entities and address natural persons as well as legal entities'. Hans W Micklitz, 'The Principles of European Contract Law and the Protection of the Weaker Party' (2004) 27(3) JCP 339, 341.

⁶³⁹ Roppo (n 597) 335-336.

⁶⁴⁰ Thomas Pfeiffer, 'Non-Negotiated Terms' in R Schulze (ed) *Common Frame of Reference and Existing EC Contract Law* (Sellier 2008) 179.

As the DCFR does not tackle small businesses contracts specifically, SMEs will share the same protection afforded to businesses in general (article II - 9:406). Such protection covers adhering businesses against terms which 'use grossly deviates from good commercial practice' and that is 'contrary to good faith and fair dealing'. Those broad expressions leave some leeway to courts to interpret them and also indicate the adoption of a cooperativist ethic which opposes any harmful behaviour of either party. Furthermore the expression '*good commercial practice*' may reflect the expectations of the commercial community of a certain trade which is consistent with the *dynamic* market-individualism ideology.⁶⁴¹

More recently the European Commission proposed an optional *Regulation on a Common European Sales Law* (CESL)⁶⁴² and one of its main purposes is clearly to benefit SMEs 'in particular, from entering cross border trade or expanding to new Member States' markets'.⁶⁴³ Generally SMEs cannot afford the costs of trading with foreign markets as it requires legal expertise of the law of contracts of different countries and translation of agreements. Consequently the aforementioned regulation may offer an alternative solution to those problems because SMEs can opt to use this regime in cross-border transactions. As this set of rules shall be identical in all 27 Member States, there is no need to adapt contracts to different national contract law.⁶⁴⁵

In addition small businesses contracting outside their jurisdiction may be protected by the provisions of this proposed regime which also tackles unfair terms in 'contracts between traders'. They reproduce the wording of the DCFR provisions as they consider unfair non-negotiated terms that are of 'such a nature that its use grossly deviates from *good commercial practice*, contrary to good faith and fair dealing' (art. 86).

⁶⁴¹ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 161.

⁶⁴² Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final. See further details in chapter 3.

⁶⁴³ The Common European Sales Law 'can be chosen in contracts between traders where at least one of them is an SME, drawing upon the Commission Recommendation 2003/361 concerning the definition of micro, small and medium-sized enterprises while taking into account future developments'. See Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final paras 2 and 7.

⁶⁴⁴ Poole observed that this 'regime is not intended to contracts between two large businesses'; however according to article 13(b) of the CESL 'a Member State may decide to make the Common European Sales Law available for contracts where all the parties are traders but none of them is an SME'. See Poole, *Textbook on Contract Law* (n 78) 15.

⁶⁴⁵ See <http://ec.europa.eu/justice/contract/files/common_sales_law/i11_1175_en.pdf> accessed 13 October 2011.

4.3.1. The Law Commission proposal

In 2001 The Law Commission was asked by the Department of Trade and Industry to propose a unified regime to regulate the law of unfair contract terms as well as to consider whether small businesses particularly require an extended protection.⁶⁴⁶ Following the analysis of the responses to its Consultation Paper,⁶⁴⁷ the Law Commission published a Report in 2005 which concluded that small businesses are more exposed to unfair terms than large businesses as a result of the inequality of bargaining power;⁶⁴⁸ thus just like consumers they also require a special regime.

The proposed regime extends consumer protections prescribed by the UTCCR 1999 to small businesses.⁶⁴⁹ It may benefit SMEs because currently they are mainly protected by the provisions of the Unfair Contract Terms Act 1977 and 'there is a clear potential for unfairness in terms other than those caught by UCTA'⁶⁵⁰ such as arbitration clauses, price variation clauses and termination clauses.⁶⁵¹ Those clauses are frequently included in contracts in which small businesses are customers for goods and services and under the Law Commission's proposal they shall be subjected to a 'fair and reasonable test'.⁶⁵²

Furthermore this regime allows small businesses to challenge all *non-negotiated* and *non-core terms*⁶⁵³ which should increase significantly the level of protection afforded to those businesses. SMEs are particularly susceptible to the imposition of detrimental terms in standard form contracts; especially when those terms are included in sporadic contracts that are outside their area of expertise because normally they do not have the resources to take legal advice.⁶⁵⁴ Such special protection is however limited to non-negotiated terms in deference to freedom of contract and certainty of contracts.

The need for *certainty* in B2B contracts is also consistent with the provision which prescribes that small businesses must bear the burden of proving that a non-negotiated

⁶⁴⁶ See <<http://www.justice.gov.uk/lawcommission/unfair-terms-in-contracts.htm>> accessed 05 April 2011.

⁶⁴⁷ Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002).

⁶⁴⁸ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 5.3 and 5.4.

⁶⁴⁹ See chapter 3.

⁶⁵⁰ Chen-Wishart (n 3) 497.

⁶⁵¹ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 2.31.

⁶⁵² *Ibid.* paras 5.12 and 5.26.

⁶⁵³ *Ibid.* para 2.35. Core terms are related to the definition of the main subject matter of the contract (goods or services) or to the adequacy of the price or remuneration. See reg. 6(2) of the UTCCR 1999.

⁶⁵⁴ Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) paras 5.28 and 5.29.

term is not fair and reasonable.⁶⁵⁵ Otherwise businesses would be able to 'challenge the fairness of a term when the real reason behind the challenge is to try and avoid contractual obligations' which would put at risk the market's efficiency.⁶⁵⁶

For the purpose of the proposed legislation, SMEs can make use of the special protection either against a large business (due to the inequality of bargaining power) or a small peer because 'small business contract' is defined as a contract between a small business and another business of any size.⁶⁵⁷ In contracts where both parties are considered 'small' in size, interventions may be required to prevent abuses when businesses have different levels of resources (e.g., access to legal advice).⁶⁵⁸

There are however exceptions to the application of this regime. The first one is contracts involving values higher than £500,000 because according to the Law Commission they indicate that the business is probably sufficiently sophisticated or is likely to take legal advice.⁶⁵⁹ The same reasoning is applied to companies that are associated with or under the control of a larger business because in those cases the small businesses can recourse to the controller business for assistance and support.⁶⁶⁰ The second exception is the 'financial services contracts' because they are subject to regulations by the Financial Services Authority (FSA) and the application of another regime could result in an 'over-regulation of the market'.⁶⁶¹ It is clear that the Law Commission aims to limit the application of the special regime to situations where it is absolutely required because interventions should be avoided especially in the context of B2B contracts. Consequently those businesses are also 'not covered by the pre-emptive challenges', though they 'will need to possess sufficient resources to pursue court action challenging terms as unfair'.⁶⁶²

⁶⁵⁵ See clause 17(2) of the *Unfair Contract Terms Bill* in contrast with clause 16(1) which prescribes that in a consumer contract the burden of proof that a term is fair and reasonable rests on the business. The Law Commission pointed out that despite small businesses share similarities with consumers, they are more experienced and possess more resources than the latter, and consequently they must bear the burden of proving that a term is not fair and reasonable. Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 5.85.

⁶⁵⁶ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 4.10.

⁶⁵⁷ Clause 29 of the *Unfair Contract Terms Bill*.

⁶⁵⁸ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 5.32.

⁶⁵⁹ See clause 29 of the Bill that excludes from the small business regime contracts or series contracts that contain transactions that exceed £500,000. See also Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 5.55 to 5.59.

⁶⁶⁰ Clauses 27 and 28 of the *Unfair Contract Terms Bill*.

⁶⁶¹ See Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 5.64 to 5.67. See Financial Services and Markets Act 2000.

⁶⁶² Poole, *Textbook on Contract Law* (n 78) 276.

On 25 July 2012 the Law Commission published a review and update of the aforementioned 2005 Report on 'Unfair Terms in Contracts' in the issues paper *'Unfair Terms in Consumer Contracts: A New Approach?'*. However the latter did not contain revisions to the small businesses regime originally proposed in the Report; therefore presumably this regime will not be subject to new considerations.

On the other hand the 'reform of consumer rights' proposed by the Department for Business, Innovation and Skills (BIS) through the *Consumer Bill of Rights* prescribes some protections to SMEs. As part of this reform it has launched a consultation on 'private actions in competition law' which purports to 'increase growth, by empowering small businesses to tackle anti-competitive behaviour that is stifling their business' and 'promote fairness, by enabling consumers and businesses who have suffered loss due to anti-competitive behaviour to obtain redress'.⁶⁶³ Those proposed protections however have a different scope from the protection afforded to SMEs against unfair terms.

4.4. Legislative control on unfairness in small businesses contracts in Brazil and the Mercosul

Globalisation expanded the consumer market beyond countries' borders and triggered the demand for a greater variety of products. On the one hand this phenomenon favoured the development of small businesses that are more adaptable and capable of satisfying new niche markets.⁶⁶⁴ On the other hand those businesses may need extra support to enhance their competitiveness in a globalised market; otherwise they may not withstand the difficulties of competing with large-sized companies.⁶⁶⁵

For this reason, the Mercosul proposed policies to support micro, small and medium enterprises via its Resolution 90/93 and subsequent Resolution 59/98.⁶⁶⁶ According to

⁶⁶³ Department for Business, Innovation and Skills (BIS), *Private Actions in Competition Law: A Consultation on Options for Reform* (April 2012) 4. The closing date for responses was on 24 July 2012.

⁶⁶⁴ Fernanda Kellner Oliveira Palermo, 'As Micro e Pequenas Empresas como Propulsoras do Desenvolvimento Econômico e Social: Contribuição para o Incremento das Atividades Econômicas no Âmbito do Mercosul' *Jus Navigandi* <<http://jus.uol.com.br/revista/texto/2735>> accessed 06 April 2011 [5.1]. According to Schwamm such adaptability 'perhaps (...) is simply because they are on a more human scale, and closer to the consumer's changing needs, expectations and tastes'. See Henri Schwamm, 'Small Firms in Europe' (1972) 6 *JWTL* 648, 660.

⁶⁶⁵ Paulo Roberto Colombo Arnoldi and Tais Cristina Camargo Michelin, 'Novos Enfoques da Função Social da Empresa numa Economia Globalizada' (2002) São Paulo, jul./set., v.11., *Revista de Direito Privado* 244, 248.

⁶⁶⁶ Resolutions 90/93 and 59/98 prescribe stages one and two respectively of 'policies to support micro, small and medium business'. *Resolutions* 'are adopted by the Common Market Group and are binding on all member states'. They purport to implement the decisions of the Common Market Council which is the supreme body of the Mercosul that conducts policies towards the implementation of the Treaty of Asunción. They 'cover an

those Resolutions the Member States of the Southern Common Market should identify deficiencies that may affect SMEs and create strategies to strengthen those businesses (e.g., enhance competitiveness, financial support and tax simplification). They demonstrate the concern of this regional trade agreement over the protection of SMEs, but they do not make express reference to any protection against contractual imbalances or unfairness. As a result Brazil proposed another Resolution⁶⁶⁷ which purports to tackle abusive clauses and shall be applied at Mercosul level. Although this Resolution is circumscribed to the context of B2C contracts, Brazilian courts have extended consumer protections to SMEs, thus the latter may benefit from its provisions.

The protection of small businesses is not only important to the Mercosul as a whole, but it is also fundamental to the economy of its Member States. For instance, in Brazil SMEs represent approximately 99% of businesses and generate over 14.7 millions of jobs.⁶⁶⁸ Those businesses are so invaluable to this country that their protection acquired constitutional status through article 170, IX of its Federal Constitution which prescribes that one of the principles of the economic activity is the '*preferential treatment* for small businesses organised under Brazilian law which have their head-office and management in Brazil'. Such special regime reflects the recognition of their weaker position in relation to other businesses. It is in line with the constitutional principle of equality which stipulates that equal parties should be treated equally but 'unequal parties should be given unequal treatment in the extent of their inequality'.⁶⁶⁹

Additionally this 'preferential treatment' prescribed by the Federal Constitution to SMEs supports article 6 of Act 10259/2001 according to which micro and small enterprises are the only type of businesses that can make claims in *federal small claims courts*.⁶⁷⁰ This provision makes evident that those businesses require more protection than others and equates them to natural persons. It recognises that they should be entitled to a simplified proceeding to deal with small claims because just like individuals their resources are generally limited or they are unable to seek legal advice. For this reason they are allowed

array of subject matter related to freedom of movement within the MERCOSUR area, such as commercial aspects and documents required for MERCOSUR citizens, budgetary aspects and relations with third states'. See Giupponi (n 572) 712.

⁶⁶⁷ Mercosul/CT-7/DT4-02/Reserved.

⁶⁶⁸ SEBRAE, *Anuário do Trabalho na Micro e Pequena Empresa: 2010-2011* (2011) 21-22.

⁶⁶⁹ Article 5 of the Brazilian Federal Constitution. See also Moraes (n 134) 64.

⁶⁷⁰ Federal small claims courts are competent to judge cases involving values up to 60 minimum wages (approximately £12,385) or minor offences which have as defendant the Union, the federal governmental agencies, foundations or public companies.

to designate any representative for the cause other than a lawyer⁶⁷¹ and the above proceeding enable SMEs to seek relief from harmful terms in a more straightforward manner.

This differentiated treatment given to SMEs was the basis for the creation in 2011 of an Executive Department in Brazil exclusively dedicated to micro and small businesses matters which will have the status of a government cabinet.⁶⁷² According to Bill 865/11 this body will be responsible for the creation of policies and directives which aim the strengthening, expansion and formalisation of SMEs. Although this department will not be endowed with legislative powers, it will be able to propose new law for consideration by the competent body. While it is not possible to predict the future actions of this Department, its creation will represent an important step towards the promotion and protection of SMEs in Brazil.

Nonetheless currently the specialised pieces of legislation concerning small businesses in Brazil (e.g., National Statute of Micro and Small Businesses) are mainly related to taxation, simplification of administrative obligations, access to credit, labour relations and social security.⁶⁷³ In the context of contract law MSEs are only protected by provisions applied to businesses in general, as seen in chapter 2. For instance, articles 423 and 424 of the Civil Code may be used to protect weak businesses from unfair terms imposed by large businesses in contracts of adhesion.⁶⁷⁴

However the general control over unfairness in B2B contracts may not adequately protect small businesses because they are often more vulnerable than other businesses. Most of them end their activities before completing two years of existence.⁶⁷⁵ The main reasons

⁶⁷¹ See article 10 (Act 10259/2001).

⁶⁷² The protection will be in line with the preferential treatment prescribed by article 170, IX of the Federal Constitution.

⁶⁷³ See article 179 of the Federal Constitution and the *National Statute of Micro and Small Businesses* (Declaratory Statute 123/2006). Additionally Act 9317/1996 establishes a simplified system of taxation system for micro and small businesses through the 'Integrated System for Payment of Taxes and Contributions of Micro and Small Businesses' ('SIMPLES'). Furthermore, Decree 6204/2007 prescribes a favoured treatment, differentiated and simplified for micro and small businesses in public contracting of goods, works and services within the federal public administration and Decree 6038/2007 institutes the Steering Committee of Taxation of Micro and Small Businesses.

⁶⁷⁴ Art. 423: 'when there are ambiguous or contradictory clauses in a contract of adhesion, the interpretation most favourable to the adhering party shall be adopted'. Art. 424: 'in contracts of adhesion, clauses that stipulate that the adhering party has waived in advance rights arising out of the nature are void'. See Rose (n 251) 88.

⁶⁷⁵ 'Small firms are extremists (...) they grow or decline the most rapidly; enter and leave in great numbers'. Adelman (n 604) 19. Similarly Schwamm observed that 'many small firms collapse and disappear from the

for their failure include the lack of expertise and experience of their proprietors and difficult access to professional advice,⁶⁷⁶ which leave them more exposed to abusive clauses and stipulations. In other words, the success or failure of a small business may result from a number of factors such as undercapitalisation or lack of planning. Nevertheless the constant exposure to unfair terms in their dealings is one of the factors which have a negative impact on them. This has prompted Brazilian courts to intervene in small businesses contracts as will be observed below.

4.4.1. Businesses as consumers

The general provisions of the Civil Code and the supplementary commercial legislation aim to regulate the relationships of businesses which share equal bargaining power; consequently they are often inadequate to regulate contracts which involve an unbalanced relationship. Ulhoa Coelho stressed the need for a distinct regime to deal with contracts between unequal parties. In the absence of such special rules, he suggested that small businesses are better protected under the provisions of the Consumer Protection Code.⁶⁷⁷ However while in line with the Consumer Protection Code it is incontrovertible that small businesses can be defined as a seller or supplier,⁶⁷⁸ there is some debate in relation to its treatment as a consumer.⁶⁷⁹

In Brazil there are two main approaches concerning the definition of *consumer* for the purpose of the application of the special protection. The first approach called *finalist* or *subjective* takes into account the 'non-professional' quality of the consumer as opposed to a professional supplier.⁶⁸⁰ It regards as a consumer only the final recipient of goods or services who do not profit from this activity. Consequently this restrictive approach excludes from the consumer definition a company which acquires a service or product for business purposes.⁶⁸¹

scene (...) but at the same time many new ones spring up and expand (...). Thus there is a constant process of renewal'. See Schwamm (n 664) 651.

⁶⁷⁶ Palermo (n 664) [3.2] and [3.3.].

⁶⁷⁷ Ulhoa Coelho (n 31) 167-168.

⁶⁷⁸ Article 3 of the Consumer Protection Code defines *supplier* as 'any natural or legal person public or private, domestic or foreign, as well as depersonalised entities, which develop activities of production, assembly, creation, construction, processing, importation, exportation, distribution or trading of products or services.' The definition of *supplier* contained in article 3 does not discriminate between businesses of different types and sizes, thus it may range from a family-run business to a multinational.

⁶⁷⁹ Consumer is defined by article 2 of the Consumer Protection Code as 'every natural or legal person who acquires or uses products or services as a final recipient'.

⁶⁸⁰ Ulhoa Coelho (n 31) 169.

⁶⁸¹ REsp 761557/RS (03/12/2009).

According to the second approach, known as *maximalist* or *objective*, the protection afforded to consumers may be extended to any person who acquires goods or services as their final recipient and do not reintroduce them in the market chain.⁶⁸² Therefore a business can still be treated as a consumer even if it is exercising a professional activity;⁶⁸³ hence a company will be regarded as a consumer if it purchases some paintings for the embellishment of its premises.

The main problem of the application of this approach is concerning situations which do not involve a physical exchange of goods or services. For instance, if a manufacturer uses electrical energy to run his machinery he may be materially considered a final recipient; however the energy employed will be indirectly incorporated into the goods that will be made available to the consumer market.⁶⁸⁴ As a consequence the company may not be protected as a consumer in this case.⁶⁸⁵

The position of the Superior Tribunal of Justice has moved from a finalist approach towards a maximalist approach.⁶⁸⁶ According to this court the consumer protection should not only be applied to the 'non-professional' consumer but also to *vulnerable businesses* (in the technical, legal or economic sense) who are the final recipients of goods or services.⁶⁸⁷ For instance, a person who acquires a small piece of machinery from a large supplier to be employed in a family-run business should be protected as a consumer due to her evident vulnerability.⁶⁸⁸ Consequently the consumer legislation is exceptionally

⁶⁸² See Castello Miguel (n 256) 76. For instance goods cannot be reintroduced even if they were transformed into a different good through an industrial process.

⁶⁸³ Article 2 of the Consumer Protection Code did not take into account the personal aspects of the recipient (whether he is acquiring the goods and services for personal use or business purposes). See Ibid. 78.

⁶⁸⁴ In this context Ulhoa Coelho proposed that if the goods or services were indispensable for the production process then the business will not be treated as a consumer. If they are dispensable the company may be protected under the Consumer Protection Code. See Ulhoa Coelho (n 31) 169-173.

⁶⁸⁵ According to Vidigal businesses should never be considered consumers because they will inevitably use the acquired goods or services in products which will be reintroduced into the market chain. See Geraldo Camargo Vidigal, 'A Lei de Defesa do Consumidor: sua Abrangência' in GC Vidigal (ed) *Lei de Defesa do Consumidor* (IBCB 1991) 16.

⁶⁸⁶ CC 92519/SP (04/03/2009).

⁶⁸⁷ The *technical* vulnerability is related to the party's ignorance about the actual object of the contract. The *legal* vulnerability is concerned to the lack of knowledge of the relevant law and its consequences. Finally the *economic* vulnerability is a result from the different bargaining power of the parties. See Ulhoa Coelho (n 31) 176.

⁶⁸⁸ See REsp 1010834/GO (13/10/2010). Similarly it was exceptionally admitted the application of the provisions of the Consumer Protection Code to a small farmer who acquired fertilizer for farming due to his technical, legal and economic vulnerability. See AgRg no REsp 1200156/RS (14/10/2010). A taxi driver who bought a defective car for commercial purpose was also protect under the Consumer Protection Code provisions because he was considered vulnerable in relation to a car manufacturer. See REsp 575469/RJ (06/12/2004).

applicable to disputes involving vulnerable businesses which are often micro and small enterprises.⁶⁸⁹

There is therefore an inclination for courts to interfere in relationships where a large business takes advantage of the other party. The principle of good faith is also employed as ground for intervention to avoid the exploitation of weak companies. The prevention of abuses is particularly relevant in cases involving 'asymmetric interdependences' between businesses where the dominant company aims to control the outcomes of the relationship.⁶⁹⁰

For instance, in the famous 'case of tomatoes' a large company (Cica) used to distribute tomatoes seeds to small producers and purchase their crops for subsequent industrialisation. However, without previous notice, Cica decided to stop purchasing the farmers' crops in spite of the legitimate expectation created by its prior behaviour, which caused the loss of the production. The Supreme Court of the Rio Grande do Sul State recognised that this large company was in breach of trust and acting against good faith and concluded that the farmers were entitled to claim damages.⁶⁹¹

4.5. Analysing the differences and similarities of the legislative controls on unfairness in small businesses contracts in England and Brazil

Presently neither England nor Brazil has a legislative act that specifically purports to protect SMEs and micro enterprises against unfair terms and exemption clauses; consequently they are subject to the same provisions applicable to businesses in general.

In England however the Law Commission has already proposed a special regime to control unfairness in small businesses contracts. By comparison in Brazil there is no indication of any future legislation with such a purpose; possibly because article 179 of the Federal Constitution prescribes that the special treatment that should be given to SMEs is concerned with the simplification of their administration, tax, social security and

⁶⁸⁹ More recently the Superior Court of Justice contended that a *factoring company* could not be protected under the provisions of the Consumer Protection Code because it was neither a final recipient nor a vulnerable party. See REsp 938979/DF (29/06/2012).

⁶⁹⁰ S Mouzas and D Ford, 'Contracts in Asymmetric Relationships' (2007) 1(3) *Impact of Science on Society* 42, 47.

⁶⁹¹ See TJ/RS, Embargos Infringentes 591083357, Rel. Des. Adalberto Libório Barros (01/11/1991).

credit obligations. Therefore subsequent pieces of legislation have been shaped by this provision and are generally limited to those matters.⁶⁹²

In the absence of legislative controls on unfair terms in small businesses contracts courts of both jurisdictions have adopted a more interventionist approach in contracts where one business abuses its dominant position by including harsh terms that put the other business at disadvantage. For instance, in *St Albans City & District Council v International Computers Ltd*⁶⁹³ an unreasonable limitation clause was included in a contract made between two 'businesses' (a local authority and a computer company). Although they could in principle freely negotiate terms, the court adopted 'a protectionist attitude towards the local authority which (...) is in a distinct position and is arguably in greater need of protection than a large public limited company'.⁶⁹⁴ In Brazil courts have employed provisions of the Consumer Protection Code to protect vulnerable SMEs by analogy. Although this solution may not be ideal because it depends on the discretion of the judges, in practice it has offered a more adequate protection for small businesses than the general provisions of the Civil Code.

4.5.1. Approaches adopted by courts

As seen previously, in Brazil there is a discussion in the legal literature on whether a business can be regarded as a consumer under the provisions of the Consumer Protection Code. The *objective* or *maximalist* approach defines a consumer as the party who is at the end of the market chain. On the other hand the *subjective* or *finalist* approach examines whether the party will use the goods and services as part of his professional activity.⁶⁹⁵

England adopts an approach similar to the '*finalist*' one. According to section 12(1) of the Unfair Contract Terms Act 1977 a party 'deals as consumer' if he does not make the

⁶⁹² For instance Bills and other propositions of the Brazilian National Congress have been limited to the scope of this provision. E.g., Complementary Bill PLP 12/2011 which authorises the payment of debts of social security contributions in instalments by MSEs; Bill PL 7604/2006 which establishes the suspension of tax execution during the bankruptcy of MSEs; Bill PL 4449/2004 which establishes rules for the renegotiation of debts of MSEs.

⁶⁹³ [1996] 4 All ER 481 (CA), [1995] FSR 686. The definition of 'business' prescribed by s. 14 of UCTA include 'local or public authority'. See also *Motours Ltd v Euroball (West Kent) Ltd* [2003] EWHC 614 (QB), [2003] All ER (D) 165.

⁶⁹⁴ Poole, *Casebook on Contract Law* (n 150) 288. The computer company was in fact in a strong bargaining position because it was among few eligible suppliers; hence the Court of Appeal treated the local authority as a 'quasi-consumer'. Similarly the Brazilian Superior Court of Justice decided in favour of a business considered vulnerable in a B2B contract. See REsp 1010834/GO (13/10/2010).

⁶⁹⁵ Ulhoa Coelho (n 31) 169.

contract 'in the course of a business'.⁶⁹⁶ Consequently the determination of whether a company acquired goods and services for its own use rather than for business purposes is of great significance to establish if a SME will be treated as a consumer and protected accordingly.⁶⁹⁷⁶⁹⁸

The position of the European Court of Justice may be also comparable to the 'finalist' approach, as the special protection is limited to consumers 'in the purest and fullest sense'⁶⁹⁹ and shall not be extended to protect businesses in the course of their professional activities.

For instance, in *Johann Gruber v Bay Wa AG*⁷⁰⁰ a farmer purchased tiles to reroof his farmhouse which was used partly as a private dwelling by the claimant and his family and partly for farming purposes. The tiles were defective and the farmer claimed damages against the supplier of building materials. The court decided that a 'person who concludes a contract relating to goods intended for purposes which are in part within and in part outside his trade or profession' may not rely on the special rules of the Brussels Convention which benefit consumers 'unless the trade or professional purpose is so limited as to be negligible in the overall context of the supply'.⁷⁰¹ This position was incorporated into the *Directive on Consumer Rights (2011/83/EU)*⁷⁰² which prescribes that a person shall be considered a consumer 'in the case of dual purpose contracts, where the contract is concluded for purposes partly within and partly outside the person's trade and the trade purpose is so limited as not to be predominant in the overall context of the contract'.⁷⁰³

Therefore the European and English approach can be considered more restrictive than the prevailing approach in Brazil as it does not allow the extension of the consumer protection

⁶⁹⁶ Furthermore when the consumer is not an individual (e.g., a business) the goods under or in pursuance of the contract should be of a type ordinarily supplied for private use or consumption. See s. 12(1)(c) of UCTA.

⁶⁹⁷ The meaning of 'in the course of a business' has been subject of discussion in chapter 2. See *R&B Customs Brokers Co Ltd v United Dominions Trust Ltd* [1988] 1 WLR 321 (CA) and *Stevenson v Rogers* [1999] 2 WLR 1064.

⁶⁹⁸ There are cases where it is difficult to distinguish if a weak company is acting as a business or a consumer such as in *quasi consumer* cases (e.g., *St Albans City & District Council v International Computers Ltd* [1996] 4 All ER 481 (CA), [1995] FSR 686).

⁶⁹⁹ Roppo (n 597) 306.

⁷⁰⁰ Case C-464/01 *Johann Gruber v Bay Wa AG* [2005] ECR I-439 .

⁷⁰¹ *Ibid.* paras 204-225. The position of *Gruber* was also applied in English cases such as *Turner & Co (GB) Ltd v Abi* [2010] EWHC 2078 (QB) according to which the agreement in question was not a consumer contract because it was made for the purposes of the party's business, not for his family or personal use. As a consequence unfair terms legislation was not applicable.

⁷⁰² This Directive was adopted in October 2011 by Member States in the EU's Council of Ministers.

⁷⁰³ Recital 17 of the *Directive on Consumer Rights (2011/83/EU)*.

to SMEs which make a contract with business purposes. Moreover some EU Directives (e.g., article 2 of Directive 93/13/EEC)⁷⁰⁴ as well as their respective Regulations (e.g., UTCCR 1999) and case law such as *The Republic v Patrice di Pinto*⁷⁰⁵ provide that only 'natural persons' can be regarded as consumers.⁷⁰⁶ This approach, by comparison with the finalist or maximalist approach, excludes businesses from the definition of consumer altogether.

In view of the above it is possible to conclude that the approach which has been applied by the Brazilian courts is more consistent with the general protection of the weak party in asymmetric contracts as it has extended the same protection to consumers and businesses based on their vulnerability.

4.6. Conclusion

The dichotomies of the modern contract law include the relationship between 'consumers versus merchants'.⁷⁰⁷ However 'small businesses do not fall cleanly into any of these categories' because although they are normally treated as merchants they also resemble consumers in many ways.⁷⁰⁸ Garvin contended that those businesses 'get the worse of each dichotomy': in contracts with consumers they have to provide protections to the latter based on asymmetries which may not exist, whereas in contracts with larger businesses they are treated as equals even if this is not the case.⁷⁰⁹

Additionally in the market chain they find themselves in the middle of large suppliers and consumers and they have to respond to demands from both sides. For instance, although they have to replace defective products sold to consumers, exemption clauses may prevent them from asking manufacturers for compensation.⁷¹⁰

⁷⁰⁴ Various directives limit the notion of consumer to natural persons as it can be observed from: Directive 85/577/EEC in Article 2; Directive 97/7/EC in Article 2(2); Directive 2002/65/EC in Article 2(d); Directive 87/102/EEC in Article 1(2)(a); Directive 1999/44/EC in Article 1(2)(a); Directive 98/6/EC in Article 1(e) and Article 2(1) of the Directive 2011/83/EU.

⁷⁰⁵ Case C-361/89 *The Republic v Patrice di Pinto* [1991] ECR I-1189 .

⁷⁰⁶ The Brazilian Consumer Protection Code expressly prescribes that consumers are either natural or legal persons (article 2); whereas the Unfair Terms in Consumer Contracts Regulations 1999 consider only natural persons as consumers (reg. 3(1)). Similarly the European Court of Justice also stressed in Case C-453/99 *Cape SNC v Idealservice Srl* [2001] ECR I-9049 para 1239 that in line with article 2 of the Directive 93/13/EEC 'consumers' are only 'natural persons who concluded a contract with a seller or supplier', therefore the protection against unfair terms cannot be extended to 'legal persons'.

⁷⁰⁷ Garvin (n 603) 296.

⁷⁰⁸ Those similarities include 'abilities to deal with risk' and 'fend for themselves in the market'. Ibid. 296-297.

⁷⁰⁹ Ibid. 297.

⁷¹⁰ Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) para 5.7.

A possible solution to this problem would be the implementation of a special regime to regulate small business contracts similar to the one afforded to consumer contracts as proposed by the Law Commission. This special protection may be justified due the fact that SMEs also lack resources and bargaining strength in contracts.

However special protections given to consumers and small businesses may result in the *fragmentation* of the contract law system which has been structured according to a 'binary articulation': a general part that is applied to any contract and a special part that deals with particular types of contract.⁷¹¹ For instance in Brazil although the Civil Code regulates 'contract in general' and 'various types of contracts',⁷¹² the Consumer Protection Code prescribes a differentiated regime for B2C contracts. The coexistence of these two Codes creates conflicts of law⁷¹³ that may be aggravated by the introduction of a small business regime in the area of contract law.

For this reason a more general regulation of *asymmetric relations* may prevent such fragmentation as well as unnecessary complexity for the interpreter. This control may be applicable to all contracts involving a dominant business and a weaker party (that may be a consumer or a business);⁷¹⁴ hence the avoidance of various regimes to deal with different types of vulnerable parties may afford more coherence to the system.

Hondius agreed that the new paradigm should be the '*protection of the weak party*' which can be extended to 'non-consumers, such as small businesspersons'.⁷¹⁵⁷¹⁶ SMEs would therefore be protected in an asymmetric B2B contract where 'the stronger party is likely to be able to dominate and influence the conclusion of contracts'.⁷¹⁷

⁷¹¹ Roppo (n 597) 344.

⁷¹² 'Contract in general' (articles 421 to 480) and 'various types of contracts' (articles 481 to 954).

⁷¹³ See chapter 5 on unresolved issues concerning the controls on unfairness in contracts.

⁷¹⁴ Roppo (n 597) 346.

⁷¹⁵ See Hondius (n 121) 246-250.

⁷¹⁶ Roppo suggested that regulations should protect '*customers*' instead '*consumers*' whilst dealing with a business on the grounds that 'customer' may include consumer or other business. The author referred to this contract as S2C (*supplier to customer*) and identified a number of Directives that deal with this type of contract. For instance according to Directive 2007/64/EC on payment services, consumers and enterprises do not share the same position and do not need the same level of protection; however micro-enterprises should be treated in the same way as consumers (recital 20). Additionally Regulation 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) [2008] OJ L 177/6 that replaced the Rome Convention of 1980 prescribes special protection to the weaker party (recital 23) alongside the protection of consumers (e.g., recital 24) where there are asymmetric market relationships. See Roppo (n 597) 315-316.

⁷¹⁷ Mouzas and Ford (n 690) 43.

According to Waddams the above paradigm is not wholly unfamiliar to English law. Waddams provided a number of examples in which courts in England set aside contracts based on 'unfairness and inequality of exchange' in order to protect the weaker party.⁷¹⁸ Those examples include cases of undue influence, unconscionable transactions and unjust enrichment.⁷¹⁹ By comparison Brazilian courts have extended the application of consumer protection to cases in which the weakness or vulnerability of a business is demonstrated (e.g., SMEs).⁷²⁰

Independently of the approach adopted arguably small businesses need a protection more suitable to their peculiarities. Although one could say that SMEs are not as vulnerable as consumers, those businesses often cannot compete in equal conditions with their larger counterparts in terms of bargaining power, lower costs, better prices, advertising and so forth.⁷²¹ For this reason a special protection, either through the application of a 'SME regime' or through a 'weak party regime', would greatly benefit those businesses and improve their chances of survival and growth in the marketplace.

⁷¹⁸ Stephen Waddams, 'Protection of Weaker Parties in English law' in M Kenny, J Devenney and LF O'Mahony (eds), *Unconscionability in European Private Financial Transactions: Protecting the Vulnerable* (Cambridge University Press 2010) 28.

⁷¹⁹ *Ibid.*

⁷²⁰ See CC 92519/SP (04/03/2009) and REsp 938979/DF (29/06/2012).

⁷²¹ Rice (n 600) 234-236.

CHAPTER 5. ANALYSIS OF UNRESOLVED ISSUES CONCERNING THE LEGISLATIVE CONTROLS ON UNFAIRNESS IN B2B AND B2C CONTRACTS IN ENGLAND AND BRAZIL

5.1. Context

As examined in the previous chapters, the English and Brazilian legal systems recognise that unfair terms and unreasonable exemption clauses may be included in consumer and business contracts. For this reason both jurisdictions have adopted legislative mechanisms which aim to prevent the application of the above terms or to render them ineffective. Nonetheless legislation which was enacted to solve the problem of unfairness in contracts is itself tainted by imperfections; hence it requires solutions to its own problems.

The first step to improve the legislation of both countries and make them more efficient is to identify its *unresolved issues*, which is the main objective of this chapter. Following the analysis of the problems that affect each of those legal systems individually, this study will proceed to the comparison of the identified issues. The subsequent chapter in its turn will identify lessons that England and Brazil may learn from each other in order to improve their respective legal system.

Due to fundamental distinctions between English law and Brazilian law, it is expected that they will raise issues of different nature. In England the Law Commission acknowledged the existence of inconsistencies and overlapping within the internal legislation of this jurisdiction.⁷²² Part of the problem is caused by the imposition of concepts and rules typical of civilian traditions to this common law system through the implementation of EU Directives.

By comparison, Brazil has its legislation organised in Codes which are a comprehensive collection of 'general clauses and legal principles' that intend to be 'a formulation of all inclusive rules' of a particular area of law.⁷²³ In other words the Brazilian legal system just like other civilian jurisdictions is considered 'complete, coherent with no gaps or antinomies';⁷²⁴ thus in principle it should be free of internal inconsistencies as opposed to the English legal system. However in practice the civilian legal systems are also not

⁷²² Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005).

⁷²³ De Cruz (n 10) 48.

⁷²⁴ Chaim Perelman, *Lógica Jurídica* (2nd edn, Martins Fontes 2004) 34.

impervious to flaws because their law is created by legislators who are imperfect beings. In fact there are observable conflicts among legal provisions which regulate the topic in analysis in Brazil. Although the Brazilian legal system prescribes ways of dealing with this problem,⁷²⁵ their application is not always straightforward.

5.2. Analysis of unresolved issues concerning the legislative controls on unfairness in B2B and B2C contracts in England

As seen above, the main issues surrounding the current statutory controls over unfair terms and exemption clauses in English law result from discrepancies in its internal legislation, in particular between UCTA 1977 and the UTCCR 1999. Those inconsistencies are partly caused by problems in the implementation of the Directive on Unfair Terms in Consumer Contracts into the English legal system.

5.2.1. Inconsistencies between UCTA and the UTCCR

In English law the *Unfair Contract Terms Act 1977* and the *Unfair Terms in Consumer Contracts Regulations 1999* are among the most relevant pieces of legislation for the purpose of this study. However, their intricate wording in addition to overlaps and inconsistencies between them has caused a great deal of complexity in the context of B2C contracts.⁷²⁶ This lack of clarity and transparency is particularly detrimental to consumers who usually struggle to understand the extent of their rights and obligations. It is also inconvenient for those businesses which would prefer to avoid using terms that may be regarded as ineffective by law.⁷²⁷

One of the most notorious differences between UCTA and UTCCR 1999 is related to their scope. While the Regulations are confined to consumer contracts and terms which were not individually negotiated, UCTA is also applicable to B2B contracts and negotiated terms. Nonetheless the UTCCR cover more types of consumer contracts than UCTA as the latter does not extend to various types of contracts (e.g., insurance, patent).⁷²⁸ The scope of the Regulations in its turn is also subject to exceptions which include 'contracts relating

⁷²⁵ Criteria of anteriority, speciality and hierarchy which will be analysed later in the chapter.

⁷²⁶ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 1.4.

⁷²⁷ Macdonald, 'Unifying Unfair Terms Legislation' (n 5) 69-72.

⁷²⁸ Schedule 1 contains a list of contracts that are not within the scope of the Act. UCTA is also not applicable to arbitration clauses (s. 13 (2)) neither to international supply contracts (s. 26).

to employment, succession rights, rights under family law, and the incorporation and organisation of companies and partnerships'.⁷²⁹

Although UCTA was the first statute in England that purported to control the unfairness of contracts more generally, its title is misleading because the Act does not cover all unfair terms, but only exemption clauses that seek to exclude or limit liability.⁷³⁰ Those clauses are also regulated by the UTCCR 1999, but unfair terms which are not exemption clauses may be affected only by the Regulations.

On the other hand, as the definition of 'consumer' in UCTA is wider than in the UTCCR 1999⁷³¹ some exemption clauses can be included in its scope but not in the Regulations.⁷³²⁷³³ This distinction between the 'consumer' definitions may result in other discrepancies in the application of both pieces of legislation to an individual case. For instance, a person who buys goods at auction is not a consumer for the purpose of UCTA (s. 12(2)), but he may be regarded as such within the scope of the Regulations.

Further differences consist of the fact that although UCTA is quite detailed in comparison with UTCCR 1999, the latter contain general provisions (e.g., reg. 5(1)) that provide more leeway to courts in the control on unfairness in consumer contracts. Beale contended that this discretion conferred on judges gives rise to some degree of *uncertainty* to businesses, but such uncertainty could be minimised through the use of '*black lists*'.⁷³⁴ Those lists would enable businesses to predict with more accuracy the risks of invalidation of terms and protect their interests accordingly. As a consequence the '*grey list*' (which terms are not presumptively invalid) provided by Schedule 2 of the Regulations may not allow suppliers to anticipate with sufficient certainty whether a term will be considered ineffective by judges.⁷³⁵

⁷²⁹ Howells and Brownsword (n 193) 244. The UTCCR are also neither applied to contractual terms which reflect mandatory statutory or regulatory provisions of the United Kingdom nor to provisions or principles of international conventions to which the Member States or the Community are party (reg. 4(2)).

⁷³⁰ Koffman and Macdonald (n 1) 199.

⁷³¹ According to UCTA 1977, a party 'deals as consumer' if does not make the contract in the course of a business or holds him out as doing so; the other party does make the contract in the course of a business; and (...) the goods passing under or in pursuance of the contract are of a type ordinarily supplied for private use or consumption (s. 12(1)). The UTCCR 1999 in its turn define consumer as 'any natural person who is acting for purposes which are outside his trade, business or profession (reg. 3(1)).

⁷³² F.M.B. Reynolds, 'Unfair Contract Terms' (1994) 110 LQR 1, 2.

⁷³³ As seen in chapter 3, according to the UTCCR 1999 the definition of consumer is limited to 'natural person'; whereas for the purpose of UCTA companies may also deal as consumers.

⁷³⁴ Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 246.

⁷³⁵ Ibid.

A 'black list' however can be found in UCTA as this Act makes certain exclusion or restriction clauses of no effect at all⁷³⁶ (terms are 'unfair under all circumstances') and subject the others to a *reasonableness test* ('rebuttable presumption of unfairness').⁷³⁷ The Law Commission proposed that this 'requirement of reasonableness' should be combined with the 'fairness test' of the Regulations and replaced by a 'fair and reasonable' test with no express reference to 'good faith' in order to facilitate its application by UK lawyers.⁷³⁸

The Law Commission highlighted the main differences between UCTA and the UTCCR 1999 in its Consultation Paper as outlined below:⁷³⁹

	UCTA 1977	UTCCR 1999
Types of Contracts	Applies to both B2C and B2B contracts.	Apply only to B2C contracts.
Types of Clauses	Applies only to exclusion and limitation of liability clauses (and indemnity clauses in consumer contracts).	Apply to any kind of term other than the definition of the main subject matter of the contract and the price.
Black list/ Grey list	Makes certain exclusions or restrictions of no effect at all (<i>black list</i>).	Do not make any particular type of term of no effect at all (<i>grey list</i>).
Review Mechanism	Subjects others to a <i>reasonableness</i> test.	Subject the terms to a <i>fairness</i> test.
Guidelines	Contains guidelines for the application of the reasonableness test.	Do not contain detailed guidelines as to how the fairness test should be applied, but contain a so-called <i>grey list</i> of terms which 'may be regarded' as unfair.
Burden of Proof	Puts the burden of proving that a term within its scope is reasonable on the party seeking to rely on the clause.	Leave the burden of proof that the clause is unfair on the consumer.
Standard Form/ Negotiated Terms	Applies for the most part whether the terms were negotiated or were in a 'standard form'.	Apply only to 'non-negotiated' terms.

⁷³⁶ See Koffman and Macdonald (n 1) 201. E.g., 'business liability for death or personal injury to anyone caused by negligence (s. 2(1)) and business liability for breach of the implied terms as to the description, quality, etc in contracts for the supply of goods to a party dealing as a consumer (ss. 6(2), 7(2))'. See Chen-Wishart (n 3) 479. The black-list contains terms which will be always regarded as unfair because their application would inevitably have harmful consequences to the interests of the party who did not draft them. For that reason the other party should not be allowed to argue for the reasonableness of those terms in order to enforce them.

⁷³⁷ Schillig (n 424) 357.

⁷³⁸ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) paras 3.85 and 3.91.

⁷³⁹ This table was based on the Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) paras 2.18 to 2.19 and Chen-Wishart (n 3) 463.

Application to B2C Contracts	Does not apply to certain types of contract, even when they are consumer contracts.	Apply to consumer contracts of all kinds.
Enforcement Mechanism and Effect	Has effect only between the immediate parties.	Are not only effective between the parties but empower various bodies to take action to prevent the use of unfair terms.

5.2.2. Problems in the implementation of Directive 93/13/EEC

Due to time constraints the implementation of the *Directive on Unfair Terms in Consumer Contracts*⁷⁴⁰ into English Law was rushed and made through Regulations. In line with Section 2(2) of the European Communities Act 1972,⁷⁴¹ this directive could have instead amended the existing national law (e.g., UCTA)⁷⁴² and repealed inconsistent legislation 'to create a coherent and harmonised whole'.⁷⁴³ As a consequence although England introduced the substance of the directive, it 'fails to harmonise the instrument with existing legislation'.⁷⁴⁴

The contents of the Directive 93/13/EEC and the manner in which the implementation was carried out caused a number of uncertainties and complexities that have been subject of extensive debate in the legal literature.⁷⁴⁵ This study will examine some of the most common problems identified by interpreters.

⁷⁴⁰ Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts [1993] OJ L95/29.

⁷⁴¹ Section 2(2) (European Communities Act 1972): 'Subject to Schedule 2 to this Act, at any time after its passing Her Majesty may by Order in Council, and any designated Minister or department may [by order, rules, regulations or scheme], make provision - (a) for the purpose of implementing any [EU obligation] of the United Kingdom, or enabling any such obligation to be implemented, or of enabling any rights enjoyed or to be enjoyed by the United Kingdom under or by virtue of the Treaties to be exercised; or (b) for the purpose of dealing with matters arising out of or related to any such obligation or rights or the coming into force, or the operation from time to time, of subsection (1) above; and in the exercise of any statutory power or duty, including any power to give directions or to legislate by means of orders, rules, regulations or other subordinate instrument, the person entrusted with the power or duty may have regard to the [objects of the EU] and to any such obligation or rights as aforesaid.'

⁷⁴² In France and Germany the Directive 93/13/EEC 'was grafted on to the national systems', 'but in England it was dealt with separately'. See Youngs (n 110) 623.

⁷⁴³ Howard Johnson, 'Unfair Contract Terms: Implementation Problems' (1994) 13(6) IBFL 66, 66. See also Reynolds (n 732) 2.

⁷⁴⁴ Hondius (n 121) 249.

⁷⁴⁵ According to Johnson the UK government is 'choosing to adopt a complex and ill-fitting manner of implementation which, outside of an Alice in Wonderland-type world, it is difficult to see being at all user friendly for either business or consumers'. See Johnson (n 743) 66.

5.2.2.1. Definition of unfair terms

At the heart of the Directive 93/13/EEC is the definition of 'unfair terms' in its article 3.1 which was already exhaustively examined:

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.

Article 3.3 (which makes reference to 'an indicative and non-exhaustive list of the terms which may be regarded as unfair') is also important in delineating the meaning of unfair terms, but its interrelationship with article 3.1 was not specified by the directive as those provisions do not make reciprocal references.⁷⁴⁶ Therefore it is possible to argue either that article 3.3 is supplementary to article 3.1 or that they are independent tests of unfairness.⁷⁴⁷

Brownsword, Howells and Wilhelmsson contended that from the analysis of article 3.1 it is quite evident that a term is *unfair* if it causes: (i) 'a significant imbalance' (ii) 'to the detriment of the consumer'; but it is unclear if (i) and (ii) necessarily implies that the term is contrary to (iii) 'the requirement of good faith' or if (iii) is an independent condition. Moreover if the requirement of *good faith* is regarded as an independent condition there are further questions on whether such condition has a procedural or substantive nature or whether it involves both procedural and substantive elements, as examined in chapters 1 and 3.⁷⁴⁸

Legal literature has not reached a consensus on this matter yet. One of the consequences of the pressured implementation of the directive was that the wording of this article 3.1 was practically reproduced in reg. 5(1); hence the concept of '*good faith*' was transplanted into English law quite apart from any question of its compatibility with UCTA 1977 or the common law and the UK government did not specify its preferable interpretation.⁷⁴⁹

⁷⁴⁶ Brownsword, Howells and Wilhelmsson, 'Between Market and Welfare: Some Reflections on Article 3 of the EC Directive on Unfair Terms in Consumer Contracts' (n 77) 33-36.

⁷⁴⁷ Ibid.

⁷⁴⁸ Ibid. 31-32.

⁷⁴⁹ Ibid. 32.

Another issue concerning the good faith prescribed by article 3.1 is that its application is limited to the *performance* of the contracts as examined in chapters 2 and 3. Quagliato argued that in England 'the assumption is that the parties enter into negotiation at their own risk and unless and until they conclude the contract they have no claim whatever on the other party',⁷⁵⁰ because as Furmston, Norisada and Poole observed in common law 'it has tended to take the position that either there is a contract or there is not'.⁷⁵¹

In England such absence of good faith in *negotiations* may give rise to unjust situations at the pre-contractual stage.⁷⁵² In order to offer some protection to people who may have legitimate expectations created during the bargaining process, the English law has adopted piecemeal solutions such as negligent misstatement, promissory estoppel and restitution.⁷⁵³ However the adoption of a general duty of good faith applicable to all contractual stages may offer a more adequate protection to parties in negotiation, as will be seen in chapter 6.

A further limitation on the application of the requirement of good faith is that it is only applicable to *standard form contracts* in transactions involving consumers, which may prove this requirement 'largely redundant in English consumer protection law'.⁷⁵⁴ For instance harsh terms that may disadvantage consumers may be included in contracts regarded as negotiated. Moreover if the purpose of good faith is to avoid the unfair surprise as proposed by Dugan,⁷⁵⁵ then suppliers may satisfy such requirement by simply bringing the contents of terms to the attention of consumers or clarifying their meaning.⁷⁵⁶

5.2.2.2. Interpretation of general clauses by Courts

Willet suggested that the generality of clauses used in the definition of unfair terms such as *good faith* and *significant imbalance* means that 'they can often only be given real practical meaning and direction by reference to some background ethic' which are based

⁷⁵⁰ Quagliato (n 82) 218.

⁷⁵¹ For this reason common law 'has not found it easy to give legal effect' to the perception that interim agreements during the negotiating process may bind parties. See Furmston, Norisada and Poole, *Contract Formation and Letters of Intent: A Comparative Assessment* (n 84) 267.

⁷⁵² See chapters 2 and 6.

⁷⁵³ Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part II' (n 224) 118.

⁷⁵⁴ See also Brownsword, 'Two Concepts of Good Faith' (n 160) 242.

⁷⁵⁵ According to Dugan 'surprise' may constitute 'abuse' when 'the content of the standardized term diverges from the expectations of the nondrafter'. See Robert Dugan, 'Good Faith and the Enforceability of Standardized Terms' (1980-1981) 22 WMLR 1, 4.

⁷⁵⁶ Brownsword, 'Two Concepts of Good Faith' (n 160) 242.

either on 'values of trader *self interest* and consumer *self reliance*' or on the protection of the consumer.⁷⁵⁷ Although the latter ethic is more in line with the EU position, the (now) Supreme Court has adopted the former ethic which does not provide the same level of protection as intended at EU level and remains influenced 'by strong individualistic values' typical of common law.⁷⁵⁸

For instance in *Director General of Fair Trading v First National Bank plc*⁷⁵⁹ the House of Lords understood that the term which stipulated that a bank could charge interest at contractual rate after the judgment was not unfair because banks should be able to recover the whole amount of interest due on default.⁷⁶⁰ Therefore the right of the bank to pursue its self-interest was more important than the 'economic impact' that this decision had on the consumer.⁷⁶¹

5.2.2.3. Exceptions to the fairness assessment

While article 3 of the Directive 93/13/EEC prescribes a *test of fairness* to contractual terms in general, article 4.2 (implemented by reg. 6(2)) expressly exempts from the above test the so-called 'core terms' (related to the definition of the main subject matter of the contract or to the adequacy of the price and remuneration) as long as those terms are *written in plain intelligible language*.⁷⁶²

Bright observed that the reason behind this exception is to exclude terms which may reflect a 'free choice' of the parties because 'the price and quality of products' are two aspects that consumers usually take into account in their decision on entering or not a contract.⁷⁶³ For the same reason terms which were negotiated are also excluded from the fairness test.

⁷⁵⁷ Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 413.

⁷⁵⁸ Ibid. 415 and 431. 'The effect has been to limit the protective potential of the general clause; notably, in cases where it might provide protection that was not available under pre-existing domestic law'.

⁷⁵⁹ [2001] UKHL 52, [2002] 1 AC 481.

⁷⁶⁰ *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 AC 481 [43].

⁷⁶¹ Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 421-422.

⁷⁶² In Case C-484/08 *Caja de Ahorros y Monte de Piedad de Madrid v Asociación de Usuarios de Servicios Bancarios (Ausbanc)* [2010] ECR I-04785 the European Court decided that articles 4(2) and 8 of the Directive 93/13/EEC does not preclude national legislation which authorises a judicial review as to the fairness of core terms, even if they are drafted in plain, intelligible language. This not however the case of English law which transposed art. 4(2) into reg. 6(2).

⁷⁶³ Bright, 'Winning the Battle against Unfair Contract Terms' (n 434) 344.

Although apparently straightforward, the application of reg. 6(2) contains some difficulties. First of all it is unclear 'whose standard of plainness and intelligibility is to apply'.⁷⁶⁴ This may give rise to a great deal of uncertainty as its determination is a prerequisite for the exemption of the core provisions.

Furthermore, even if it was possible to establish that the term was written in plain intelligible language, reg. 6(2) prescribes that the assessment of fairness of such term 'shall not relate to' core terms. Howells and Brownsword noted that this provision may leave the interpreter under the impression that the Regulations 'prohibit reference to the core provisions in assessing the fairness of non-core terms' when in reality 'in assessing the fairness of a term, reference should be made to "all the other terms of the contract"'.⁷⁶⁵ Otherwise it would be rather problematic to apply the test of fairness 'which looks to a significant detrimental imbalance in relation to one non-core term if the imbalance basically lies in the core term'.⁷⁶⁶

All the above discussion however would be meaningless in the impossibility of determining which terms can be regarded as 'core'. This leads to another problem concerning 'where the line might be drawn between definitional and non-definitional⁷⁶⁷ terms', because only those terms which define the main subject-matter of the contract will be excluded from the fairness test.⁷⁶⁸ On the occasions when English courts confronted this problem, they rejected the definitional argument used as 'an attempted evasion of desirable control over unfair terms'.⁷⁶⁹ In other words, judges tend to adopt a more restrictive approach when considering a term as 'core', otherwise there would have a 'potential for the directive to be rendered largely ineffective'⁷⁷⁰ if a large number of terms could be excluded from the test of fairness.

However, as seen in chapter 3, in *Office of Fair Trading v Abbey National plc and Others*⁷⁷¹ the Supreme Court held that bank charges for unauthorised overdrafts were core terms under reg. 6(2) even though the Court of Appeal and the OFT argued that

⁷⁶⁴ Howells and Brownsword (n 193) 248.

⁷⁶⁵ *Ibid.*

⁷⁶⁶ Elizabeth Macdonald, 'Mapping the Unfair Contract Terms Act 1977 and the Directive on Unfair Terms in Consumer Contracts' [1994] JBL 441, 460.

⁷⁶⁷ E.g., clauses dealing with secondary obligations.

⁷⁶⁸ Macdonald, 'Mapping the Unfair Contract Terms Act 1977 and the Directive on Unfair Terms in Consumer Contracts' (n 766) 461.

⁷⁶⁹ *Phillips Products Ltd v Hyland* [1987] 1 WLR 659, 666.

⁷⁷⁰ Macdonald, 'Mapping the Unfair Contract Terms Act 1977 and the Directive on Unfair Terms in Consumer Contracts' (n 766) 462.

⁷⁷¹ [2009] UKSC 6, [2010] 1 AC 696, [2009] EWCA Civ 116.

those charges would not be perceived by consumers as 'essential to the bargain'.⁷⁷² This decision just added more uncertainty to the definition of 'price or remuneration'.

It is noteworthy that the Law Commission has recently published new recommendations, as mentioned in the earlier chapters, which suggested a different interpretation for the 'price and main subject matter exemption' and proposed that only terms which are *transparent* and *prominent* should be exempted from the fairness test.⁷⁷³ Those recommendations were open to consultation and may result in significant changes to reg. 6(2) which may improve its clarity and facilitate its application by courts.

5.2.2.4. Pre-emptive challenges

Article 3 prescribes an *ex casu* challenge to the unfairness of contractual terms which means that it can be proposed by individual consumers, but fails to distinguish it from the *pre-emptive* challenge described by article 7(2) of the Directive.⁷⁷⁴ The latter introduced a preventive mechanism against the continued use of unfair terms in contracts which can be proposed by 'persons or organizations' who have a legitimate interest under national law in protecting consumers.⁷⁷⁵

According to article 7 each Member State should provide *adequate and effective means* to prevent the continued use of unfair terms in contracts concluded with consumers by sellers or suppliers. However there are questions as to whether this provision was fully or adequately implemented. For instance it is unclear if the injunction procedures are sufficient to fulfil the purpose of this provision or whether it would also require *criminal sanctions*.⁷⁷⁶ Nevertheless there is some reluctance in relation to the application of the latter in the absence of 'black-list' terms (which are automatically of no effect), because

⁷⁷² Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 426.

⁷⁷³ See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) paras 8.2 and 8.4.

⁷⁷⁴ The directive 'does not explicitly identify the fairness regime applicable to each kind of challenge'. According to Brownsword, Howells and Wilhelmsson there are two approaches in the application of article 3 of the EC Directive 93/13 (that was implemented by reg. 5). The first one is that art. 3(1) is applied as a master test to pre-emptive and *ex casu* challenges and art. 3(3) is only a check list of sample unfair terms. In line with the second approach, art. 3(1) is applied to *ex casu* challenges whilst art. 3(3) is applied to pre-emptive challenges. See Brownsword, Howells and Wilhelmsson, 'Between Market and Welfare: Some Reflections on Article 3 of the EC Directive on Unfair Terms in Consumer Contracts' (n 77) 28 and 36-37.

⁷⁷⁵ In England even though the Director General of the Office of Fair Trading (DGFT) and qualifying bodies are 'unable to offer redress to private disputes' they can propose pre-emptive challenges to unfairness as stated in reg. 12. Roland Fletcher, 'Good Faith or a Contagious Disease of Alien Origin?' (2002) 23(1) BLR 5, 5-6.

⁷⁷⁶ Howells and Brownsword (n 193) 259. More recently part 3 of the *Consumer Protection from Unfair Trading Regulations 2008* regards certain unfair commercial practices as criminal offences.

the 'grey list' in the Regulations may not provide enough certainty for the application of criminal sanctions as discussed in chapter 3.⁷⁷⁷

5.3. Analysis of unresolved issues concerning the legislative controls on unfairness in B2B and B2C contracts in Brazil

Marques suggested that one of the main challenges of the contemporary Brazilian lawyer and courts is to deal with the plurality of legislative acts and potential conflicts among them.⁷⁷⁸ In Brazil the interpretation of legislative provisions used to adopt a more *formalist* approach, according to which courts were essentially limited to a mechanical application of the rules to the facts.⁷⁷⁹ As a consequence apparent disagreements between legal provisions which regulate the same subject matter caused some perplexity among judges.

This *formalist* thinking was mitigated by the introduction of general clauses, such as good faith, which have given judges more flexibility in the application of the law and led to the adoption of a more *realist* approach. The latter may be more adequate than the former approach in view that:

'Gaps will always exist because not everything can be anticipated or accounted for in advance; conflicts may arise between different bodies of rules; [...] and language is subject to ambiguity'.⁷⁸⁰

Nonetheless conflicts and ambiguities are problems which are not limited to legal rules created by legislators, but they also affect contractual terms drafted by parties. In the latter case however the law of contracts may afford some guidance to interpreters. For instance if the term is unclear, the Civil Code and the Consumer Protection Code prescribe that the interpretation most favourable to the adhering party or to the consumer should be adopted,⁷⁸¹ which is in line with the interventionist approach adopted by the Brazilian legal system in favour of the weaker party.

⁷⁷⁷ Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 254.

⁷⁷⁸ Claudia Lima Marques, 'Diálogo entre o Código de Defesa do Consumidor e o Novo Código Civil: do Diálogo das Fontes no Combate às Cláusulas Abusivas' (2003) São Paulo, jan./mar, v. 12, f. 45 Revista de Direito do Consumidor 71, 72.

⁷⁷⁹ Alberto Amaral Júnior, 'A Boa Fé e o Controle das Cláusulas Contratuais Abusivas nas Relações de Consumo' (1993) São Paulo, n.6, abr/jun, Revista de Direito do Consumidor 27, 32.

⁷⁸⁰ Tamanaha (n 113) 190.

⁷⁸¹ See article 423 of the Civil Code and article 47 of the Consumer Protection Code.

5.3.1. Conflicts of law

In Brazil there are three main pieces of legislation that tackle contractual unfairness: the Federal Constitution, the Civil Code and the Consumer Protection Code. In order to remedy possible *conflicts of law*,⁷⁸² the Brazilian legal system prescribes mechanisms which aim to harmonise and coordinate its rules: the criteria of *anteriority*, *speciality* and *hierarchy*. They are particularly important to a civil law jurisdiction which presupposes an articulated system of abstract rules that should be exhaustive and consistent.⁷⁸³

Brazilian courts and legal practitioners employ those mechanisms on a regular basis in order to identify the applicable rule to individual cases. On a number of occasions however such exercise is not an obvious task. For instance although the Civil Code and Consumer Protection Code share fundamental principles, such as the social function of contracts, their provisions may contain some divergences which can give rise to disputes concerning their application.

5.3.1.1. Civil Code *versus* Consumer Protection Code

In cases where there are apparent conflicts between the provisions of the Civil Code and the Consumer Protection Code, the criteria of *hierarchy* and *anteriority* may not be of great assistance. Both codes are federal acts, thus they belong to the same category of law. Additionally although the Civil Code was enacted over a decade after the Consumer Protection Code, the former did not revoke the later because they are (at least in theory) compatible and have different areas of application.⁷⁸⁴

Therefore in the emergence of conflicts involving the aforementioned Codes the only applicable criterion is the *speciality* one, according to which in a B2C contract the general

⁷⁸² 'Conflict of laws' in Brazil is concerned mainly to the internal legislation; whereas in England it 'comes into play whenever a dispute before the English court contains one or more foreign elements'. See Abla J. Mayss, *Principles of Conflicts of Laws* (3rd edn, Cavendish 1999) 11.

⁷⁸³ Fuller suggested that a man who is subjected to contradictory orders from the law cannot be expected to respond appropriately to future orders; thus the need for dealing with apparent contradiction in the law. See Lon L. Fuller, *The Morality of Law* (2nd edn, Yale University Press 1969) 66.

⁷⁸⁴ Under article 2 of the *Law of Introduction to the Brazilian Civil Code* 'unless intended to have temporary effect, legislation shall be in force until other legislation modifies or revokes it'. In addition its first paragraph prescribes that 'subsequent legislation revokes earlier legislation when it expressly so declares, when it is incompatible with the earlier or when it entirely regulates the matter dealt with the earlier legislation'. See Rose (n 251) 1.

rules of the Civil Code are considered subsidiary to the special rules of the Consumer Protection Code.⁷⁸⁵

In order to apply this criterion, it is necessary to establish the scope of application of each of those Codes. Contracts between sellers/suppliers and consumers are governed by the Consumer Protection Code which prescribes protective measures in favour of consumers on the basis of the inequality of bargaining strength between parties. Other civil obligations are generally regulated by the Civil Code or special legislation that presumes a relative equality between parties and is less interventionist.

The determination of the area of application of the Civil Code to contracts is a *herculean task* in this highly complex, micro-codified, plural and fluid legal system; because the roles of the parties in the market and society change from one act to another.⁷⁸⁶

The Civil Code protects mainly individual rights, whereas the Consumer Protection Code purports to protect consumers individually and collectively.⁷⁸⁷ For this reason, once interpreters establish that a contract is a B2C agreement they have to determine whether the subjective right in question is individual or collective because the applicable rules and proceedings may differ.⁷⁸⁸ For example, a contract of sale made between a company and a consumer is clearly a B2C contract. If its terms affect the rights and interests of various consumers (determined or not), certain public bodies and associations can propose a legal action to protect them collectively.⁷⁸⁹

It is noteworthy that there are provisions of the Civil Code that are considered of 'public order' (mandatory rules) and as such they should prevail over the Consumer Protection Code rules in spite of the criterion of speciality.⁷⁹⁰ However one could argue that all rules

⁷⁸⁵ Marques, 'Diálogo entre o Código de Defesa do Consumidor e o Novo Código Civil: do Diálogo das Fontes no Combate às Cláusulas Abusivas' (n 778) 98. According to article 2, second paragraph of the *Law of Introduction to the Brazilian Civil Code* 'new legislation that establishes general or special provisions on a par with the existing legislation neither revokes nor modifies the earlier legislation'. See Rose (n 251) 1.

⁷⁸⁶ Marques, 'Diálogo entre o Código de Defesa do Consumidor e o Novo Código Civil: do Diálogo das Fontes no Combate às Cláusulas Abusivas' (n 778) 87.

⁷⁸⁷ See article 81 of the Consumer Protection Code.

⁷⁸⁸ Marques, 'Diálogo entre o Código de Defesa do Consumidor e o Novo Código Civil: do Diálogo das Fontes no Combate às Cláusulas Abusivas' (n 778) 80.

⁷⁸⁹ See *Public Civil Action Act* (Act 7347/1985).

⁷⁹⁰ Mandatory rules are always binding and cannot be excluded by the agreement of the parties. According to the sole paragraph of article 2035 (Civil Code) 'no agreement shall prevail if it is contrary to rules of public order, such as those established by this Code to ensure the social function of property and contracts'. See Rose (n 251) 433.

of the Consumer Protection Code are of 'public order' and 'social interest' in line with its article 1; consequently their special provisions should always prevail.⁷⁹¹

Nonetheless article 7 of the Consumer Protection Code expressly prescribes that its provisions do not exclude the application of other pieces of legislation;⁷⁹² because although this code is a special law in the context of consumer relations, it recognises that its rules are not exhaustive and complete.

For instance, although article 51 of this code prescribes a list of abusive clauses that are considered void, the conceptual basis for interpretation of when a juridical transaction is void is actually found in article 166 of the Civil Code.⁷⁹³ In addition, provisions of the Civil Code may prevail over the Consumer Protection Code if their interpretation is more favourable to consumers.⁷⁹⁴

5.3.2. General rules of contracts

Contracts between businesses or non-consumers are regulated by the general rules of articles 421 to 426 of the Civil Code.⁷⁹⁵ Those contracts are presumably made between equal parties who are able to negotiate the content of terms. However if a court concludes that there is an inequality of bargaining power between the parties, it may apply the rules of the Consumer Protection Code by analogy.⁷⁹⁶

⁷⁹¹ Article 1 of the Consumer Protection Code prescribes that 'the present Code establish rules of consumer protection, which are of public order and social interest in accordance with articles 5, XXXII and 170, V of the Federal Constitution and article 48 of its Transitional Provisions.' According to art. 5, XXXII of the Federal Constitution the Brazilian fundamental rights and guarantees include the protection of consumers and art. 170, V stipulates that one of the principles of the economic activity is the consumer protection. In addition article 48 of its Transitional Provisions prescribes that the National Congress should draw up a consumer protection code within 120 days of the Constitution's promulgation.

⁷⁹² Art. 7 of the Consumer Protection Code: 'the rights prescribed by this Code do not exclude other rights arising from treaties or international conventions to which Brazil is signatory, the internal legislation, the regulations issued by administrative authorities as well as those derived from general principles of law, analogy, customs and equity'.

⁷⁹³ For example, according to article 166 a juridical transaction is void when: 'IV – it is not made in the form prescribed by law'; (...) 'VII - the law expressly declares it to be void or prohibits the transaction, without imposing any sanction'. See Rose (n 251) 43.

⁷⁹⁴ E.g., art 431 (Civil Code) 'a penalty must be reduced by the judge, on an equitable basis, if the principal obligation has been performed in part, or if the amount of the penalty is manifestly excessive, considering the nature and purpose of the transaction'. See Ibid. 86.

⁷⁹⁵ Those general rules of contracts have a subsidiary application in B2C contracts.

⁷⁹⁶ The Superior Court of Justice has extended the protection offered to consumers against abusive clauses to vulnerable parties even if they are not strictly considered consumers. Justice Nancy Andrighi applied the maximalist approach promoting a wider application of the rules of the Consumer Protection Code. See REsp 1010834/GO (13/10/2010). See chapter 4.

Article 424 is the only provision of the Civil Code that expressly regulates abusive clauses. It says 'in contracts of adhesion, clauses that stipulate that the adhering party has waived, in advance, rights arising out of the nature of the transaction are void'.⁷⁹⁷ Nevertheless this Code does not contain a definition of '*contract of adhesion*'; by comparison the Consumer Protection Code defines the above type of contract as 'one whose clauses have been approved by the competent authority or which has been established unilaterally by the supplier of goods or services without giving the consumer the opportunity to discuss or substantially modify its contents'.⁷⁹⁸ However the Brazilian Supreme Federal Court decided that this definition cannot be extended to contracts in general because its scope should be limited to consumer contracts.⁷⁹⁹

5.3.2.1. Deficiencies of article 422 (Civil Code)

Unquestionably article 422 is one of the most important general provisions of the Brazilian law of contracts. As seen previously, it prescribes that 'the contracting parties are bound to observe the principles of probity and good faith, both in entering into the contract and in its performance'.⁸⁰⁰

Notwithstanding the relevance of this provision, Junqueira de Azevedo contended that it is 'insufficient and deficient'.⁸⁰¹ Article 422 leaves unclear whether parties are allowed to agree on the exclusion of this duty of good faith and whether they can define the standard of this obligation in the performance of the contract.⁸⁰² Moreover, its application is limited from the moment when parties enter the contract to its performance; thus it does not expressly include the pre-contractual and post-contractual stages in which good faith is also of great relevance as seen in chapter 3.

Nonetheless as Tucci pointed out case law and legal literature have extended the duty of good faith beyond the limits of article 422, because parties are expected to respect the trust created before and after they enter and perform a contract as well as the reasonable

⁷⁹⁷ Rose (n 251) 88.

⁷⁹⁸ See article 54 of the Consumer Protection Code.

⁷⁹⁹ SEC (Sentença Estrangeira Contestada) 5847-1 (01/12/1999).

⁸⁰⁰ Rose (n 251) 88.

⁸⁰¹ Antonio Junqueira de Azevedo, 'Insuficiências, Deficiências e Desatualização do Projeto de Código Civil na Questão da Boa-Fé Objetiva nos Contratos' (2000) São Paulo, maio, v. 89, f. 775 Revista dos Tribunais 11, 11.

⁸⁰² By comparison the *American Uniform Commercial Code* explicitly provides in § 1-302(b) that, while the effect of its provisions may be modified by agreement, the obligation of good faith 'may not be disclaimed by agreement' but the parties may by agreement 'determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.' See *Ibid.* 12.

expectations of the other party at all times.⁸⁰³ Therefore the duty of good faith has also been applied to the negotiation stage and to the enforcement stage when parties do not fulfil the obligation satisfactorily.

5.3.3. Functions of the concept of good faith

The aforementioned article 422 and article 113⁸⁰⁴ of the Civil Code prescribe that the principle of good faith has essentially the function of guiding the interpretation of contracts.⁸⁰⁵ Nonetheless Junqueira de Azevedo argued that this code has neglected another two fundamental functions of this principle.⁸⁰⁶

For instance the *supplementary* function was overlooked by those provisions. This function purports to supply an omitted term which would be important for the determination of parties' rights and duties.⁸⁰⁷ It is however expressly prescribed in other pieces of legislation such as article 4.8 of the *Principles for International Commercial Contracts* of the UNIDROIT.⁸⁰⁸

The other omitted function is the *rectification* of abusive clauses which purports to prevent or tackle unfair terms and that can be found in more recent legislation of other jurisdictions such as EU Member States.⁸⁰⁹ Junqueira de Azevedo argued that the reason why this function cannot be found in the current Brazilian Civil Code is due the significant amount of time elapsed between its draft Bill and its enactment; thus by the time when

⁸⁰³ Cibele Pinheiro Marçal Cruz Tucci, 'Teoria Geral da Boa-Fé Objetiva' (2002) São Paulo, v. 22, f. 68 Revista do Advogado 100, 105.

⁸⁰⁴ Article 113 (Civil Code) 'juridical transactions shall be interpreted in conformity with good faith and the practice of the place in which they are made'. See Rose (n 251) 34.

⁸⁰⁵ Article 113 adopts good faith as an external and objective criterion of interpretation of contracts; whereas article 112 adopts a subjective criterion according to the will of the parties. It says 'in declarations of will, more heed shall be given to the intention revealed through the declaration than to the literal meaning of the language'. See Pinheiro (n 117) 168 and Rose (n 251) 34.

⁸⁰⁶ Junqueira de Azevedo, 'Insuficiências, Deficiências e Desatualização do Projeto de Código Civil na Questão da Boa-Fé Objetiva nos Contratos' (n 801) 14-15.

⁸⁰⁷ Ibid. This function also implies the existence of secondary duties of good faith such as information.

⁸⁰⁸ Article 4.8 (Supplying an Omitted Term): (1) Where the parties to a contract have not agreed with respect to a term which is important for a determination of their rights and duties, a term which is appropriate in the circumstances shall be supplied. (2) In determining what is an appropriate term regard shall be had, among other factors, to (a) the intention of the parties; (b) the nature and purpose of the contract; (c) *good faith* and fair dealing; (d) reasonableness. In addition article 5.2. prescribes implied obligations which 'stem from: (a) the nature and purpose of the contract; (b) practices established between the parties and usages; (c) *good faith* and fair dealing; (d) reasonableness'.

⁸⁰⁹ Junqueira de Azevedo, 'Insuficiências, Deficiências e Desatualização do Projeto de Código Civil na Questão da Boa-Fé Objetiva nos Contratos' (n 801) 14-15.

this code finally came into force, part of its contents was already outdated.⁸¹⁰ As a consequence even though the enactment of the Consumer Protection Code was prior to the new Civil Code, its contents are more modern and up-to-date and include a provision that declares void abusive clauses which are incompatible with good faith (art. 51, IV).

5.4. Analysing the differences and similarities between these unresolved issues concerning the legislative controls on unfairness in B2B and B2C contracts in England and Brazil

As can be observed, although the Brazilian legal system purports to be exhaustive, it is far from being perfect. Brazilian legislators have created a complex system of interrelated pieces of legislation in an attempt to cover all possible situations that may result in abuses of the weaker party. As a consequence the interpretation and application of legal provisions may be quite challenging at times.

Nevertheless the codification of the civil legislation and in particular of the consumer law has undoubtedly improved the protection afforded to contractual parties, which has been reinforced by court decisions that aimed at achieving a fair application of contractual terms and the protection of the vulnerable party.

The English legal system shares a similar problem concerning the harmonious coexistence of different pieces of legislation which tackle the unfairness of contractual terms, in particular UCTA and the UTCCR. Macdonald contended that they are 'completely unrelated to each other' and their 'complexities become considerable when their differences and overlaps fall to be considered'.⁸¹¹ In addition there are also questions on whether the Directive 93/13/EEC was satisfactorily implemented by the Regulations in England.

5.4.1. Inconsistent legislation

The above pieces of legislation in England are neither user friendly to consumers who should be able to easily understand the rights that they are entitled to; nor to businesses

⁸¹⁰ Ibid. 14-15. The Bill of the current Civil Code dates back to 1975, but it was published only on 11/01/2002 coming into force on 13/01/2003.

⁸¹¹ See Macdonald, 'Unifying Unfair Terms Legislation' (n 5) 69. See Law Commission, *Unfair Terms in Contracts* (Law Com CP No 166, 2002) paras 3.1 to 3.124 which addressed 'overlaps and differences between UCTA and UTCCR'.

who require a reasonable level of certainty and predictability in their transactions. Brownsword pointed out that 'rules need to be clear, results should be calculable, people must know where they stand'.⁸¹²

Before the Consumer Protection Code came into force in 1991, the Brazilian consumer legislation used to face a similar problem to the one that English law is experiencing nowadays, i.e. the lack of a unified regime to deal with the protection of consumers.⁸¹³ According to Bittar the piecemeal legislation about the topic did not have a concrete application and did not prevent abusive practices against consumers.⁸¹⁴ The Consumer Protection Code significantly improved the consistency of the consumer rules, but judges should be mindful that there are still some situations that may be covered by provisions of the Civil Code as seen previously.

By comparison in the context of business contracts, some fundamental institutions of commercial law in Brazil (e.g., bankruptcy, debt instrument and business corporation) are regulated by different legislative acts.⁸¹⁵ Such decentralisation of the legislation that governs B2B contracts may lead to its lack of unity and to the discredit of the provisions of the Civil Code;⁸¹⁶ but it is possible to argue that because they cover distinct topics with different areas of application, there are no overlaps or conflicts among them.⁸¹⁷

Contradictions and inconsistencies between rules of the same legal system should be carefully addressed by legislators and interpreters. Fuller remarked that 'legislative carelessness about the jibe of statutes with one another can be very hurtful to legality and there is no simple rule by which to undo the damage'.⁸¹⁸

⁸¹² Brownsword, 'Two Concepts of Good Faith' (n 160) 234.

⁸¹³ There were various statutes which preceded the Consumer Protection Code and aimed to protect consumers including: Act 1521/1951 (prescribes crimes against the public economy); Statutory Instrument 4/1962 (regulates the intervention in the economic domain to ensure the distribution of indispensable products for the consumption of the population); Act 4680/1965 (regulates the advertising activity); Act 6463/1977 (makes mandatory the declaration of the total price in sales made in instalments); Public Civil Action Act (Act 7347/1985, regulates the public civil action for damages caused to the environment and consumers as well as to properties and rights of artistic, aesthetic, historical and touristic value).

⁸¹⁴ Carlos Alberto Bittar, 'Os Contratos de Adesão e o Sancionamento de Cláusulas Abusivas' (1989) São Paulo, out, v. 78, f. 648 Revista dos Tribunais 17, 17-20.

⁸¹⁵ See Act 11101/2005 (Bankruptcy Act); Decree 2044/1908 (define Bills of Exchange and Promissory Notes) and Act 6404/1976 (Business Corporation Act).

⁸¹⁶ Castello Miguel (n 256) 98-100.

⁸¹⁷ In addition their enactment enabled a more straightforward update of the law that regulates business contracts. See chapter 2.

⁸¹⁸ Fuller (n 783) 69.

5.4.2. General clauses

The Brazilian legal system adopts general concepts such as good faith, social function, public order and public interest which afford a certain degree of flexibility to courts. In the words of Martins-Costa, 'legislators left "open windows" (...) in the form of "general clauses" that can be filled by judges according to the individual case'.⁸¹⁹

However the use of general clauses still faces some resistance in England on the grounds that it may create uncertainties that can negatively affect the market.⁸²⁰ For instance, if suppliers cannot predict whether terms will be considered ineffective, they may increase prices in order to compensate for unexpected losses switching the burden to consumers.

As observed earlier in Brazil the introduction of such general clauses influenced the transition of the courts' approach from a *formalist* to a *realist* one; hence judges are no longer limited to the application of 'the letter of the law'. By comparison, English courts also adopt the realism ideology, but this results from the application of equity and the system of precedents.

5.4.3. Collective protection

Article 81 of the Brazilian Consumer Protection Code prescribes the protection of consumers' rights and interests either individually or collectively. The *collective protection* covers the so-called 'diffuse, collective and individual-homogeneous interests' of a determined or indeterminate group of consumers. Such protection can be provided by public bodies (e.g., public prosecution services, Federal Government, States, Municipalities and Federal District) as well as by relevant associations⁸²¹ through a *public civil action* in accordance with Act 7347/1985.⁸²² In addition there are other examples of

⁸¹⁹ See Judith Martins-Costa, 'O Novo Código Civil Brasileiro: em Busca da 'Ética da Situação' in J Martins-Costa and GLC Branco (eds), *Diretrizes Teóricas do Novo Código Civil Brasileiro* (Saraiva 2002) 118.

⁸²⁰ *Interfoto Picture Library Ltd v Stilleto Visual Programmes Ltd* [1989] QB 433.

⁸²¹ See art. 82 of the Consumer Protection Code. These associations must be legally constituted for at least one year and their institutional purpose must include the protection of consumer's rights and interests.

⁸²² The reciprocity between the Public Civil Action Act (Act 7347/1985) and the Consumer Protection Code can be found in articles 90 and 117 of the latter.

'collective actions' in Brazil for other purposes⁸²³ which include the *popular action* and the *collective injunction*.⁸²⁴

The Consumer Protection Code also provides in its article 6, VII that one of the basic consumers' rights is the access to judicial and administrative bodies for prevention or redress for material or moral damages of individual, *collective* or *diffuse* interests which include the protection against unfair terms.

The above provisions contain noticeable similarities with the text of article 7(2) of the Directive 93/13/EEC:

Persons or organizations, having a legitimate interest under national law in protecting consumers, may take action according to the national law concerned before the courts or before competent administrative bodies for a decision as to whether contractual terms drawn up for general use are unfair, so that they can apply appropriate and effective means to prevent the continued use of such terms.

However in England parties cannot have recourse to administrative bodies because under the Regulations only courts can decide whether or not a term is unfair.⁸²⁵ Nonetheless the provisions of the UTCCR 1999 may benefit consumers collectively as their reg. 12 provides that the Director General of the Office of Fair Trading and qualifying bodies may apply for an *injunction* against any person who appears to be using or recommending the use of unfair terms in consumer contracts. Consequently such injunction does not aim to protect an individual consumer but all consumers who could be affected by an unfair term made for general use.

The English legal system includes other examples of collective protection of consumers. For instance part 8 of the Enterprise Act 2002 enables *enforcers* to seek undertakings or enforcement orders for breach of community and domestic infringements that may harm the collective interests of consumers.⁸²⁶ More recently the Commission of the European

⁸²³ Manuela Pereira Savio, 'Ação Civil Pública e Ação Coletiva: Problema Terminológico' Páginas de Direito <<http://tex.pro.br/tex/listagem-de-artigos/179-artigos-ago-2009/5631-acao-civil-publica-e-acao-coletiva-problema-terminologico>> accessed 12 January 2011.

⁸²⁴ According to art. 5, LXXIII (Federal Constitution) and Act 4717/1965 any citizen is entitled to propose a *Popular Action* to make void an act injurious to the public property, the administrative morality, the environment and the historic and cultural heritage. On the other hand, political parties and certain entities and associations can apply for a *Collective Injunction* to protect a clear legal right if conditions of art. 5, LXX (Federal Constitution) are satisfied.

⁸²⁵ See reg. 12(3) of UTCCR.

⁸²⁶ In addition s. 47B of the Competition Act 1998 provides that a specified body may bring proceedings before the Competition Appeal Tribunal (CAT) which include consumer claims made on behalf of at least two

Communities presented a *Green Paper on Consumer Collective Redress*⁸²⁷ that proposes a mechanism to seek redress when multiple consumers are harmed by the same or a similar practice of a trader. It ultimately aims to address 'consumer mass claims' which tend to increase with the growth of cross-border transactions and online shopping.⁸²⁸

It is possible to argue that collective actions have the potential to increase significantly the consumer protection in England. Beale contended that 'individual challenges to unfair terms will always remain few because of the many obstacles to effective legal action by individual consumers (...) so we must look to supplementation of individual private remedies by public action or collective action'.⁸²⁹

5.4.4. Specialised courts

Beale suggested that perhaps cases which examine the unfairness of terms for general use in B2C contracts should be decided by *specialised courts* which would be able to build up experience and deal more efficiently with a large range of information required in those cases.⁸³⁰ However those decisions have currently been made by higher courts or county courts under reg. 12.⁸³¹

In Brazil article 5, IV of the Consumer Protection Code⁸³² stipulated the creation of small claims courts and courts specialised in consumer protection.⁸³³ In line with this provision some Brazilian States such as São Paulo and Bahia established those specialised courts; which were however subsequently closed down⁸³⁴ because 'in practice there was no

individuals. Furthermore, under rule 19.10 of the Schedule 2 of the Civil Procedure (Amendment) Rules 2000 (SI 2000/221) the so-called Group Litigation Order (GLO) permits a number of claims, which has given rise to common or related issues (of fact or law), to be managed as a group.

⁸²⁷ Commission, 'Green Paper on Consumer Collective Redress' COM (2008) 794 final.

⁸²⁸ See <http://ec.europa.eu/consumers/redress_cons/collective_redress_en.htm#Green> accessed 10 October 2011.

⁸²⁹ Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 251.

⁸³⁰ *Ibid.* 257.

⁸³¹ In the context of the present study there are decisions made by higher courts such as in *Office of Fair Trading v Abbey National plc and Others* [2009] UKSC 6, [2010] 1 AC 696, [2009] EWCA Civ 116 which clashed with the OFT's views. The Supreme Court's decision in this case is still surrounded by controversy.

⁸³² Article 5, IV provides that in order to execute the National Policy for Consumer Relations, the Government shall use as a tool the creation of Small Claims Courts and Specialised Courts to solve consumer disputes.

⁸³³ Those specialised courts differs from the small claims courts because they deal mainly with collective claims (although they can also make decisions about individual claims). See Grinover and others (n 499) 135-136.

⁸³⁴ Some Brazilian States created specialised courts via internal legislation. For instance, art. 32, I of the Declaratory Statute 762/1994 of the State of São Paulo prescribed the creation of five specialised courts to deal with consumer relations and collective actions. Those courts were closed down a few years later by the Declaratory Statute 877/2000. Similarly, the State law 6982/1996 of Bahia determined the establishment of specialised courts to decide consumer cases involving values that exceed 40 minimum wages and that were

interest or motivation to implement such courts'.⁸³⁵ This represented an enormous setback in the development of a more effective consumer protection in Brazil because those courts would be competent to deal with individual as well as collective claims. More recently other States (including Salvador, Vitória, Aracaju and Maceió) established courts specialised in diffuses and collectives' interests with a great focus on consumer protection;⁸³⁶ but there is still the need for the creation of specialised courts which tackle individual claims in this area.

5.4.5. Pre-contractual liability

In England there is no general rule which imposes liability to parties before they are actually bound by a contract. In other words parties can break off negotiations according to their convenience for the sake of freedom of contract.⁸³⁷ However there is case law which indicates a concern to offer some protection to parties at pre-contractual stage. For instance in *Blackpool and Fylde Aero Club v Blackpool BC*⁸³⁸ the Court of Appeal held that the plaintiff complied with the terms of the advertised procedure for the submission of tenders for the concession to operate pleasure flights from Blackpool airport. Consequently 'if he submits a conforming tender before the deadline he is entitled, not as a matter of mere expectation but of contractual right' to have his tender considered.⁸³⁹

Brownsword observed that in the above case 'the court followed the line taken in a number of other jurisdictions that the law of contract is capable of giving some protection to the interests of commercial parties who are working towards an exchange';⁸⁴⁰ but the English contract law lacks express provisions which purport to protect parties at the negotiation stage.

By comparison, as seen previously, in Brazil legal literature extended the application of the principle of good faith to negotiations and the Superior Tribunal of Justice recognised

outside the scope of the small claim courts. However, they were also subsequently closed down by the Resolution 18/2008 (Supreme Court of the State).

⁸³⁵ Figueiredo and Figueiredo (n 272) 294.

⁸³⁶ Grinover and others (n 34) 135-136. In addition to consumer protection other *collective interests* include environment and properties and rights of artistic, aesthetic, historical and touristic value in accordance with Act 7347/1985.

⁸³⁷ See *Walford v Miles* [1992] 2 AC 128.

⁸³⁸ [1990] 1 WLR 1195 (CA).

⁸³⁹ *Blackpool and Fylde Aero Club v Blackpool BC* [1990] 1 WLR 1195 (CA), 1202.

⁸⁴⁰ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 145.

that parties must not act in bad faith at this stage.⁸⁴¹ In addition it is possible to argue that the pre-contractual liability is implicitly recognised in the provision that prescribes extra-contractual liability for damages caused by voluntary act or omission.⁸⁴²

5.4.6. Absence of a small business regime

As discussed in chapter 4, neither the English nor the Brazilian legal system currently offer a special regime to protect small businesses against abusive clauses in their contractual dealings. The lack of statutory protection has left those businesses in a disadvantageous position in the face of larger businesses as the latter often take advantage of their stronger bargaining power to include provisions that benefit them unilaterally.

For this reason the general protection available to businesses in B2B contracts is insufficient to protect the interests of SMEs; thus the inexistence of a special regime for small businesses is a major issue that should be addressed by both jurisdictions. While the Law Commission has already recommended the implementation of such regime to protect SMEs against unfair terms, in Brazil there is no indication of any proposals for similar provisions.

5.5. Conclusion

Although the legislation which tackles unfair terms in England and Brazil is not perfect, it still represents a major development towards a more comprehensive protection of the weaker party. It also demonstrates a concern of both countries over the imbalance of contractual relations which can give rise to abuses, in particular in contracts involving consumers.

However notwithstanding the increasing control over unfair terms or abusive clauses in the above jurisdictions, 'organisations continue to find it difficult to resist using what to them are conventional standard terms in order to protect their own position'.⁸⁴³ Businesses benefit from the fact that most consumers or their weaker counterparties (e.g., SMEs) are usually not aware of their rights and only few of them may attempt to

⁸⁴¹ REsp 49564/SP (24/04/2007).

⁸⁴² Article 186 of the Civil Code. Interpreters can also apply general rules of civil liability prescribed by articles 389 and 927 of the Civil Code. See chapter 3.

⁸⁴³ Bray and Pickford (n 352) 30.

negotiate better terms or recourse to courts. This justifies the risk assumed by sellers and suppliers of including unjust terms that aim to reduce costs and/or increase profits even if they may be declared ineffective afterwards.⁸⁴⁴

Such lack of awareness regarding contractual rights will not be solved only by the proposal of new legislation or by amendments to the current one, but it may also require the introduction of new government's policies⁸⁴⁵ and campaigns to increase the consciousness of the population about their rights as consumers.⁸⁴⁶ Nonetheless the enactment of a clearer and user-friendlier legislation would be invaluable to enhance the comprehension by consumers and vulnerable parties of the available mechanisms to protect their interests.

English law is already looking for possible solutions to discrepancies within its internal legislation such as the unified regime for the control on unfair terms proposed by the Law Commission. The European Union has also shown a concern over the need to review its *consumer acquis* and European contract law. More recently the EU's Council of Ministers approved the adoption of the *Directive on Consumer Rights* (2011/83/EU) which aims to simplify and update 'the applicable rules, removing inconsistencies and closing unwanted gaps in the rules'.⁸⁴⁷

Equally in Brazil the adoption of codes purports to organise rules of a certain area (e.g., consumer protection) in a systematic way in order to facilitate their understanding and application. In addition, there are mechanisms to prevent and overcome apparent conflicts of law which enable interpreters to choose the most appropriate provision for an individual case.

However it is not only the difficulties to understand and apply the legal provisions that have discouraged parties from recourse to the law. Many consumers and SMEs have been

⁸⁴⁴ Beale observed that 'businesses continue to use even terms that are automatically invalid under the Unfair Contract Terms Act (...) presumably in the hope that the presence of the clause will deter consumers from seeking redress'. See Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333) 254.

⁸⁴⁵ The Department for Business, Innovation and Skills (BIS) is a government department of the UK which team of ministers includes the Minister for Employment Relations, Consumer and Postal Affairs who is responsible for consumer policies and consumer affairs.

⁸⁴⁶ In Brazil, Act 10504/2002 institutes the 'National Day of the Consumer' which is celebrated every 15th March and includes debates, lectures and other events that aim to disseminate consumers' awareness of their rights.

⁸⁴⁷ See Recital 2 of the *Directive on Consumer Rights* (2011/83/EU). This Directive will be implemented in England by the *Consumer Bill of Rights*

driven away from courts due to high costs and long delays of legal procedures.⁸⁴⁸ In other words the time and money spent in a legal action may not be deemed worthwhile in relation to the benefits that consumers may derive from it and there is also the risk of an unfavourable result.⁸⁴⁹

In an attempt to minimise such problems, both legislatures have prescribed alternative ways to deal with claims which involve low values which are simpler, faster and more cost-effective. In Brazil, the *Small Claims Courts Act* (Act 9099/1995) allows consumers to propose legal action against companies without the need of technical assistance (i.e., lawyers) when the value of the cause does not exceed the equivalent of 20 minimum wages.⁸⁵⁰ Article 2 of the same Act provides that the proceeding of these courts 'will be guided by the criteria of orality, simplicity, informality, procedural economy and swiftness seeking where possible, a conciliation or deal'. Additionally article 6 of Act 10259/2001 prescribes that in addition to natural persons, micro and small enterprises can also have recourse to federal small claims courts.⁸⁵¹

Similarly in England, consumers and small businesses may resort to county courts that have a simplified proceeding to tackle small claims which include cases of goods not supplied and faulty goods.⁸⁵² There are also alternative ways to settle disputes such as arbitration, mediation and ombudsmen schemes which are called 'Alternative Dispute

⁸⁴⁸ Junqueira de Azevedo contended that law has been developed through changes of paradigms. In the context of law the first paradigm was developed in the *liberal state*. It was entirely based on the law and on its security. The law was considered universal, general and complete; therefore judges were limited to repeat the legislation. In the *social state*, this paradigm was replaced by a system in which the *pivot* was the judge not the law. The legislation gave more freedom to judges to make their decisions through the adoption of indeterminate legal concepts and general clauses, such as good faith, social function, public order and public interest. However this paradigma may create too much uncertainty. Consequently nowadays there has been a shift to a new paradigm (called *post-modern*) that is the avoidance of courts. Parties have recourse to alternative ways to deal with conflicts, such as arbitration, due to high costs and delays of judicial proceedings. See Junqueira de Azevedo, 'Insuficiências, Deficiências e Desatualização do Projeto de Código Civil na Questão da Boa-Fé Objetiva nos Contratos' (n 801) 16 and Castello Miguel (n 256) 88-89. Kuhn defines 'paradigms' as 'universally recognized scientific achievements that for a time provide model problems and solutions to a community of practitioners'. According to this author 'Sciences have developed through changes of paradigms'. See Thomas S. Kuhn, *The Structure of Scientific Revolutions* (2nd edn, University of Chicago Press 1970) vii.

⁸⁴⁹ Lewis (n 323) 93.

⁸⁵⁰ See article 9 of Act 9099/1995. Currently the minimum wages in Brazil is R\$622; therefore 20 minimum wages is R\$12,440 that is approximately £3,920.

⁸⁵¹ Federal small claims courts are competent to judge cases involving values up to 60 minimum wages (approximately £11,760) or minor offences which have as defendant the Union, the federal governmental agencies, foundations or public companies.

⁸⁵² For claims up to £5,000 (£1,000 for personal injury and disrepair claims). See Part 27 ('the small claims track') of the Civil Procedure Rules 1998.

Resolution' (ADR) schemes. They enable parties to avoid courts and opt for a more flexible, faster and less costly proceeding.⁸⁵³

In summary the implementation of a more effective protection of consumers and weak parties will not depend solely on the identification and solution of problems of the current legislation. The awareness of parties about their rights is also essential to enable them to act against abuses and achieve practical results. Moreover legislatures should provide effective means to parties to ensure recourse to legal proceedings⁸⁵⁴ otherwise the legislation, no matter how perfect it is, may lose its meaning and purpose.

⁸⁵³ The European Commission is currently preparing a legislative proposal to promote *Alternative Dispute Resolution* (ADR) schemes in the EU, including 'the possible development of an EU-wide online dispute resolution system for e-commerce transactions covering both B2B and B2C situations'. See Commission, 'Review of the "Small Business Act" for Europe' COM (2011) 78 final 12.

⁸⁵⁴ Undoubtedly small claim courts and alternative means of redress have facilitated the access to courts, but such special proceedings are limited to claims that involve small amounts of money or specific situations. This leaves a high number of consumers and vulnerable parties depending on ordinary judicial proceedings that can be expensive and slow. Collective actions have a great potential to enhance the protection of parties who would not have adequate means to propose individual actions.

CHAPTER 6. COMPARATIVE EVALUATION OF THE LEGISLATIVE CONTROLS ON UNFAIRNESS IN B2B AND B2C CONTRACTS IN ENGLAND AND BRAZIL

6.1. Context

Traditionally comparatists have been interested in the study of western legal traditions, particularly in differences and similarities between common law and civil law systems.⁸⁵⁵ The present study adopted this archetype as it involved the comparison between the English and the Brazilian legal systems, representing the above legal traditions. The popularity of the comparison of those legal systems may result from the fact that they are among the most widespread and influential in the world.⁸⁵⁶

According to David the considerable expansion of common law and civil law throughout the globe was due to *reception* or *colonisation*.⁸⁵⁷ England gave origin to *common law* and disseminated it to its colonies. This legal system 'tends to be case-centred and hence judge-centred, allowing scope for a discretionary, *ad hoc*, pragmatic approach to the particular problems that appear before the courts';⁸⁵⁸ whereas the *civil law* derived from Roman law 'tends to be a codified body of general abstract principles which control the exercise of judicial discretion'.⁸⁵⁹ Brazil inherited the civil law system from its time as a Portuguese colony. Since then the Brazilian legislation has been influenced by the European continental system of law which in particular has shaped its private law.

As discussed in chapter 1, while England can be unquestionably adopted as a paradigm for a common law system in a comparative study; more traditional comparatists may contend that the Brazilian law is not suitable to represent a civil law system. Instead they would prefer to employ 'mature legal systems' such as France or Italy in the comparison.⁸⁶⁰ Nonetheless the peculiarity of the Brazilian legal system may be seemed as an advantage rather than a negative characteristic. Örüçü observed that the future of comparative law consists in the 'appreciation of diversity'; thus it is precisely on the

⁸⁵⁵ Örüçü, 'Comparatists and Extraordinary Places' (n 55) 467.

⁸⁵⁶ David and Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (n 16) 27.

⁸⁵⁷ David observed that in some countries which were not colonised there was a voluntary reception of the civil law and common law (e.g., some Muslim countries). See *Ibid.* 23-25.

⁸⁵⁸ Slapper and Kelly (n 20) 5.

⁸⁵⁹ *Ibid.*

⁸⁶⁰ Zweigert and Kötz (n 48) 41.

'extraordinary' nature of the Brazilian law where the importance of this comparison lies.⁸⁶¹ Furthermore Baxter and Ong maintained that 'the wealth of creative ideas flowing from both the new and the developing worlds can at times be astonishing in its fecundity'.⁸⁶²

The relevance of this study therefore is based on the examination of two distinct legal systems, which can provide unique insights about their rules. This comparison did not only identify the differences between them, but also highlighted their similarities.⁸⁶³ In fact this study also observed the existence of overlaps between the relevant law of England and Brazil.

In England case law was the main source of law for centuries, but nowadays statutes (Acts of Parliament) are 'the most important source of law, in the sense that they prevail over most of the other sources'.⁸⁶⁴ For instance the problem of contractual unfairness is addressed by pieces of legislation such as the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contracts Regulations 1999; although they do not lessen the importance of judicial precedents as it can be observed from cases such as *Director General of Fair Trading v First National Bank plc*⁸⁶⁵ and *Office of Fair Trading v Abbey National plc and Others*.⁸⁶⁶

By comparison although the main Brazilian legal sources are statutes and Codes, courts have adopted a more flexible approach to protect vulnerable parties. In Brazil much of the control on unfairness in the context of small businesses contracts has been made through the analogical application of the consumer protection by courts in the absence of statutory provisions.⁸⁶⁷ In addition more recently the *binding judicial precedent* was introduced into the Brazilian legal system prescribing that decisions made by the Supreme Federal Court bind lower courts and public administration.⁸⁶⁸ This provision was subject to

⁸⁶¹ Özücü, 'Comparatists and Extraordinary Places' (n 55) 470.

⁸⁶² See Baxter and Ong (n 56) 89.

⁸⁶³ David observed that due to the numerous contacts over the centuries among countries which adopt common law and civil law the differences between those legal traditions have diminished. David and Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (n 16) 25.

⁸⁶⁴ Catherine Elliott and Frances Quinn, *English Legal System* (10th edn, Longman 2009) 9. David observed that 'the formulation of the legal rules tends more and more to be conceived in Common law countries as it is in the countries of the Romano-Germanic family'. See David and Brierley, *Major Legal Systems in the World Today: An Introduction to the Comparative Study of Law* (n 16) 25.

⁸⁶⁵ [2001] UKHL 52, [2002] 1 AC 481.

⁸⁶⁶ [2009] UKSC 6, [2010] 1 AC 696, [2009] EWCA Civ 116.

⁸⁶⁷ See chapter 4.

⁸⁶⁸ This binding judicial precedent ('súmula vinculante') was introduced by the Constitutional Amendment 45 in 2004, which added the article 103-A to the Brazilian Federal Constitution and provides that the Supreme Federal Court may, *ex officio* or by provocation, by decision of two thirds of its members, following repeated

criticism because it gave law-making powers to the Judiciary which is an attribution that should be restricted to the legislature according to the 'principle of the separation of powers';⁸⁶⁹ but notwithstanding its application the statutory law still prevails in Brazil.

From the analysis of the above considerations it is possible to argue that the different emphases that the above legal systems give to case law and statutes represent one of the main differences between them. Nevertheless legislation and judicial precedents are entwined in practice: the latter are the result of the interpretation of the former by courts and courts may create law through this interpretative process. Therefore despite formal distinctions between both legal systems, they may have similar practical implications.

Although in civil law jurisdictions courts do not 'deliberately set out to create law';⁸⁷⁰ 'prior judicial opinions' have a '*persuasive effect*' over future decisions even though they are still relegated as an ancillary source of law.⁸⁷¹ For instance the Brazilian Superior Tribunal of Justice has published numerous 'judicial precedents' that summarise its prevailing understanding on specific topics which interpretation has already been laid down.⁸⁷² Although not binding, they serve as a guide to parties and judges of lower courts on how certain cases will be interpreted by this higher court.⁸⁷³ The Supreme Federal Court on the other hand can publish 'binding judicial precedents', as seen above, despite the inconsistency of the latter with the civilian tradition; but so far this court has not published any binding precedent concerning unfairness in contracts.⁸⁷⁴

By comparison, common law courts apply the law to the facts through interpretation and create law 'by making legal principles which courts lower down the hierarchy are bound to

decisions on constitutional matters, approve *binding judicial precedent* which, from its publication in the official press, will have *binding effect* on other bodies of the Judiciary and on the direct and indirect public Administration at federal, state and municipal level. This court can also revise or cancel *binding judicial precedents* as prescribed by law. See also Act 11417/06 which regulates article 103-A.

⁸⁶⁹ According to the 'principle of separation of powers' the three branches of the government (Legislative, Executive and Judicial) are independent and each power should be limited to its own competences and prerogatives. See Moraes (n 134) 187. According to Scalia when judges apply the common law method of judging they inappropriately usurp the power that should belong to legislators. See Antonin Scalia, 'Common Law Courts in a Civil-Law System: The Role of United States Federal Courts in Interpreting the Constitution and Laws' (The Tanner Lectures on Human Values 1995) 86.

⁸⁷⁰ Tamanaha (n 113) 190.

⁸⁷¹ Scalia (n 869) 83.

⁸⁷² In 2012 there were almost 500 precedents published by the Superior Court of Justice. See <http://www.stj.jus.br/SCON/sumulas/toc.jsp?livre=@docn&tipo_visualizacao=RESUMO&menu=SIM> accessed 05 September 2012.

⁸⁷³ E.g., precedent 302 of this Court prescribes that a term of a health insurance contract is unfair when it limits the hospitalisation time of the insured and precedent 469 prescribes that the Consumer Protection Code is applicable to health insurance contracts.

⁸⁷⁴ See <<http://www.stf.jus.br/portal/cms/verTexto.asp?servico=jurisprudenciaSumulaVinculante>> accessed 06 August 2012.

follow'.⁸⁷⁵ Judicial decisions therefore are regarded as a significant source of law for this legal system.⁸⁷⁶ In the context of the present study however, English courts were limited to the examination of the scope of application of the relevant law; thus they did not create principles to govern the matter of unfairness.⁸⁷⁷

6.1.1. Comparing the approaches of the Brazilian law and the English law towards the controls on unfairness in B2B and B2C contracts

The different approaches of the Brazilian law and the English law towards the controls on unfairness in contracts reflect the differences between the hierarchies of legal values of their respective legal systems.⁸⁷⁸ For instance they attach distinct weights to values such as freedom of contract and good faith.

In the context of business contracts, common law courts are mainly concerned to protect the freedom of contract of the parties and to ensure the enforcement of terms which were freely agreed in order to promote certainty of contractual relations.⁸⁷⁹ There is the prevalence of the *market-individualism* ideology and parties are expected to defend their own interests. English judges should only 'correct or integrate' contractual terms if 'specific statutory rules require them to do so'.⁸⁸⁰ Those legislative interferences are however more usual in the context of B2C contracts.

On the other hand in Brazil the freedom of contract is limited by principles such as the social function of the contracts and good faith which also cover agreements between businesses.⁸⁸¹ In fact this limitation to the freedom of contract by the social function of the contracts can only be found in the Civil Code of Brazil.⁸⁸² Furthermore civilian judges in general 'have a larger power to evaluate the fairness of the contract and intervene to

⁸⁷⁵ Ewan MacIntyre, *Business Law* (5th edn, Longman 2010) 9.

⁸⁷⁶ Scalia observed that 'an absolute prerequisite to common-law lawmaking is the doctrine of *stare decisis* - that is, the principle that a decision made in one case will be followed in the next. Quite obviously, without such a principle common-law courts would not be making any "law"; they would just be resolving the particular dispute before them.' See Scalia (n 869) 83.

⁸⁷⁷ See *Smith v Eric S. Bush* [1990] 1 AC 831 and *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 AC 481.

⁸⁷⁸ Moura Vicente (n 290) 35.

⁸⁷⁹ Moss (n 221) 68.

⁸⁸⁰ *Ibid.* 68-69.

⁸⁸¹ See article 421 of the Civil Code.

⁸⁸² Tartuce (n 263) 244.

reinstate the balance of interests between the parties because they are guided by principles such as good faith.⁸⁸³

To a certain degree the legal values of both legal systems converge in the context of B2C contracts. They are both in line with the *consumer welfarism* ideology as they regulate more attentively consumer contracts to prevent abuses of the consumer's vulnerability in the marketplace. This position can be inferred from the analysis of pieces of legislation such as the UTCCR 1999 and the Brazilian Consumer Protection Code. However despite fundamental similarities between the English and Brazilian legislation which regulates B2C contracts, they still have differences that reflect the distinctions between their legal families. One of the main differences is the treatment given to the concept of good faith. Whilst it is regarded as a general principle in the Brazilian law its application is more restricted in English law, as will be examined later in this chapter.

The present comparison so far aimed to provide an insight as to how the above legal systems address the problem of unfairness in B2B and B2C contracts and to allow an understanding of the reasons underpinning their similarities and differences. From this point the analysis will evaluate possible lessons that one system can learn from the other.⁸⁸⁴

6.2. Evaluation of lessons that Brazilian law can learn from the English legislative controls on unfairness in business and consumer contracts

Brazil adopts the civil law tradition which considers Codes one of its primary sources of law. As Codes are 'authoritative, comprehensive and systematic collection of general clauses and legal principles' judges should be confined to the application of their provisions,⁸⁸⁵ for this reason one could argue that the Brazilian legal system adopts a more *formalist* approach. According to the formalism ideology courts should follow uncritically the rule-book which is deemed a 'closed logical system' where there is no room for judicial discretion.⁸⁸⁶ In line with that, formalists judges:

⁸⁸³ Moss (n 221) 68-69. See article 422 of the Civil Code.

⁸⁸⁴ According to Collins one of the objectives of comparative contract law is the identification of the best solutions to legal problems and the recommendation of their inclusion into the other jurisdiction. See Hugh Collins, 'Methods and Aims of Comparative Contract Law' (1991) 11(3) OJLS 396, 396-399.

⁸⁸⁵ De Cruz (n 10) 46-48.

⁸⁸⁶ Brownsword and Adams, *Understanding Contract Law* (n 127) 188-189.

[D]o not legislate, do not exercise discretion (...), have no truck with policy, and do not look outside conventional legal texts - mainly statutes, constitutional provisions, and precedents (authoritative judicial decisions) - for guidance in deciding new cases.⁸⁸⁷

As seen in chapter 5, the introduction of general clauses in the Brazilian legal system, such as the principle of good faith, required a change of posture by courts from a *formalist* approach to what Amaral Junior called a *teleological* or *finalist* approach.⁸⁸⁸ The latter may be equated to the *realist* approach as both contend that judges should not be limited to a mechanical application of the rule to the fact, but instead they should consider the purposes and goals of the rule. In other words, courts should be more 'result-orientated' than 'rule-orientated'.⁸⁸⁹ The principle of the social function of the contracts in Brazil is a clear example of the adoption of this approach. This principle prescribes that contracts should be interpreted according to 'the conceptions of the social milieu in which they are inserted' and should ensure the balance between parties preventing unjust situations.⁸⁹⁰

This 'result-orientated' attitude requires a higher level of judicial discretion which used to be atypical to civil traditions. For this reason according to Amaral Junior, Brazilian courts could learn from common law countries where this approach is widely disseminated.⁸⁹¹ In England 'most modern judges tend to adopt a realist approach'⁸⁹² and they may bend the rules in favour of fairer decisions because differently from formalist judges, realist judges 'must act as custodians of practical justice and convenience, not simply as the keepers of the code'.⁸⁹³

For instance in England courts can apply remedies in equity which are discretionary and based on maxims that purport to ensure that decisions are 'morally fair',⁸⁹⁴ such as 'he who comes to equity must come with clean hands'.⁸⁹⁵ Therefore in spite of a considerable

⁸⁸⁷ Tamanaha (n 113) 181.

⁸⁸⁸ Amaral Júnior (n 888) 32.

⁸⁸⁹ Brownsword and Adams, *Understanding Contract Law* (n 127) 190.

⁸⁹⁰ Tartuce (n 263) 239-240. In the words of article 2035, sole paragraph of the Civil Code: 'no agreement shall prevail if it is contrary to rules of public order, such as those established by this Code to ensure the social function of the property and contracts'. See Rose (n 251) 433.

⁸⁹¹ Amaral Júnior (n 888) 32.

⁸⁹² Poole, *Textbook on Contract Law* (n 78) 10.

⁸⁹³ Brownsword and Adams, *Understanding Contract Law* (n 886) 191.

⁸⁹⁴ Elliott and Quinn (n 864) 118. Waddams observed that 'courts of equity had often set aside contracts on a variety of grounds related (in general terms) to unfairness'. See Waddams (n 718) 26.

⁸⁹⁵ *D&C Builders Ltd v Rees* [1966] 2 QB 617 (CA).

increase in the importance of statute law in England in the twentieth and twenty-first centuries,⁸⁹⁶ English courts still make decisions based on equity.⁸⁹⁷

Nonetheless this does not mean that decisions made by judges in common law are completely discretionary. Tamanaha observed that even in decisions involving open provisions such as fairness and reasonableness, judges 'will often agree in their judgments because they have undergone a similar training in the legal tradition and its values, and many share social views that span other differences'.⁸⁹⁸ Furthermore according to the doctrine of judicial precedent 'courts are bound to follow decisions of higher courts and, usually, previous decisions of their own' which also provides consistency in their rulings.⁸⁹⁹

The English system of precedents also has other advantages. It may be particularly beneficial in the context of B2B contracts as it 'allows for excellent updating of the law in a way which can keep up with changing business trends'.⁹⁰⁰ Consequently this system may regulate business contracts more adequately than Codes and statutes typical of the civil law as the latter require a complex and often slow process to be modified which may not meet the needs of a changing market.⁹⁰¹

6.3. Evaluation of lessons that English law can learn from the Brazilian legislative controls on unfairness in business and consumer contracts

As mentioned earlier although case law is still an integral part of the English legal system, currently its main source of law is *statutes* just like Brazil. However Steyn noted that 'in the matter of high technique the jurisprudence [and statute law] of common law and civil law countries sharply differ' and that at the heart of the differences is the 'generality of legal rules'.⁹⁰² Whereas statutes in England purport to provide 'detailed and concrete regulation', the legislation of civil law countries tend to state 'broad principles'.⁹⁰³ Indeed general principles, such as good faith, play an important role in the Brazilian legal system.

⁸⁹⁶ Slapper and Kelly (n 20) 7.

⁸⁹⁷ Following the Judicature Acts of 1873–75 courts can apply common law and equity rules; in fact 'now both systems have been effectively subsumed under the one term: common law'. See Ibid. 6-7.

⁸⁹⁸ Tamanaha (n 113) 192.

⁸⁹⁹ Routledge (ed), *English Legal System Lawcards 2010-2011* (7th edn, Routledge 2010) 25.

⁹⁰⁰ MacIntyre (n 875) 27.

⁹⁰¹ Ibid.

⁹⁰² Johan Steyn, 'The Role of Good Faith and Fair Dealing in Contract Law: A Hair-Shirt Philosophy' (1991) 6 Denning LJ 131, 131.

⁹⁰³ Ibid.

In line with Steyn J's observation, in *Interfoto Picture Library Ltd v Stilleto Visual Programmes Ltd*⁹⁰⁴ Bingham LJ noted that:

In many civil law systems, and perhaps in most legal systems outside the common law world, the law of obligations recognises and enforces an overriding principle that in making and carrying out contracts parties should act in good faith (...) English law has, characteristically, committed itself to no such overriding principle but has developed piecemeal solutions in response to demonstrated problems of unfairness.

In other words English law did not adopt a general principle of good faith as civil law jurisdictions did; instead it developed its own controls on unfairness that have similar outcomes.⁹⁰⁵ According to this *neutral* approach there is no need to rewrite the English doctrine as either the latter is equivalent to a broad principle of good faith or there is no practical difference between the application of those piecemeal solutions and such a general clause.⁹⁰⁶

Nonetheless Brownsword contended that if the outcomes are equivalent, then the adoption of good faith as an overriding principle by English law would be preferable because it would enable a 'doctrine harmonisation' with other European legal systems.⁹⁰⁷ Furthermore the scope of this principle is wider than the English solutions.

Although there are statutory controls in England over unfairness, such as UCTA and UTCCR 1999, they are limited to certain types of terms (e.g., exemption clauses, non-negotiated terms) and are applicable mainly to consumer contracts. A general principle of good faith in its turn may be applied to B2B and B2C contracts and covers terms in general. Furthermore this principle can be extended to protect parties at the negotiation stage in a way which operates differently from the English approach which rejects the application of a general rule of pre-contractual liability.⁹⁰⁸

⁹⁰⁴ [1989] QB 433, 439.

⁹⁰⁵ Chen-Wishart observed that other common law jurisdictions (e.g., Australia and the USA) 'developed a general principle against unfairness in contract formation' 'under the banner of unconscionability' and civilian jurisdictions 'under the banner of good faith', but 'this has been resisted by English courts'. See Chen-Wishart (n 3) 400.

⁹⁰⁶ Brownsword, 'Individualism, Cooperativism and an Ethic for European Contract Law' (n 81) 629. See also Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 120.

⁹⁰⁷ Brownsword, 'Individualism, Cooperativism and an Ethic for European Contract Law' (n 81) 629.

⁹⁰⁸ See *Walford v Miles* [1992] 2 AC 128. See also Carter and Furmston, 'Good Faith and Fairness in the Negotiation of Contracts Part II' (n 224) 117-118.

Good faith may also comprise secondary duties such as *transparency* and *information* which in Brazil imply that sellers and suppliers are prohibited from omitting information about the products or services when doing so they may mislead the consumer;⁹⁰⁹ whereas the English legal system did not recognise a 'duty of disclosure for a party who knows that the other party is ignorant of a critical fact'.⁹¹⁰ Therefore such duty to inform could have allowed a fairer solution in cases such as *L'Estrange v F Graucob Ltd.*⁹¹¹ In this case an exemption clause was included in an order form which was written in small print in a poor quality paper. The buyer did not read the document, but because she signed it, the High Court held that she was bound by its terms in the absence of fraud or misrepresentation due to the 'primacy of signature'.⁹¹²

It is noteworthy that this decision would have been different following the enactment of the Unfair Contract Terms Act 1977. Under s. 6(3) the above clause could have been deemed unenforceable because the liability for breach of the implied term that goods are fit for purpose 'can be excluded or restricted' as 'against *a person dealing otherwise than as consumer*' only if the exemption clause satisfies the requirement of reasonableness.⁹¹³ In addition Schedule 2(c) of the same Act stipulates that the assessment of such reasonableness should take into account 'whether the customer knew or ought reasonably to have known of the existence and extent of the term'.

Nevertheless the application of the above piecemeal solution is still not as straightforward as the application of good faith. Moreover it may not protect adequately a small business because the latter will be generally regarded as 'a person dealing otherwise than as consumer'; hence the standards of reasonableness may not take into consideration its vulnerable position. In the Brazilian context as the buyer was a small business, courts could have protected her through the analogical application of the consumer protection rules according to which in order to be valid, terms of standard form contracts shall be drafted in plain and legible font.⁹¹⁴ Moreover clauses that imply a limitation on consumer rights should be highlighted to draw the consumer attention to their significance to ensure

⁹⁰⁹ See Nobre Júnior, 'A Proteção Contratual no Código do Consumidor e o Âmbito de sua Aplicação' (n 469) 282. See also See REsp 586316/MG (19/03/2009) and articles 31 and 46 of the Consumer Protection Code.

⁹¹⁰ Ole Lando, 'Is Good Faith an Over-Arching General Clause in the Principles of European Contract Law?' (2007) 15(6) ERCL 841, 850. Similarly Cockburn CJ contended in *Smith v Hughes* that 'the question is not what a man of scrupulous morality or nice honour would do under such circumstances (...) there was plainly no legal obligation in the plaintiff in the first instance to state whether the oats were new or old.' *Smith v Hughes* (1871) L.R. 6 QB 597, 603-604.

⁹¹¹ [1934] 2 KB 394.

⁹¹² *L'Estrange v F Graucob Ltd* [1934] 2 KB 394, 403.

⁹¹³ Poole, *Casebook on Contract Law* (n 150) 204.

⁹¹⁴ Article 54, paragraph 3 of the Consumer Protection Code.

that the consumer or the vulnerable party will make an informed decision aware of all possible consequences.⁹¹⁵

A similar protection is available to consumers in England, but currently such protection is not extended to small businesses. For instance under reg. 7(1) 'a seller or supplier shall ensure that any written term of a contract is expressed in plain, intelligible language'. In addition more recently reg. 6(1) of the 'Consumer Protection from Unfair Trading Regulations 2008' (CPRs) prescribes that a commercial practice is a *misleading omission* if it 'omits or hide material information; provides material information in a manner which is unclear, unintelligible, ambiguous or untimely' and as a result 'it causes or is likely to cause the average consumer to take a transactional decision he would not have taken otherwise'.⁹¹⁶

One of the reasons why English courts reject the application of general clauses (such as good faith) in B2B contracts is because the adoption of vague concepts may threaten the certainty of commercial relationships.⁹¹⁷ For this reason in *Union Eagle Ltd v Golden Achievement Ltd*⁹¹⁸ the Privy Council dismissed the specific performance of an agreement concerning the sale of a flat in Hong Kong in which the buyer was only ten minutes late in tendering the purchase price. Lord Hoffman contended that the non-enforcement of the contract 'on the ground that this would be "unconscionable" is sufficient to create uncertainty' in a rising and volatile market.⁹¹⁹

By comparison in Brazil the application of good faith as an overarching principle could have led to a different outcome in this case. In line with this legal system as the buyer was trying to complete the contract according to the agreed terms, the vendor would not be allowed to rescind the agreement and forfeit the deposit based on such insignificant

⁹¹⁵ Article 54, paragraph 4 of the Consumer Protection Code.

⁹¹⁶ In March 2012 the Law Commission published a *Report on Consumer Redress for Misleading and Aggressive Practices* and recommended a limited reform to the CPRs according to which 'traders should not be liable for omissions as a specific category, but should be liable where the overall presentation of a product or service would be likely to mislead the average consumer'. See Law Commission, *Consumer Redress for Misleading and Aggressive Practices* (Law Com No 332, 2012) para 7.36.

⁹¹⁷ See Lando (n 910) 848.

⁹¹⁸ [1997] AC 514.

⁹¹⁹ Nonetheless Lord Hoffman added that 'the same need for certainty is not present in all transactions and the difficult cases have involved attempts to define the jurisdiction in a way which will enable justice to be done in appropriate cases without destabilising normal commercial relationships.' See *Union Eagle Ltd v Golden Achievement Ltd* [1997] AC 514, 519.

delay as he would be acting against good faith.⁹²⁰ It is unlikely that a delay of ten minutes would harm the interests of the vendor in the context of the sale of a property.⁹²¹ In addition, the buyer would be protected by the principle of the social function of contracts according to which the fulfilment of the agreement's purpose would be more important than the strict interpretation of the terms.⁹²²

In another case, *Arcos Ltd v EA Ronaasen & Son*,⁹²³ a buyer who made a bad bargain could reject timbers which were perfectly fit for their purpose only because they were slightly thicker than the description.⁹²⁴ In Brazil the buyer would not be allowed to take advantage of the situation because the interpretation of the contract should be done 'in conformity with good faith'.⁹²⁵ Therefore as the supplier fulfilled his side of the bargain, the buyer's attitude would be deemed as bad faith; thus the latter would not be entitled to reject the goods.

A more concrete example on how good faith may be efficiently applied to prevent unfair outcomes in a B2B contract can be found in the comparison between *Baird Textile Holdings Limited v Marks & Spencer Plc*⁹²⁶ and the Brazilian 'case of tomatoes'. As seen in chapter 4, in this Brazilian case a large company (Cica) used to purchase the tomatoes cultivated by small producers. However with no reasonable notice it decided to stop buying the farmer's crops which caused the loss of the production. The local court considered that Cica was in breach of a duty of good faith and ordered it to pay damages to the farmers.⁹²⁷

By comparison in the *Baird Textile* case a retailer company (M&S) cancelled a supply arrangement made with a textile company which was ongoing for thirty years. As a result the latter sought damages on the basis that there was an implied contractual obligation that parties were dealing in good faith and that such arrangement would only be

⁹²⁰ The high value of the deposit H.K.\$420,000 (approximately £34,500) may indicate a non-honourable reason to terminate the contract. Additionally the Civil Code prescribes that juridical transactions shall be interpreted in conformity with good faith. See articles 112 and 113 of the Civil Code.

⁹²¹ Although the scenario would be different, for instance, in the sale of shares where each minute is crucial.

⁹²² Tartuce (n 263). See also articles 240 and 421 of the Civil Code.

⁹²³ [1933] AC 470 (HL).

⁹²⁴ Atkin LJ observed that 'the right view is that the conditions of the contract must be strictly performed. If a condition is not performed the buyer has a right to reject'. *Arcos Ltd v EA Ronaasen & Son* [1933] AC 470 (HL), 480. See also Lando (n 910) 850. As Poole observed this case dealt with a 'strict contractual obligation', thus even an insignificant failure of performance of the obligation may imply a breach of contract. See Poole, *Textbook on Contract Law* (n 78) 281.

⁹²⁵ Articles 112 and 421 of the Civil Code.

⁹²⁶ [2001] EWCA Civ 274.

⁹²⁷ See TJ/RS, Embargos Infringentes 591083357, Rel. Des. Adalberto Libório Barros (01/11/1991).

terminated upon a reasonable notice of three years.⁹²⁸ The Court of Appeal however rejected the above argument and Mance LJ observed that in English law there is a 'general refusal' to recognise the duty of good faith as an implied contractual term;⁹²⁹ differently from the Brazilian law where an *implied* general clause of good faith can be inferred from articles 4, III and 51, XV of the Consumer Protection Code as seen in chapter 3.

In addition the fact that there was not an express contract between the parties aggravated the uncertainty of the terms.⁹³⁰ Although in the Brazilian 'case of tomatoes' an express contract was also absent, the principle of good faith is applicable as a general clause at the pre-contractual stage and there is also the provision of extra-contractual liability⁹³¹ which allow judges to protect vulnerable parties in this situation.

Those examples indicate that piecemeal solutions in England may not tackle unfairness as efficiently as countries that adopt good faith as an overriding principle. Moura Vicente noted that 'the protection afforded to parties by English law during the negotiation and formation of the contracts is far inferior to the protection provided by the legislation of Portugal, Italy, Germany and now also of Brazil', due to the absence of good faith as a general clause in contracts in England.⁹³² Nonetheless an English lawyer may disagree with such point of view and contend that solutions which favour the certainty of commercial agreements should prevail over the application of this principle.⁹³³

Another disadvantage of the non-adoption of good faith as an overarching clause is the discrepancy that it may create between the law of England and other EU Member States. For instance article 1:201(1) of *Principles of European Contract Law* (PECL), article 1:103 of the *Draft Common Frame of Reference* (DCFR) and article 2(1) of the *Proposal for a Regulation on a Common European Sales Law* (CESL) expressly prescribe that parties must act in accordance with 'good faith and fair dealing' which reflect the approach of

⁹²⁸ Poole, *Casebook on Contract Law* (n 150) 163-164.

⁹²⁹ *Baird Textile Holdings Ltd v Marks & Spencer Plc* [2001] EWCA Civ 274 [68].

⁹³⁰ Poole, *Casebook on Contract Law* (n 150) 163-164.

⁹³¹ Article 186 of the Civil Code.

⁹³² Moura Vicente (n 290) 35.

⁹³³ According to Law Commission, *An Optional Common European Sales Law: Advantages and Problems (Advice to the UK Government)* (2011) 'all systems of commercial contract law must grapple with the tension between certainty and fairness. English and Scots law have a reputation for leaning towards the certainty end of the scale. By contrast, the CESL is firmly towards the fairness end. It sets high standards of good faith and fair dealing and provides many discretionary remedies to a party who has suffered from a lack of good faith'. See <http://lawcommission.justice.gov.uk/docs/Common_European_Sales_Law_Summary.pdf> accessed 13 July 2012.

continental European countries. For those civil law jurisdictions 'good faith and fair dealing' is 'penicillin [that] permeates all parts of the system and kills all the pernicious germs'; whereas the British 'only wish to operate on parts of the system'.⁹³⁴

However Beale suggested that the aforementioned provisions may not prescribe a general clause of good faith; otherwise the inclusion of other articles which also stipulate for the application of good faith in PECL, DCFR and CESL would be meaningless.⁹³⁵ Nonetheless there is no reason why general and specific provisions prescribing good faith cannot coexist.⁹³⁶ For instance the Brazilian Civil Code prescribes general clauses of good faith in the interpretation and performance of the contracts⁹³⁷ concurrently to the application of this principle in specific provisions related to abuse of rights, insurance contract, possession of properties and so forth.⁹³⁸

6.3.1. Evaluation of the acceptance and recognition of the concept of good faith as a mechanism for controlling the fairness of contractual terms in England

As observed above, the piecemeal solutions offered by English doctrine may be not as efficient as the application of a general principle of good faith. Nevertheless there is still a considerable opposition to the adoption of such principle by English lawyers.⁹³⁹ Due to the 'well known aversion to general principles that is a feature of common law reasoning',⁹⁴⁰ 'British courts have energetically rejected this doctrine on several occasions treating it like a contagious disease of alien origin'.⁹⁴¹ Brownsword enumerated recurrent *negative* arguments which will be examined as follow.⁹⁴²

⁹³⁴ Lando (n 910) 853. Although is possible to argue that the above definition of 'good faith and fair dealing' may be consistent with the idea of 'fair and open dealing' of *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2002] 1 AC 481.

⁹³⁵ Hugh Beale, 'General Clauses and Specific Rules in the Principles of European Contract Law' in S Grundmann and D Mazeaud (eds), *General Clauses and Standards in European Contract Laws: Comparative Law, EC Law and Contract Law Codification* (Kluwer Law International 2006) 211-213.

⁹³⁶ Lando (n 910) 853.

⁹³⁷ Articles 113 and 422 of the Civil Code.

⁹³⁸ See articles 187, 765, 878 and 1202 of the Civil Code.

⁹³⁹ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 114-115.

⁹⁴⁰ Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 432.

⁹⁴¹ Gunther Teubner, 'Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Differences' (1998) 61 MLR 11, 11.

⁹⁴² Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 114-120.

First of all the adoption of the doctrine of good faith is inconsistent with the *individualist ethic* of English contract law⁹⁴³ because it implies that contracting parties should take into consideration the legitimate expectations or interests of the other party.⁹⁴⁴ It may also affect the 'self-reliance ethic' typical of the market trading according to which parties should be entitled to pursue their own interests.⁹⁴⁵ Furthermore the autonomy of the parties and the freedom of contract may be considerably impinged by good faith because courts may interfere in bargains agreed by parties when the latter act against this principle.⁹⁴⁶

Other drawbacks of good faith were already examined in chapter 2 and are directed at B2B contracts. The main arguments against this doctrine revolve around the idea that this concept would create uncertainty in commercial agreements; because it is unclear the extent of the limitations that good faith imposes on the parties' freedom of contract and such restrictions may involve questions of a moral nature that cannot be objectively defined.⁹⁴⁷ It may also be difficult to determine whether or not a party acted in good or bad faith because this evaluation may involve the analysis of the parties' reasons or state of mind which also can give rise to uncertainties.⁹⁴⁸ Furthermore a general clause may be inappropriate in certain contracting situations which require a more specific regulation and where opportunistic behaviour is expected, such as in commodities contracts.⁹⁴⁹

Even the adherents of the *neutral* view may ultimately agree with the above negative view because if the English legal system already offers solutions to the problem of unfairness in contracts then there is no need to replace them with a general doctrine of good faith.⁹⁵⁰ Indeed all those arguments created a sceptical approach concerning the adoption of good faith as an overarching principle in English contract law and 'no more

⁹⁴³ Ibid. 123.

⁹⁴⁴ 'In its classical expression English contract law presupposes an individualistic ethic'. See Brownsword, 'Individualism, Cooperativism and an Ethic for European Contract Law' (n 81) 631.

⁹⁴⁵ Brownsword and Adams, *Understanding Contract Law* (n 127) 194, 195. See *Suisse Atlantique Société d'Armement Maritime S.A. Appellants v N.V. Rotterdamsche Kolen Centrale Respondents* [1967] 1 AC 361, 392 where the House of Lords favoured the freedom of contract and the parties' intentions. Also in *Walford v Miles* [1992] 2 AC 128, 138 Ackner LJ contended that 'each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations'.

⁹⁴⁶ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 115.

⁹⁴⁷ Ibid. 115. See also Moss (n 221) 70.

⁹⁴⁸ See *Regalian Properties Plc v London Docklands Development Corp* [1995] 1 WLR 212. See also Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 116-117.

⁹⁴⁹ Ibid. 119. See also Bridge (n 221) 147.

⁹⁵⁰ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 122.

than a minority of English lawyers' supports its incorporation into the domestic legal system.⁹⁵¹

Despite the current prevalence of the negative view there are some compelling arguments that support the adoption of such general clause by English law. Powell contended that good faith addresses the problem of unfairness in a more direct and transparent way rather than having recourse to 'contortions and subterfuges' such as 'implied promises' to give effect to a sense of justice to a case.⁹⁵² More recently the *Proposal for a Regulation on a Common European Sales Law (CESL)*⁹⁵³ adopted a position in line with the above proposition as it prescribes that parties should behave in accordance with 'good faith and fair dealing' which is defined as 'a standard of conduct characterised by honesty, openness and consideration for the interests of the other party to the transaction or relationship in question' (art. 2). Therefore it expressly purports to prevent unfairness in a more straightforward manner.

Furthermore English law incorporated the provisions of the Unfair Commercial Practices Directive (UCPD)⁹⁵⁴ via the *Consumer Protection from Unfair Trading Regulations 2008* (CPRs).⁹⁵⁵ According to them, 'traders will have to comply with a standard of professional diligence, which requires consideration of honest market practices and good faith'⁹⁵⁶ whether the commercial practice occur 'before, during or after a commercial transaction (if any) in relation to a product'.⁹⁵⁷ Therefore it is possible to suggest that currently traders in England should observe good faith in all contractual stages under the CPRs.⁹⁵⁸

This principle may also work as an 'umbrella principle' which could give the legal ground that courts need to achieve fairer results where specific doctrines (e.g., duress) cannot be

⁹⁵¹ Ibid. 123.

⁹⁵² Powell (n 86) 26. See also *Ingham v Emes* [1955] 2 QB 366 (CA).

⁹⁵³ Article 2 of the Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final.

⁹⁵⁴ European Parliament and Council Directive 2005/29/EC of 11 May 2005 on Unfair Commercial Practices Directive [2005] OJ L149/22.

⁹⁵⁵ SI 2008/1277.

⁹⁵⁶ Christian Twigg-Flesner and others, *An Analysis of the Application and Scope of the Unfair Commercial Practices Directive: A Report for the Department of Trade and Industry* (May 2005) iii.

⁹⁵⁷ See reg. 2(1)(b) of the CPRs.

⁹⁵⁸ According to Willet 'there is a "cradle to grave" regime covering practices such as advertising, persuasion and negotiation at the pre-contractual stage; post contractual alterations or variations; performance, delivery etc by the trader; performance, payment etc by the consumer; complaint handling; after sales service; and enforcement by either party'. See Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 418.

applied.⁹⁵⁹ The examples in the preceding section illustrate those propositions. In *L'Estrange v F Graucob Ltd*⁹⁶⁰ Maugham LJ admitted that 'I regret the decision to which I have come, but I am bound by legal rules and cannot decide the case on other considerations'.⁹⁶¹

Furthermore courts would be able to provide a better protection to the expectations of the parties if there was an implied duty to act in good faith.⁹⁶² In *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd*⁹⁶³ if such duty could have been implied then the Court of Appeal could have inferred that the parties' expectations were of cooperation and equal distribution of risks in a joint venture which could have allowed a different outcome.⁹⁶⁴

Therefore there are indications that the English legal system would benefit from the introduction of a general clause of good faith. This principle has been applied efficiently in the Brazilian legal system and reservations raised by the negative view did not materialise in the context of this jurisdiction. Good faith did not create uncertainties; on the contrary it provided more stability to contractual relationships as parties can trust each other. Furthermore the application of this principle by courts is not completely discretionary but it is made in accordance with the other terms of the contract and the circumstances of the individual case, thus generally parties are able to predict its outcomes and know where they stand.⁹⁶⁵

6.4. Conclusion

Comparative law has a number of significant functions and aims. In the present study this methodology was employed to compare the English and Brazilian legal systems in order to ascertain their 'likenesses and differences' as well as to analyse 'objectively and

⁹⁵⁹ Summers (n 455) 198-199 and 215. Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 124.

⁹⁶⁰ [1934] 2 KB 394.

⁹⁶¹ *L'Estrange v F Graucob Ltd* [1934] 2 KB 394, 405.

⁹⁶² Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 124-128. Steyn LJ contended that the protection of the reasonable expectations of the parties ultimately performs the same function as the principle of good faith. See Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (n 125) 459.

⁹⁶³ [1995] EMLR 472 (CA).

⁹⁶⁴ Brownsword, *Contract Law: Themes for the Twenty-first Century* (n 127) 126-127.

⁹⁶⁵ For instance 'the duty to negotiate in good faith simply imposes a minimal standard of behavior on the negotiating parties and not some highly idealistic and unachievable moral standard'. See David I Bristow and Reva Seth, 'Good faith in Negotiations' (Nov 2000-Jan 2001) 55(4) *Disp Resol J* 16, 21.

systematically the solutions which the various systems offer for a given legal problem',⁹⁶⁶ i.e. 'unfairness' in B2B and B2C contracts. The inclusion of a foreign system in the search for ways of resolving a legal problem provides a 'much richer range of model solutions' than it would be available in the study of one's own jurisdiction.⁹⁶⁷

The application of comparative law is not unfamiliar to English and Brazilian courts. They have used 'foreign law and foreign legal ideas as a means of shaping national law when this is unclear, contradictory, or otherwise in need of reform'.⁹⁶⁸ In England, for instance, Lord Bingham observed in *Fairchild v Glenhaven Funeral Services Ltd.*⁹⁶⁹

If, however, a decision is given in this country which offends one's basic sense of justice, and if consideration of international sources suggests that a different and more acceptable decision would be given in most other jurisdictions, *whatever their legal tradition*, this must prompt anxious review of the decision in question.

Nonetheless the application of civil law as a parameter to solve common law cases is not unanimous. In *White v Jones*⁹⁷⁰ Lord Goff asserted that:

Strongly though I support the study of comparative law, I hesitate to embark in an opinion such as this upon a comparison, however brief, with a *civil law* system; because experience has taught me how very difficult, and indeed potentially misleading, such an exercise can be.⁹⁷¹

Such reservation is understandable in view of potential problems that may affect an adequate use of concepts and rules from one legal system to another.⁹⁷² Gutteridge pointed out that one of the main barriers is the language and 'conceptual differences of legal terminologies' (e.g., the expression 'equity' can have a different connotation in a civil law jurisdiction).⁹⁷³ Furthermore the unfamiliarity with the other legal system may result in an inappropriate use of one's own legal conceptions and expectations due to cultural differences between the systems.⁹⁷⁴

⁹⁶⁶ Walther Hug, 'The History of Comparative Law' (1931-1932) 45 Harv L Rev 1027, 1027.

⁹⁶⁷ Zweigert and Kötz (n 48) 15.

⁹⁶⁸ Basil S. Markesinis, *Comparative law in the Courtroom and Classroom: the Story of the Last Thirty-five Years* (Hart 2003) 157. See *Greatorex v Greatorex* [2000] EWHC 223 (QB).

⁹⁶⁹ [2002] UKHL 22, [2003] 1 AC 32.

⁹⁷⁰ [1995] 2 AC 207.

⁹⁷¹ *White v Jones* [1995] 2 AC 207, 263.

⁹⁷² 'The House made clear that, while these materials were helpful and could support legal argument, they were not to be regarded as determinative or binding on the court in any way (...) to preserve the conventions of the English court and hierarchy of the binding precedent'. See De Cruz (n 10) 22.

⁹⁷³ Harold C Gutteridge, 'Comparative Aspects of Legal Terminology' (1937-1938) 12 Tul L Rev 401, 401-405.

⁹⁷⁴ De Cruz (n 10) 219-230.

Those problems however can be avoided with a proper application of comparative methods which may address those 'perils and pitfalls';⁹⁷⁵ therefore the latter should not prevent the use of comparative law when it can provide a fairer solution to an individual case. Mayss contended that 'an underlying reason for applying a foreign law, rather than English law, is to serve the interests of the parties to the case and achieve justice';⁹⁷⁶ hence one could suggest that courts in England 'are now invoking continental law to a remarkable degree'⁹⁷⁷ when civil law can reach a more satisfactory outcome.

The Brazilian legal system in its turn has not been opposed to the application of comparative law when its legislation does not expressly regulate the matter.⁹⁷⁸ In fact under article 4 of the *Law of Introduction to the Brazilian Civil Code*⁹⁷⁹ 'when the legislation is silent, the judge shall decide the case according to analogy, customs and the general principles of law'.⁹⁸⁰ This open provision may allow judges to look for solutions in foreign jurisdictions in the silence of the national law because they cannot abstain from deciding. It is possible to argue that it may be more natural to Brazilian courts to make references to foreign legal systems than their English counterparts because the law of Brazil was inspired by alien legislation (mainly European),⁹⁸¹ whereas England gave origin to its own legal system (common law).

Another indication of the acceptance of comparative law by the Brazilian legal system is the express reference to its use in article 8 of the *Consolidated Labour Laws*⁹⁸² which prescribes that:

Administrative authorities and Labour Courts, in the absence of legal or contractual provisions shall decide as appropriate according to case law, analogy,

⁹⁷⁵ Ibid. 219.

⁹⁷⁶ Abba J Mayss, *Principles of Conflict of Laws* (3rd edn, Principles of Law Series, Cavendish 1999) 4. Similarly North and Fawcett observed that 'there is no sacred principle that pervades all decisions but, when the circumstances indicate that the internal law of a foreign country will provide a solution more just, more convenient and more in accord with the expectations of the parties than the internal law of England, the English judge does not hesitate to give effect to the foreign rules.' See Peter North and J. J. Fawcett, *Cheshire and North's Private International Law* (12th edn, Butterworths 1992) 39.

⁹⁷⁷ Zweigert and Kötz (n 48) 19.

⁹⁷⁸ There are a number of decisions of the Superior Court of Justice which make reference to comparative law such as REsp 1174235/RJ (28/02/2012); REsp 302906/SP (01/12/2010); REsp 1149529/RJ (12/03/2010); REsp 963686/RS (27/08/2009) and REsp 4138/PR (03/12/1990). Equally the Supreme Federal Court also refers to comparative law in various decisions: RE 477554/MG (26/08/2011); HC 109544/BA (31/08/2011); MI 708/DF (31/10/2008); RHC 90376/RJ (17/05/2007); AI 529694/RS (11/03/2005); HC 76060/SC (15/05/1998) and so forth.

⁹⁷⁹ Decree-law 4657/1942.

⁹⁸⁰ Rose (n 251) 2.

⁹⁸¹ The Consumer Protection Code was substantially influenced by the French '*Projet de Code de la Consommation*' and the Civil Code by the Italian Civil Code. See Grinover and others (n 34) 7.

⁹⁸² Decree-law 5452/1943.

equity, other principles and general rules of law, especially labour law, and yet, *comparative law* according to customs and traditions.

In line with this provision Justice Rosa Maria Weber of the Superior Labour Court observed that 'we can find in comparative law a fertile source of experiences that can be used as example of possible solutions to the problem'.⁹⁸³

Therefore comparative law has played an important function in the context of national legal systems (such as England and Brazil) and its importance can be also extended to the context of 'international trade regimes'.⁹⁸⁴ For instance in the European Union there has been an increasing interaction between common law and civil law which has required the harmonisation of its law.⁹⁸⁵ Such harmonisation is 'designed to effect an approximation or co-ordination of different legal provisions or systems by eliminating major differences and creating minimum requirements or standards'.⁹⁸⁶ This function of comparative law has been also employed in the Mercosul as its resolutions have to reconcile the legislation of all its Member States.⁹⁸⁷

Comparative law can be employed to achieve distinct aims at national or international level and may have different rationales. In line with Collins, the rationale of the present study can be classified as *positivist* or *utilitarian* because it sought the best solutions to a legal problem through the comparison of rules and techniques of distinct jurisdictions (England and Brazil) and recommended lessons that those legal systems can learn from each other as examined in the preceding sections.⁹⁸⁸ This work also contained a more indirect rationale which was to allow a better understanding of one's own legal system through the analysis of doctrines of a foreign jurisdiction.⁹⁸⁹ Comparatists may have a better understanding of the logic behind the concepts and rules of their national system while examining the reasons why they differ from the other legal system.⁹⁹⁰

⁹⁸³ Proceeding RR - 108100-45.2007.5.04.0009 (23/04/2010).

⁹⁸⁴ Those trade regimes are outside or above the national ones and include: the EU, the Mercosul, NAFTA, etc. See Mathias Reimann, 'Beyond National Systems: A Comparative Law for the International Age' (2000-2001) 75 Tul L Rev 1103, 1107.

⁹⁸⁵ De Cruz (n 10) 23-26 and Zweigert and Kötz (n 48) 28-29.

⁹⁸⁶ See W. J. Kamba, 'Comparative Law - A Theoretical Framework' (1974) 23 ICLQ 485, 501.

⁹⁸⁷ In the context of the Mercosul the comparison of the law of its Member States is in principle more straightforward than in the EU because all members adopt the civil law tradition. However as seen previously their legislation has some significant differences such as distinct levels of consumer protection.

⁹⁸⁸ Collins, 'Methods and Aims of Comparative Contract Law' (n 884) 397.

⁹⁸⁹ Ibid. 398-399.

⁹⁹⁰ Ibid. 399. The differences in the application of good faith for instance reflect more fundamental distinctions between the English and Brazilian legal systems.

CHAPTER 7. CONCLUSION

7.1. Context

Ordinary people and businesses are daily exposed to contracts which may contain unfair provisions. Those unfair terms are often imposed in *standard form contracts* which are drafted by the party who holds a greater bargaining strength; hence the weaker party usually faces a 'take-it-or-leave-it' situation and is unable to negotiate its contents.⁹⁹¹

The widespread use of 'contracts of adhesion' and the frequent inclusion of unjust terms or unreasonable exemption clauses made imperative the establishment of limits to them. Distinct jurisdictions developed different ways to prevent or tackle those unfair terms. The solutions applied to the problem of unfairness may vary between jurisdictions because they are invariably influenced by their legal traditions (e.g., common law or civil law) and other characteristics of their milieu (e.g., cultural, social and economic).

The prime objective of this study was to compare how two distinct jurisdictions (England and Brazil) deal with contractual unfairness through the imposition of legislative controls.⁹⁹² This comparison enabled the identification of major issues and weaknesses of the relevant legislation in both legal systems, as well as strengths and lessons that may be derived from each system and applied to the other.

This work also examined the differences in the extent to which unfair terms are imposed on businesses (including small businesses) and consumers. Businesses parties are normally in a better position to negotiate terms with their counterparties as often they share a similar bargaining power. In addition, in B2B contracts the inclusion of exemption clauses or harsh terms may be compensated by terms which offer additional benefits (e.g., better prices and allocation of insurance). However this assumption of parity between parties cannot be extended to small businesses because they are often in a disadvantageous position in the face of large businesses. For similar reasons consumers commonly have to accept terms imposed by sellers and suppliers.

⁹⁹¹ As Lord Reid observed 'in the ordinary way the customer has no time to read [the standard terms contracts], and if he did read them he would probably not understand them. and if he did understand and object to any of them, he would generally be told he could take it or leave it. and if he then went to another supplier the result would be the same. Freedom to contract must surely imply some choice or room for bargaining.' See *Suisse Atlantique Société d'Armement Maritime S.A. Appellants v N.V. Rotterdamsche Kolen Centrale Respondents* [1967] 1 AC 361, 406.

⁹⁹² More precisely in B2C, B2B and small business contracts.

As a result of the above differences the level of protection afforded by legislation to businesses and consumers will vary according to their needs. Both the English and Brazilian legal systems allow more leeway to business parties to define the terms of their agreements because they normally are able to protect their own interests. B2C contracts however are more closely regulated by the law of both jurisdictions because usually consumers are in a more vulnerable position in the market and require a special protection. Small businesses, just like consumers, are more exposed to disadvantageous terms but presently there is no special regime either in England or Brazil which offers a specialised protection to them. For this reason Brazilian courts have adopted a more interventionist approach to protect their interests and avoid the exploitation of their vulnerability; whereas the Law Commission has proposed a special regime for SMEs.

Although in the past decades significant developments could be observed in England and Brazil concerning the prevention of contractual unfairness (largely in the context of consumer agreements)⁹⁹³ the current legislation still needs to be improved. As seen in chapter 5 there are overlaps and conflicts within the internal legislation of both jurisdictions (e.g., UCTA and UTCCR; Civil Code and Consumer Protection Code) and their provisions may be insufficient to deal with all situations of unfairness (e.g., in England there is no general rule of pre-contractual liability and in Brazil small businesses are not satisfactorily protected against abusive clauses).

Part of the solution to issues of the unfair terms legislation in England and Brazil may be found within their own jurisdictions. For instance in England the Law Commission proposed a unified regime to tackle unfair terms in contracts,⁹⁹⁴ whereas the Brazilian legal system prescribes criteria to deal with conflicts of law.⁹⁹⁵ However there are problems which cannot be adequately addressed by the internal law of those jurisdictions; therefore they may find better ways to tackle them in another legal system via comparative law. As examined in chapter 6, the English legal system could benefit from the example set by the Brazilian law which has efficiently applied good faith as a general clause to deal with unfairness at all contractual stages. On the other hand the Brazilian legal system could learn from the English system of precedents which allow the law to

⁹⁹³ E.g., Unfair Terms in Consumer Contracts Regulations 1999 and Consumer Protection Code.

⁹⁹⁴ See chapters 2 and 3.

⁹⁹⁵ Criteria of anteriority, speciality and hierarchy. See chapter 5.

adapt to new situations more readily than Codes;⁹⁹⁶ hence it would be more advantageous for B2B contracts.

7.2. Review of aims and objectives

This work purported to analyse pieces of legislation which regulate terms on the basis of their 'unfairness' and are not limited to the 'legislative regulation of specific terms'.⁹⁹⁷ In addition they make use of 'general clauses' such as good faith and reasonableness to tackle abusive clauses.⁹⁹⁸ Chapters 2, 3 and 4 examined those legislative controls on unfair terms in the English and Brazilian legal systems in the context of B2B, B2C and small business contracts respectively. The understanding of the relevant legislation and case law in the context of England and Brazil was a prerequisite for the comparative analysis which was ultimately the essence of this research.

Zweigert and Kötz observed that 'whoever reads or uses a work on comparative law must be familiar with the basic material, or he will be in no position to make the necessary comparisons'.⁹⁹⁹ For this reason the comparative examination between those legal systems was made at the final part of each of the above chapters following the examination of the English law and Brazilian law separately. The comparison highlighted their differences and similarities in the context of the distinct types of contracts.

Nonetheless the main aim of the thesis had an *evaluative* nature which in the words of Cryer, Hervey and Sokhi-Bulley means to assess the way that the legal world is, and subject the law to appraisal.¹⁰⁰⁰ According to them 'where shortfalls are identified' evaluative scholarship may suggest 'how things might be improved'.¹⁰⁰¹ In line with that, this work identified and examined the existing problems of the above controls in chapter 5 and evaluated in chapter 6 lessons that the Brazilian law may learn from English law and vice versa.

This work applied the comparative law methodology because it was deemed the most appropriate to achieve the above aims of the proposed research. The choice of the

⁹⁹⁶ MacIntyre (n 875) 27.

⁹⁹⁷ Poole, *Textbook on Contract Law* (n 6) 244.

⁹⁹⁸ Willett, 'General Clauses and the Competing Ethics of European Consumer Law in the UK' (n 9) 412.

⁹⁹⁹ Zweigert and Kötz (n 48) 43.

¹⁰⁰⁰ Cryer, Hervey and Sokhi-Bulley (n 52) 9.

¹⁰⁰¹ *Ibid.*

methodology, theory and approaches however may be a 'matter of personal style. Our choice of style reflects our professional and personal goals'.¹⁰⁰² Although this work was conducted in the most objective way possible, the fact that the researcher is a Brazilian lawyer arguably directed the study to emphasise the need for consumer protection, which is the dominant view in Brazil. This may also have influenced the researcher to adopt a more positive approach towards the application of good faith as an overriding principle in English law as this concept is already widely accepted as such in civil law jurisdictions.

7.3. Limitations

As seen in chapter one, this work was a *micro-comparison* limited to the analysis of statutory controls of unfair terms and exemption clauses in B2B, B2C and small businesses contracts because it would not be feasible to analyse all types of contracts or the entire legal systems in question. In the same chapter it was discussed that some comparatists may criticise the choice of the Brazilian legal system for a comparative study with the English legal system because it is not regarded as a 'mature legal system'. Nevertheless as already discussed in chapter 6, the 'extraordinariness' of the Brazilian law is actually what enriched the proposed comparison as it enabled the analysis of the research problem from a distinct perspective.¹⁰⁰³

One could also contend that this work did not cover all mechanisms for controlling unfairness in contracts. However as acknowledged from the beginning, the scope of this study was limited to 'legislative controls' for practical reasons. The study of all controls on unfairness would be excessively wide as it would include common law concepts such as fraud, misrepresentation, duress and undue influence; which in a comparative study with the Brazilian law would require the analysis of numerous provisions of the Civil Code that deal with defects of juridical transactions (mistake, ignorance, wrongful conduct, coercion, state of peril, lesion and fraud against creditors).¹⁰⁰⁴

¹⁰⁰² Ibid. 8-9.

¹⁰⁰³ Örucü, 'Comparatists and Extraordinary Places' (n 55) 470 and Baxter and Ong (n 56) 89.

¹⁰⁰⁴ Articles 138 to 165 of the Brazilian Civil Code (Act 10406/2002).

7.4. Contributions of the research

There are a number of studies which tackle directly or indirectly the problem of contractual unfairness and/or which evaluate different ways to deal with this problem.¹⁰⁰⁵ Some of these studies encompass a comparative component involving more than one jurisdiction and there is a considerable amount of work dedicated to the comparison between English law and the law of the Continental Member States. England is often referred as a paradigm for a common law jurisdiction which may experience problems integrating with other EU Member States that adopt a civilian tradition¹⁰⁰⁶ and the harmonisation of the EU law has been a popular topic in the most recent literature.¹⁰⁰⁷

There are no works however which compare the English legal system with the Brazilian legal system in this context. A possible reason for the absence of comparisons involving the Brazilian law is that more traditional comparatists would prefer to exam 'mature legal systems' rather than 'affiliated legal systems' as seen previously.¹⁰⁰⁸ Furthermore the insufficient knowledge of the law of an 'extraordinary place' such as Brazil and of its language (Portuguese) is another barrier which may have prevented or discouraged the inclusion of this jurisdiction in a comparative analysis with a European jurisdiction. The fact that the researcher is a Brazilian lawyer provided the means to overcome this problem and to carry out a reliable analysis of this legal system.¹⁰⁰⁹

Another probable reason for the non-existence of studies involving the above jurisdictions is that arguably comparisons tend to be circumscribed to countries which share more common features. Therefore comparative studies with English law may either include other common law jurisdictions (e.g., USA)¹⁰¹⁰ or the law of other EU Member States;

¹⁰⁰⁵ For example: Beale, 'Legislative Control of Fairness: The Directive on Unfair Terms in Consumer Contracts' (n 333); Bright, 'Winning the Battle against Unfair Contract Terms' (n 434); Macdonald, 'Mapping the Unfair Contract Terms Act 1977 and the Directive on Unfair Terms in Consumer Contracts' (n 766).

¹⁰⁰⁶ Miller (n 373).

¹⁰⁰⁷ Horst Eidenmuller and others, 'The Common Frame of Reference for European Private Law - Policy Choices and Codification Problems' (2008) 28(4) OJLS 659; Simon Whittaker, 'A Framework of Principle for European Contract Law?' (2009) 125(Oct) LQR 616; Ewan Mckendrick, 'Harmonisation of European Contract Law: The State We Are In' in S Vogenauer and S Weatherill (eds), *The Harmonisation of European Contract Law: Implications for European Private Laws, Business and Legal Practice* (Hart 2006); Reiner Schulze (ed), *Common Frame of Reference and Existing EC Contract Law* (Sellier 2008).

¹⁰⁰⁸ Zweigert and Kötz (n 48) 41. See chapter 6.

¹⁰⁰⁹ This will avoid certain problems which can affect comparisons such as 'the possible lack of a deep level of knowledge of languages, pitfalls related to translation, especially translation of culture-specific concepts, and cultural deficit'. See Özücü, 'Methodology of Comparative Law' (n 49) 450.

¹⁰¹⁰ R Reed, 'Foreign Precedents and Judicial Reasoning: the American Debate and British Practice' (2008) 124 LQR 253; Patrick S. Atiyah and Robert S. Summers, *Form and Substance in Anglo-American Law: A Comparative Study in Legal Reasoning, Legal Theory, and Legal Institutions* (Clarendon Press, Oxford, 1991).

whereas comparisons with the Brazilian law may include other civil law jurisdictions (e.g., Germany and Portugal)¹⁰¹¹ or the law of other members of the Mercosul (e.g., Argentina).¹⁰¹²

Yet the uniqueness of this work consisted precisely in placing side-by-side those two legal systems which at first sight did not have much in common since they were developed in countries with distinct backgrounds. The understanding of their contrasting characteristics, or even of their resemblances, enabled a reflective exercise on the reasons why each of the systems developed its legislative controls on unfairness into the present state.

Despite belonging to two distinct legal families, both jurisdictions recognised that consumers are in no position to protect their own interests; hence the responsibility for protecting them has fallen upon their governments.¹⁰¹³ As a consequence the latter have enacted special legal provisions to this end. Although this study highlighted some noticeable differences between the legislation of England and Brazil in this context, in essence the law of both countries is consistent with the *consumer welfarist* ideology as seen in chapter 1.¹⁰¹⁴

There are also fundamental similarities between the English and Brazilian law in the context of B2B contracts as both prescribe fewer restrictions to business parties and arguably are more in line with the *dynamic market-individualism* ideology. Nonetheless the degree of freedom of contract given to parties is to some extent different in England and Brazil. Whereas 'the commercial culture of England (...) obviously is founded more

¹⁰¹¹ Luiz G. S. Adolfo, 'Estudo Comparado do Direito de Sequência na Legislação Autoral de Brasil, Alemanha, Espanha, França e Portugal' (1998) São Leopoldo, set/dez, v. 31, n. 83 Estudos Jurídicos 15; Lúcio G. Gouveia, 'O Dever de Cooperação dos Juízes e Tribunais com as Partes: uma Análise sob a Ótica do Direito Comparado (Alemanha, Portugal e Brasil)' (2000) Recife, jan/jun, v. 5, n. 11, Revista da Esmape 247.

¹⁰¹² José Inácio G. Franceschini, 'Legislação de Defesa da Concorrência Comparada: Brasil-Argentina, Contribuição ao Tratado Mercosul' (1992) Brasília, out/dez, n. 7 Boletim de Integração Latino-Americana 26; Fernando Rezende, 'Harmonização Tributária no Mercosul - Brasil x Argentina' (1993) Brasília, abr/jun, v. 2, n. 4 Tributação em Revista 9.

¹⁰¹³ Brownsword and Adams, *Understanding Contract Law* (n 127) 177.

¹⁰¹⁴ See UTCCR 1999 and the Brazilian Consumer Protection Code. As seen earlier the industrialisation of England and Brazil led to the development of the modern mass production and consumption in large scale. The latter in its turn implied in a widespread use of standard form contracts which facilitate the inclusion of unfair terms by the stronger party of the contract, in particular in B2C contracts. This required the development of a special regime for consumer protection to prevent the abuses of the vulnerability of consumers in both jurisdictions.

directly on the play of market forces',¹⁰¹⁵ in Brazil business are limited by principles such as good faith and the social function of the contracts which define their behaviour.

Such concept of good faith was used in this work as an apposite example that reflects fundamental differences between the English and Brazilian legal systems. For instance, as examined above, the Brazilian law can afford more protection to business parties through the application of this concept and in this jurisdiction good faith has the status of a general principle which should be observed at all contractual stages including negotiations. By comparison in English law the application of good faith is limited to B2C contracts and to the performance stage,¹⁰¹⁶ hence it does not cover parties during negotiations in line with *Walford and Miles*.¹⁰¹⁷

7.5. Recommendations

The present work identified in chapter 5 issues that negatively affect the efficiency of the law of England and Brazil regarding the control on unfair terms and unreasonable exemption clauses. One of the main problems is the internal inconsistencies and conflicts within their legal systems. In Brazil there are already mechanisms in place that deal with those conflicts of law (the criteria of anteriority, speciality and hierarchy); whereas in England the Law Commission proposed in 2005 a unified regime to replace UCTA 1977 and UTCCR 1999 which are the main pieces of legislation that tackle contractual unfairness.¹⁰¹⁸

Although the Law Commission's recommendations were already accepted by the Government, their implementation were on hold awaiting for the outcome of the *Proposal for a Directive on Consumer Rights*¹⁰¹⁹ which purported to repeal four existing consumer directives (including the Directive 93/13/EEC) and to introduce more consistent provisions. Nonetheless when the *Directive on Consumer Rights* was approved by the EU's Council of Ministers in October 2011 the only change made to the *Directive on Unfair*

¹⁰¹⁵ Geraint Howells and Thomas Wilhelmsson, 'EC Consumer Law: Has it Come of Age?' (2003) 28(3) EL Rev 370, 385.

¹⁰¹⁶ See reg. 5(1) of UTCCR 1999.

¹⁰¹⁷ [1992] 2 AC 128.

¹⁰¹⁸ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005).

¹⁰¹⁹ Commission, 'Proposal for a Directive on Consumer Rights' COM (2008) 614 final. See also <<http://lawcommission.justice.gov.uk/areas/unfair-terms-in-contracts.htm>> accessed 02 February 2012.

Terms in Consumer Contracts was a small amendment to its article 8.¹⁰²⁰ However due to the time elapse since 2005 and the developments in the case law during this time, the Law Commission proposed in July 2012 a review and update of its recommendations which is open for consultation until 25 October 2012.

The Department for Business, Innovation and Skills (BIS) in its turn proposed a *Consumer Bill of Rights* in September 2011 which aims to implement the *Directive on Consumer Rights* and reform the current consumer legislation in the UK.¹⁰²¹ As mentioned earlier it is not clear how the Law Commission recommendations will interact with the proposed *Consumer Bill of Rights* because the scope of the former is wider than of the latter as it includes provisions which cover B2B and small business contracts. On the other hand the above Bill deals with aspects of the consumer relations other than unfairness in contracts, such as the rights of the consumers concerning 'faulty goods and poor services' and it also aims to 'update the law to clarify rights in relation to digital content'.¹⁰²² Nevertheless BIS and the Law Commission should coordinate the development of both initiatives in a way that their provisions regarding consumer contracts are consistent and in harmony.¹⁰²³

Although the new Law Commission's recommendations aim to update its original proposals they still persist in rejecting the application of 'good faith' in favour of a 'fair and reasonable' test.¹⁰²⁴ This study however disagrees with the position adopted by the Law Commission towards the concept of 'good faith'. Instead of taking into account all advantages and improvements that this concept could offer to the English legal system, it seemed that the Law Commission preferred to avoid controversies. It suggested that the 'requirement of reasonableness' of UCTA 1977 and the 'fairness test' of UTCCR 1999 should be combined and replaced by the above 'fair and reasonable test' with no express reference to 'good faith', on the grounds that this concept is unfamiliar and confusing to

¹⁰²⁰ This amendment requires that Member States shall inform the European Commission if they adopt most stringent provisions that ensure a higher degree of consumer protection. See article 32 of the Directive on Consumer Rights (2011/83/EU). The new rules have to be transposed only by 13 December 2013.

¹⁰²¹ See <<http://www.bis.gov.uk/policies/consumer-issues/consumer-rights>> accessed 01 October 2011.

¹⁰²² Department for Business, Innovation and Skills (BIS), *Enhancing Consumer Confidence by Clarifying Consumer Law: Consultation on the Supply of Goods, Services and Digital Content* (July 2012) 6.

¹⁰²³ The fact that the Law Commission consultation will be followed by an Advice to the Department for Business Innovation and Skills (BIS) in spring 2013 may assist the consistency between both initiatives. See <http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm> accessed 26 July 2012.

¹⁰²⁴ The consultation launched in July 2012 only questioned if consultees agree that courts should take into account 'the extent to which it was transparent; the substance and effect of the term; and all the circumstances existing at the time it was agreed' when deciding if a term is 'fair and reasonable'. See Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012) paras 9.47 and 9.50.

English lawyers and that each Member State can choose the 'form and method' of implementation of EU Directives.¹⁰²⁵

However the researcher shares the same concerns as those respondents who did not agree with the Law Commission's opinion.¹⁰²⁶ According to our view the intended result of the Directive 93/13/EEC will not be achieved with the exclusion of good faith from the 'fairness test', as this concept is regarded a fundamental principle in civilian systems which influenced the making of the Directive in question.¹⁰²⁷ For this reason it cannot be simply ignored by the English law and substituted by a 'fair and reasonable test' as they are not equivalents according to the EU law. For instance the 'Principles of European Contract Law' (PECL) make reference to the duties of 'good faith *and* fair dealing' and it refers to the requirement of 'reasonableness' in a separate provision.¹⁰²⁸

Another reason against the exclusion of good faith is that overall this concept may bring more advantages than disadvantages to the English legal system as discussed in chapter 6. Additionally the acceptance and implementation of concepts and rules typical of civil law is an inevitable part of the process of harmonisation between the English law and the law of the other Member States. Furthermore as this work previously proposed the application of good faith as an overriding principle may allow English courts to make fairer decisions where the existing piecemeal solutions are not satisfactory.

In this respect, this study recommended that the English courts and interpreters should look at a civilian jurisdiction for a better comprehension of the scope and extent of this concept. It therefore employed the Brazilian law as a model or comparator of a legal system which has efficiently applied good faith as a general principle in the context of B2C and B2B contracts.

The present work also recognises that the Law Commission's recommendations have their merits and that 'this draft legislation will inevitably be a great improvement on the current

¹⁰²⁵ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 3.86. See also Article 288 (ex Article 249 TEC) of the Consolidated version of the Treaty on European Union and the Treaty on the Functioning of the European Union: 'A directive shall be binding, as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods.'

¹⁰²⁶ Law Commission, *Unfair Terms in Contracts* (Law Com No 292, 2005) para 3.88.

¹⁰²⁷ The Law Society observed that 'any reform has to be undertaken carefully, in order to make sure the original provisions of the Directive are given effect and EU law is not breached'. See Response by the Law Society to Law Commission, *Unfair Terms in Consumer Contracts: A New Approach? Issues Paper* (Law Com No 292, 2012) para 15.

¹⁰²⁸ See articles 1:201 and 1:302 of PECL.

law'.¹⁰²⁹ Perhaps one of the most significant additions would be the introduction of a special regime for small businesses because, as analysed in chapter 4, SMEs would benefit greatly from an extra protection. As previously noted, by comparison with the English legal system there is no indication that the Brazilian legal system is concerned to enact special protections to small businesses against abusive clauses in their dealings. Arguably this jurisdiction may consider sufficient the protection provided by its general provisions even though courts' decisions have consistently pointed in the opposite direction as they have protected SMEs through the analogous application of the provisions of the Consumer Protection Code.

For this reason the Brazilian legal system should emulate the recommendations of the Law Commission and propose a special contractual regime for small businesses which meet their specific needs. The interventionist approach adopted by Brazilian courts to protect vulnerable businesses should be deemed as an *interim measure* applied only in the absence of adequate legislation. As a jurisdiction which adopts the civil law tradition, it is particularly important to the Brazilian law to cover situations which have been subject to litigation as its legal system should be comprehensive and free of gaps.

7.5.1. Suggestions for further research

A comparison similar to the present one could also be made between the Brazilian law and the American law.¹⁰³⁰ The United States of America inherited the common law tradition from England, but they developed a system with its own characteristics. There is a general acceptance of good faith in this jurisdiction¹⁰³¹ which is expressly prescribed in the *Uniform Commercial Code* and in the *American Institute's Restatement (Second) of Contracts*.¹⁰³² This doctrine has been applied 'in a wide variety of situations' in the USA;¹⁰³³ thus case law of this country may be a rich source for research and may provide distinct insights concerning the application of good faith in a different common law system.

¹⁰²⁹ Poole, *Textbook on Contract Law* (n 78) 277.

¹⁰³⁰ Although there are works which involve the Brazilian law and the American law, they do not have the same purpose of the present study. E.g., Quagliato (n 82); Anelize S. Aguiar, 'The Law Applicable to International Trade Transactions with Brazilian Parties: A Comparative Study of the Brazilian Law, the CISG, and the American Law about Contract Formation' (2011) 17(3) *Law and Business Review of the Americas* 487.

¹⁰³¹ E. Allan Farnsworth, 'Good Faith in Contract Performance' in J Beatson and D Friedmann (eds), *Good faith and Fault in Contract Law* (Oxford University Press 1997) 155.

¹⁰³² See § 1-201 (19) and § 1-203 of the Uniform Commercial Code (UCC) and §205 of the Restatement (Second) of Contracts.

¹⁰³³ See Farnsworth (n 1031) 159.

Additional resources for further research may be also found in the ongoing legislative proposals relevant to this study, such as the *Consumer Bill of Rights* and the new Law Commission recommendations.¹⁰³⁴ If implemented they may introduce significant changes in this area and give rise to different issues in the forthcoming years.

Similarly if the proposed special regime for small businesses comes into force, it will be a prominent area of study especially in view of the peculiarities of SMEs and their importance to the economy. For those who are concerned with an excessive fragmentation of contract law that may result from the implementation of yet another special regime, there is a more recent position in the legal literature which proposes a general protection of the weaker party in 'asymmetric contracts'¹⁰³⁵ and seems to be a fertile area to be explored.

There is still also plenty of room for comparative studies between the common law of England and the civil law systems of the Continental Member States as part of the harmonisation process of the EU law. There are also questions related to the scope of harmonisation such as whether it should be limited to cross-border transactions or also extended to internal contracts and whether it should cover only B2B or B2C contracts or both.¹⁰³⁶

Recently the European Commission proposed an optional *Regulation on a Common European Sales Law*¹⁰³⁷ which prescribes a 'single set of rules' for cross-border contracts involving EU Member States.¹⁰³⁸ The purpose of this Regulation is to increase the level of consumer protection and to facilitate the transactions across the European Union. Although the availability of one common regime of contract law for all Members States has its merits, its effectiveness may be limited by the fact that it is applicable on a 'voluntary basis, upon an express agreement of the parties'.¹⁰³⁹ Therefore only after its implementation it will be possible to examine its relevance and impact on the contractual relations in the context of the EU. Further comparative analysis may be required to allow adjustments to its rules in order to meet the different realities of the Member States.

¹⁰³⁴ Law Commission, *Unfair Terms in Consumer Contracts: A New Approach?* (Law Com No 292, 2012).

¹⁰³⁵ Roppo (n 597).

¹⁰³⁶ See Picat and Soccio (n 365) 408.

¹⁰³⁷ See Commission, 'Proposal for a Regulation on a Common European Sales Law' COM (2011) 635 final.

¹⁰³⁸ *Ibid.* 4.

¹⁰³⁹ *Ibid.* 8.

Finally the above harmonisation of the EU law leads to another question which is the viability of the creation of a European Civil Code. This would be a long term project which would need to be carefully developed in order to reasonably satisfy the needs of the Members States and to respect their cultural differences. Although there are some arguments in favour of the creation of this Code such as that it would strengthen the trade of the EU internally and in the international market,¹⁰⁴⁰ it mainly faces a great deal of opposition. Members States will not replace their domestic law in favour of an EU Code unless they can identify clear advantages in doing that. Comparative studies can provide more compelling arguments which can support both sides (for and against) and may enable Member States to decide whether it is a project which is worthy to be pursued or whether it should be scrapped altogether.

¹⁰⁴⁰ In addition Picat and Soccio contended that although objections to this Code are based on the argument that 'legal pluralism constitutes the strength of Europe', 'cultural pluralism does not make Europe an economic force capable of rivalling other economic powers such as the United States, the emerging countries, Russia, Brazil, China, India, etc.' See Picat and Soccio (n 365) 399-407.

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Appendices

Appendix 1: Unfair Contract Terms Act 1977

UNFAIR CONTRACT TERMS ACT 1977

1977 CHAPTER 50

An Act to impose further limits on the extent to which under the law of England and Wales and Northern Ireland civil liability for breach of contract, or for negligence or other breach of duty, can be avoided by means of contract terms and otherwise, and under the law of Scotland civil liability can be avoided by means of contract terms

[26th October 1977]

BE IT ENACTED by the Queen's most Excellent Majesty, by and with the advice and consent of the Lords Spiritual and Temporal, and Commons, in this present Parliament assembled, and by the authority of the same, as follows:—

PART I

AMENDMENT OF LAW FOR ENGLAND AND WALES AND NORTHERN IRELAND

Introductory

1. Scope of Part I

- (1) For the purposes of this Part of this Act, "negligence" means the breach—
- (a) of any obligation, arising from the express or implied terms of a contract, to take reasonable care or exercise reasonable skill in the performance of the contract;
 - (b) of any common law duty to take reasonable care or exercise reasonable skill (but not any stricter duty);
 - (c) of the common duty of care imposed by the Occupiers' Liability Act 1957 or the Occupiers' Liability Act (Northern Ireland) 1957.
- (2) This Part of this Act is subject to Part III; and in relation to contracts, the operation of sections 2 to 4 and 7 is subject to the exceptions made by Schedule 1.
- (3) In the case of both contract and tort, sections 2 to 7 apply (except where the contrary is stated in section 6(4)) only to business liability, that is liability for breach of obligations or duties arising—
- (a) from things done or to be done by a person in the course of a business (whether his own business or another's); or
 - (b) from the occupation of premises used for business purposes of the occupier;
- and references to liability are to be read accordingly [but liability of an occupier of premises for breach of an obligation or duty towards a person obtaining access to the premises for recreational or educational purposes, being liability for loss or damage suffered by reason of the dangerous state of the premises, is not a business liability of the

occupier unless granting that person such access for the purposes concerned falls within the business purposes of the occupier].

(4) In relation to any breach of duty or obligation, it is immaterial for any purpose of this Part of this Act whether the breach was inadvertent or intentional, or whether liability for it arises directly or vicariously.

2. Negligence liability

(1) A person cannot by reference to any contract term or to a notice given to persons generally or to particular persons exclude or restrict his liability for death or personal injury resulting from negligence.

(2) In the case of other loss or damage, a person cannot so exclude or restrict his liability for negligence except in so far as the term or notice satisfies the requirement of reasonableness.

(3) Where a contract term or notice purports to exclude or restrict liability for negligence a person's agreement to or awareness of it is not of itself to be taken as indicating his voluntary acceptance of any risk.

3. Liability arising in contract

(1) This section applies as between contracting parties where one of them deals as consumer or on the other's written standard terms of business.

(2) As against that party, the other cannot by reference to any contract term—
(a) when himself in breach of contract, exclude or restrict any liability of his in respect of the breach; or
(b) claim to be entitled—
(i) to render a contractual performance substantially different from that which was reasonably expected of him, or
(ii) in respect of the whole or any part of his contractual obligation, to render no performance at all,

except in so far as (in any of the cases mentioned above in this subsection) the contract term satisfies the requirement of reasonableness.

4. Unreasonable indemnity clauses

(1) A person dealing as consumer cannot by reference to any contract term be made to indemnify another person (whether a party to the contract or not) in respect of liability that may be incurred by the other for negligence or breach of contract, except in so far as the contract term satisfies the requirement of reasonableness.

(2) This section applies whether the liability in question—
(a) is directly that of the person to be indemnified or is incurred by him vicariously;
(b) is to the person dealing as consumer or to someone else.

5. "Guarantee" of consumer goods

(1) In the case of goods of a type ordinarily supplied for private use or consumption, where loss or damage—

- (a) arises from the goods proving defective while in consumer use; and
- (b) results from the negligence of a person concerned in the manufacture or distribution of the goods,

liability for the loss or damage cannot be excluded or restricted by reference to any contract term or notice contained in or operating by reference to a guarantee of the goods.

(2) For these purposes—

- (a) goods are to be regarded as "in consumer use" when a person is using them, or has them in his possession for use, otherwise than exclusively for the purposes of a business; and
- (b) anything in writing is a guarantee if it contains or purports to contain some promise or assurance (however worded or presented) that defects will be made good by complete or partial replacement, or by repair, monetary compensation or otherwise.

(3) This section does not apply as between the parties to a contract under or in pursuance of which possession or ownership of the goods passed.

6. Sale and hire-purchase

(1) Liability for breach of the obligations arising from—

- (a) [section 12 of the Sale of Goods Act 1979] (seller's implied undertakings as to title, etc);
- (b) section 8 of the Supply of Goods (Implied Terms) Act 1973 (the corresponding thing in relation to hire-purchase),

cannot be excluded or restricted by reference to any contract term.

(2) As against a person dealing as consumer, liability for breach of the obligations arising from—

- (a) [section 13, 14 or 15 of the 1979 Act] (seller's implied undertakings as to conformity of goods with description or sample, or as to their quality or fitness for a particular purpose);
- (b) section 9, 10 or 11 of the 1973 Act (the corresponding things in relation to hire purchase),

cannot be excluded or restricted by reference to any contract term.

(3) As against a person dealing otherwise than as consumer, the liability specified in subsection (2) above can be excluded or restricted by reference to a contract term, but only in so far as the term satisfies the requirement of reasonableness.

(4) The liabilities referred to in this section are not only the business liabilities defined by section 1(3), but include those arising under any contract of sale of goods or hire-purchase agreement.

7. Miscellaneous contracts under which goods pass

(1) Where the possession or ownership of goods passes under or in pursuance of a contract not governed by the law of sale of goods or hire-purchase, subsections (2) to (4) below apply as regards the effect (if any) to be given to contract terms excluding or restricting liability for breach of obligation arising by implication of law from the nature of the contract.

(2) As against a person dealing as consumer, liability in respect of the goods' correspondence with description or sample, or their quality or fitness for any particular purpose, cannot be excluded or restricted by reference to any such term.

(3) As against a person dealing otherwise than as consumer, that liability can be excluded or restricted by reference to such a term, but only in so far as the term satisfies the requirement of reasonableness.

[(3A) Liability for breach of the obligations arising under section 2 of the Supply of Goods and Services Act 1982 (implied terms about title etc in certain contracts for the transfer of the property in goods) cannot be excluded or restricted by references to any such term.]

(4) Liability in respect of—

(a) the right to transfer ownership of the goods, or give possession; or

(b) the assurance of quiet possession to a person taking goods in pursuance of the contract,

cannot [(in a case to which subsection (3A) above does not apply)] be excluded or restricted by reference to any such term except in so far as the term satisfies the requirement of reasonableness.

(5) [...]

Other provisions about contracts

8. [...]

9. Effect of breach

(1) Where for reliance upon it a contract term has to satisfy the requirement of reasonableness, it may be found to do so and be given effect accordingly notwithstanding that the contract has been terminated either by breach or by a party electing to treat it as repudiated.

(2) Where on a breach the contract is nevertheless affirmed by a party entitled to treat it as repudiated, this does not of itself exclude the requirement of reasonableness in relation to any contract term.

10. Evasion by means of secondary contract

A person is not bound by any contract term prejudicing or taking away rights of his which arise under, or in connection with the performance of, another contract, so far as those rights extend to the enforcement of another's liability which this Part of this Act prevents that other from excluding or restricting.

Explanatory provisions

11. The "reasonableness" test

(1) In relation to a contract term, the requirement of reasonableness for the purposes of this Part of this Act, section 3 of the Misrepresentation Act 1967 and section 3 of the Misrepresentation Act (Northern Ireland) 1967 is that the term shall have been a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made.

(2) In determining for the purposes of section 6 or 7 above whether a contract term satisfies the requirement of reasonableness, regard shall be had in particular to the matters specified in Schedule 2 to this Act; but this subsection does not prevent the court or arbitrator from holding, in accordance with any rule of law, that a term which purports to exclude or restrict any relevant liability is not a term of the contract.

(3) In relation to a notice (not being a notice having contractual effect), the requirement of reasonableness under this Act is that it should be fair and reasonable to allow reliance on it, having regard to all the circumstances obtaining when the liability arose or (but for the notice) would have arisen.

(4) Where by reference to a contract term or notice a person seeks to restrict liability to a specified sum of money, and the question arises (under this or any other Act) whether the term or notice satisfies the requirement of reasonableness, regard shall be had in particular (but without prejudice to subsection (2) above in the case of contract terms) to—

- (a) the resources which he could expect to be available to him for the purpose of meeting the liability should it arise; and
- (b) how far it was open to him to cover himself by insurance.

(5) It is for those claiming that a contract term or notice satisfies the requirement of reasonableness to show that it does.

12. "Dealing as consumer"

- (1) A party to a contract "deals as consumer" in relation to another party if—
- (a) he neither makes the contract in the course of a business nor holds himself out as doing so; and
 - (b) the other party does make the contract in the course of a business; and
 - (c) in the case of a contract governed by the law of sale of goods or hire-purchase, or by section 7 of this Act, the goods passing under or in pursuance of the contract are of a type ordinarily supplied for private use or consumption.

[(1A) But if the first party mentioned in subsection (1) is an individual paragraph (c) of that subsection must be ignored.]

- [(2) But the buyer is not in any circumstances to be regarded as dealing as consumer—
- (a) if he is an individual and the goods are second hand goods sold at public auction at which individuals have the opportunity of attending the sale in person;
 - (b) if he is not an individual and the goods are sold by auction or by competitive tender.]

(3) Subject to this, it is for those claiming that a party does not deal as consumer to show that he does not.

13. Varieties of exemption clause

(1) To the extent that this Part of this Act prevents the exclusion or restriction of any liability it also prevents—

(a) making the liability or its enforcement subject to restrictive or onerous conditions;

(b) excluding or restricting any right or remedy in respect of the liability, or subjecting a person to any prejudice in consequence of his pursuing any such right or remedy;

(c) excluding or restricting rules of evidence or procedure;

and (to that extent) sections 2 and 5 to 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.

(2) But an agreement in writing to submit present or future differences to arbitration is not to be treated under this Part of this Act as excluding or restricting any liability.

14. Interpretation of Part I

In this Part of this Act—

“business” includes a profession and the activities of any government department or local or public authority;

“goods” has the same meaning as in [the Sale of Goods Act 1979];

“hire-purchase agreement” has the same meaning as in the Consumer Credit Act 1974;

“negligence” has the meaning given by section 1(1);

“notice” includes an announcement, whether or not in writing, and any other communication or pretended communication; and

“personal injury” includes any disease and any impairment of physical or mental condition.

PART II AMENDMENT OF LAW FOR SCOTLAND

[...]

PART III PROVISIONS APPLYING TO WHOLE OF UNITED KINGDOM

Miscellaneous

26. International supply contracts

(1) The limits imposed by this Act on the extent to which a person may exclude or restrict liability by reference to a contract term do not apply to liability arising under such a contract as is described in subsection (3) below.

(2) The terms of such a contract are not subject to any requirement of reasonableness under section 3 or 4: and nothing in Part II of this Act shall require the incorporation of the terms of such a contract to be fair and reasonable for them to have effect.

(3) Subject to subsection (4), that description of contract is one whose characteristics are the following—

- (a) either it is a contract of sale of goods or it is one under or in pursuance of which the possession or ownership of goods passes; and
- (b) it is made by parties whose places of business (or, if they have none, habitual residences) are in the territories of different States (the Channel Islands and the Isle of Man being treated for this purpose as different States from the United Kingdom).

(4) A contract falls within subsection (3) above only if either—

- (a) the goods in question are, at the time of the conclusion of the contract, in the course of carriage, or will be carried, from the territory of one State to the territory of another; or
- (b) the acts constituting the offer and acceptance have been done in the territories of different States; or
- (c) the contract provides for the goods to be delivered to the territory of a State other than that within whose territory those acts were done.

27. Choice of law clauses

(1) Where the [law applicable to] a contract is the law of any part of the United Kingdom only by choice of the parties (and apart from that choice would be the law of some country outside the United Kingdom) sections 2 to 7 and 16 to 21 of this Act do not operate as part [of the law applicable to the contract].

(2) This Act has effect notwithstanding any contract term which applies or purports to apply the law of some country outside the United Kingdom, where (either or both)—

- (a) the term appears to the court, or arbitrator or arbiter to have been imposed wholly or mainly for the purpose of enabling the party imposing it to evade the operation of this Act; or
- (b) in the making of the contract one of the parties dealt as consumer, and he was then habitually resident in the United Kingdom, and the essential steps necessary for the making of the contract were taken there, whether by him or by others on his behalf.

(3) In the application of subsection (2) above to Scotland, for paragraph (b) there shall be substituted—

- “(b) the contract is a consumer contract as defined in Part II of this Act, and the consumer at the date when the contract was made was habitually resident in the United Kingdom, and the essential steps necessary for the making of the contract were taken there, whether by him or by others on his behalf.”.

28. Temporary provision for sea carriage of passengers

(1) This section applies to a contract for carriage by sea of a passenger or of a passenger and his luggage where the provisions of the Athens Convention (with or without modification) do not have, in relation to the contract, the force of law in the United Kingdom.

(2) In a case where—

- (a) the contract is not made in the United Kingdom, and
- (b) neither the place of departure nor the place of destination under it is in the United Kingdom,

a person is not precluded by this Act from excluding or restricting liability for loss or damage, being loss or damage for which the provisions of the Convention would, if they had the force of law in relation to the contract, impose liability on him.

(3) In any other case, a person is not precluded by this Act from excluding or restricting liability for that loss or damage—

(a) in so far as the exclusion or restriction would have been effective in that case had the provisions of the Convention had the force of law in relation to the contract; or

(b) in such circumstances and to such extent as may be prescribed, by reference to a prescribed term of the contract.

(4) For the purposes of subsection (3)(a), the values which shall be taken to be the official values in the United Kingdom of the amounts (expressed in gold francs) by reference to which liability under the provisions of the Convention is limited shall be such amounts in sterling as the Secretary of State may from time to time by order made by statutory instrument specify.

(5) In this section,—

(a) the references to excluding or restricting liability include doing any of those things in relation to the liability which are mentioned in section 13 or section 25 (3) and (5); and

(b) “the Athens Convention” means the Athens Convention relating to the Carriage of Passengers and their Luggage by Sea, 1974; and

(c) “prescribed” means prescribed by the Secretary of State by regulations made by statutory instrument;

and a statutory instrument containing the regulations shall be subject to annulment in pursuance of a resolution of either House of Parliament.

29. Saving for other relevant legislation

(1) Nothing in this Act removes or restricts the effect of, or prevents reliance upon, any contractual provision which—

(a) is authorised or required by the express terms or necessary implication of an enactment; or

(b) being made with a view to compliance with an international agreement to which the United Kingdom is a party, does not operate more restrictively than is contemplated by the agreement.

(2) A contract term is to be taken—

(a) for the purposes of Part I of this Act, as satisfying the requirement of reasonableness; and

(b) for those of Part II, to have been fair and reasonable to incorporate, if it is incorporated or approved by, or incorporated pursuant to a decision or ruling of, a competent authority acting in the exercise of any statutory jurisdiction or function and is not a term in a contract to which the competent authority is itself a party.

(3) In this section—

“competent authority” means any court, arbitrator or arbiter, government department or public authority;

“enactment” means any legislation (including subordinate legislation) of the United Kingdom or Northern Ireland and any instrument having effect by virtue of such legislation; and

“statutory” means conferred by an enactment.

30. [...]

General

31. Commencement; amendments; repeals

- (1) This Act comes into force on 1st February 1978.
- (2) Nothing in this Act applies to contracts made before the date on which it comes into force; but subject to this, it applies to liability for any loss or damage which is suffered on or after that date.
- (3) The enactments specified in Schedule 3 to this Act are amended as there shown.
- (4) The enactments specified in Schedule 4 to this Act are repealed to the extent specified in column 3 of that Schedule.

32. Citation and extent

- (1) This Act may be cited as the Unfair Contract Terms Act 1977.
- (2) Part I of this Act extends to England and Wales and to Northern Ireland; but it does not extend to Scotland.
- (3) Part II of this Act extends to Scotland only.
- (4) This Part of this Act extends to the whole of the United Kingdom.

**SCHEDULE 1
SCOPE OF SECTIONS 2 TO 4 AND 7**

Section 1(2)

1.

Sections 2 to 4 of this Act do not extend to—

- (a) any contract of insurance (including a contract to pay an annuity on human life);
- (b) any contract so far as it relates to the creation or transfer of an interest in land, or to the termination of such an interest, whether by extinction, merger, surrender, forfeiture or otherwise;
- (c) any contract so far as it relates to the creation or transfer of a right or interest in any patent, trade mark, copyright [or design right], registered design, technical or commercial information or other intellectual property, or relates to the termination of any such right or interest;
- (d) any contract so far as it relates—
 - (i) to the formation or dissolution of a company (which means any body corporate or unincorporated association and includes a partnership), or
 - (ii) to its constitution or the rights or obligations of its corporators or members;

(e) any contract so far as it relates to the creation or transfer of securities or of any right or interest in securities.

2.

Section 2(1) extends to—

- (a) any contract of marine salvage or towage;
- (b) any charterparty of a ship or hovercraft; and
- (c) any contract for the carriage of goods by ship or hovercraft;

but subject to this sections 2 to 4 and 7 do not extend to any such contract except in favour of a person dealing as consumer.

3.

Where goods are carried by ship or hovercraft in pursuance of a contract which either—

- (a) specifies that as the means of carriage over part of the journey to be covered, or
- (b) makes no provision as to the means of carriage and does not exclude that means,

then sections 2(2), 3 and 4 do not, except in favour of a person dealing as consumer, extend to the contract as it operates for and in relation to the carriage of the goods by that means.

4.

Section 2(1) and (2) do not extend to a contract of employment, except in favour of the employee.

5.

Section 2(1) does not affect the validity of any discharge and indemnity given by a person, on or in connection with an award to him of compensation for pneumoconiosis attributable to employment in the coal industry, in respect of any further claim arising from his contracting that disease.

**SCHEDULE 2
"GUIDELINES" FOR APPLICATION OF REASONABLENESS TEST**

Sections 11(2), 24(2)

The matters to which regard is to be had in particular for the purposes of sections 6(3), 7(3) and (4), 20 and 21 are any of the following which appear to be relevant—

- (a) the strength of the bargaining positions of the parties relative to each other, taking into account (among other things) alternative means by which the customer's requirements could have been met;
- (b) whether the customer received an inducement to agree to the term, or in accepting it had an opportunity of entering into a similar contract with other persons, but without having to accept a similar term;
- (c) whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealing between the parties);
- (d) where the term excludes or restricts any relevant liability if some condition is not complied with, whether it was reasonable at the time of the contract to expect that compliance with that condition would be practicable;
- (e) whether the goods were manufactured, processed or adapted to the special order of the customer.

SCHEDULE 3

[...]

SCHEDULE 4

[...]

Appendix 2: Directive 93/13/EEC on Unfair Terms in Consumer Contracts

COUNCIL DIRECTIVE 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular Article 100 A thereof,

Having regard to the proposal from the Commission (1),

In cooperation with the European Parliament (2),

Having regard to the opinion of the Economic and Social Committee (3),

Whereas it is necessary to adopt measures with the aim of progressively establishing the internal market before 31 December 1992; whereas the internal market comprises an area without internal frontiers in which goods, persons, services and capital move freely;

Whereas the laws of Member States relating to the terms of contract between the seller of goods or supplier of services, on the one hand, and the consumer of them, on the other hand, show many disparities, with the result that the national markets for the sale of goods and services to consumers differ from each other and that distortions of competition may arise amongst the sellers and suppliers, notably when they sell and supply in other Member States;

Whereas, in particular, the laws of Member States relating to unfair terms in consumer contracts show marked divergences;

Whereas it is the responsibility of the Member States to ensure that contracts concluded with consumers do not contain unfair terms;

Whereas, generally speaking, consumers do not know the rules of law which, in Member States other than their own, govern contracts for the sale of goods or services; whereas this lack of awareness may deter them from direct transactions for the purchase of goods or services in another Member State;

Whereas, in order to facilitate the establishment of the internal market and to safeguard the citizen in his role as consumer when acquiring goods and services under contracts which are governed by the laws of Member States other than his own, it is essential to remove unfair terms from those contracts;

Whereas sellers of goods and suppliers of services will thereby be helped in their task of selling goods and supplying services, both at home and throughout the internal market; whereas competition will thus be stimulated, so contributing to increased choice for Community citizens as consumers;

Whereas the two Community programmes for a consumer protection and information policy (4) underlined the importance of safeguarding consumers in the matter of unfair terms of contract; whereas this protection ought to be provided by laws and

regulations which are either harmonized at Community level or adopted directly at that level;

Whereas in accordance with the principle laid down under the heading 'Protection of the economic interests of the consumers', as stated in those programmes: 'acquirers of goods and services should be protected against the abuse of power by the seller or supplier, in particular against one-sided standard contracts and the unfair exclusion of essential rights in contracts';

Whereas more effective protection of the consumer can be achieved by adopting uniform rules of law in the matter of unfair terms; whereas those rules should apply to all contracts concluded between sellers or suppliers and consumers; whereas as a result inter alia contracts relating to employment, contracts relating to succession rights, contracts relating to rights under family law and contracts relating to the incorporation and organization of companies or partnership agreements must be excluded from this Directive;

Whereas the consumer must receive equal protection under contracts concluded by word of mouth and written contracts regardless, in the latter case, of whether the terms of the contract are contained in one or more documents;

Whereas, however, as they now stand, national laws allow only partial harmonization to be envisaged; whereas, in particular, only contractual terms which have not been individually negotiated are covered by this Directive; whereas Member States should have the option, with due regard for the Treaty, to afford consumers a higher level of protection through national provisions that are more stringent than those of this Directive;

Whereas the statutory or regulatory provisions of the Member States which directly or indirectly determine the terms of consumer contracts are presumed not to contain unfair terms; whereas, therefore, it does not appear to be necessary to subject the terms which reflect mandatory statutory or regulatory provisions and the principles or provisions of international conventions to which the Member States or the Community are party; whereas in that respect the wording 'mandatory statutory or regulatory provisions' in Article 1 (2) also covers rules which, according to the law, shall apply between the contracting parties provided that no other arrangements have been established;

Whereas Member States must however ensure that unfair terms are not included, particularly because this Directive also applies to trades, business or professions of a public nature;

Whereas it is necessary to fix in a general way the criteria for assessing the unfair character of contract terms;

Whereas the assessment, according to the general criteria chosen, of the unfair character of terms, in particular in sale or supply activities of a public nature providing collective services which take account of solidarity among users, must be supplemented by a means of making an overall evaluation of the different interests involved; whereas this constitutes the requirement of good faith; whereas, in making an assessment of good faith, particular regard shall be had to the strength of the bargaining positions of the parties, whether the consumer had an inducement to agree to the term and whether the goods or services were sold or supplied to the special

order of the consumer; 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;

Whereas, for the purposes of this Directive, the annexed list of terms can be of indicative value only and, because of the cause of the minimal character of the Directive, the scope of these terms may be the subject of amplification or more restrictive editing by the Member States in their national laws;

Whereas the nature of goods or services should have an influence on assessing the unfairness of contractual terms;

Whereas, for the purposes of this Directive, assessment of unfair character shall not be made of terms which describe the main subject matter of the contract nor the quality/price ratio of the goods or services supplied; whereas the main subject matter of the contract and the price/quality ratio may nevertheless be taken into account in assessing the fairness of other terms; whereas it follows, inter alia, that in insurance contracts, the terms which clearly define or circumscribe the insured risk and the insurer's liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer;

Whereas contracts should be drafted in plain, intelligible language, the consumer should actually be given an opportunity to examine all the terms and, if in doubt, the interpretation most favourable to the consumer should prevail;

Whereas Member States should ensure that unfair terms are not used in contracts concluded with consumers by a seller or supplier and that if, nevertheless, such terms are so used, they will not bind the consumer, and the contract will continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair provisions;

Whereas there is a risk that, in certain cases, the consumer may be deprived of protection under this Directive by designating the law of a non-Member country as the law applicable to the contract; whereas provisions should therefore be included in this Directive designed to avert this risk;

Whereas persons or organizations, if regarded under the law of a Member State as having a legitimate interest in the matter, must have facilities for initiating proceedings concerning terms of contract drawn up for general use in contracts concluded with consumers, and in particular unfair terms, either before a court or before an administrative authority competent to decide upon complaints or to initiate appropriate legal proceedings; whereas this possibility does not, however, entail prior verification of the general conditions obtaining in individual economic sectors;

Whereas the courts or administrative authorities of the Member States must have at their disposal adequate and effective means of preventing the continued application of unfair terms in consumer contracts,

HAS ADOPTED THIS DIRECTIVE:

Article 1

1. The purpose of this Directive is to approximate the laws, regulations and administrative provisions of the Member States relating to unfair terms in contracts concluded between a seller or supplier and a consumer.
2. The contractual terms which reflect mandatory statutory or regulatory provisions and the provisions or principles of international conventions to which the Member States or the Community are party, particularly in the transport area, shall not be subject to the provisions of this Directive.

Article 2

For the purposes of this Directive:

- (a) 'unfair terms' means the contractual terms defined in Article 3;
- (b) 'consumer' means any natural person who, in contracts covered by this Directive, is acting for purposes which are outside his trade, business or profession;
- (c) 'seller or supplier' means any natural or legal person who, in contracts covered by this Directive, is acting for purposes relating to his trade, business or profession, whether publicly owned or privately owned.

Article 3

1. 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.
2. A term shall always be regarded as not individually negotiated where it has been drafted in advance and the consumer has therefore not been able to influence the substance of the term, particularly in the context of a pre-formulated standard contract.

The fact that certain aspects of a term or one specific term have been individually negotiated shall not exclude the application of this Article to the rest of a contract if an overall assessment of the contract indicates that it is nevertheless a pre-formulated standard contract.

Where any seller or supplier claims that a standard term has been individually negotiated, the burden of proof in this respect shall be incumbent on him.

3. The Annex shall contain an indicative and non-exhaustive list of the terms which may be regarded as unfair.

Article 4

1. Without prejudice to Article 7, the unfairness of a contractual term shall be assessed, taking into account the nature of the goods or services for which the contract was concluded and by referring, at the time of conclusion of the contract, to

all the circumstances attending the conclusion of the contract and to all the other terms of the contract or of another contract on which it is dependent.

2. Assessment of the unfair nature of the terms shall relate neither to the definition of the main subject matter of the contract nor to the adequacy of the price and remuneration, on the one hand, as against the services or goods supplied in exchange, on the other, in so far as these terms are in plain intelligible language.

Article 5

In the case of contracts where all or certain terms offered to the consumer are in writing, these terms must always be drafted in plain, intelligible language. Where there is doubt about the meaning of a term, the interpretation most favourable to the consumer shall prevail. This rule on interpretation shall not apply in the context of the procedures laid down in Article 7 (2).

Article 6

1. Member States shall lay down that unfair terms used in a contract concluded with a consumer by a seller or supplier shall, as provided for under their national law, not be binding on the consumer and that the contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms.

2. Member States shall take the necessary measures to ensure that the consumer does not lose the protection granted by this Directive by virtue of the choice of the law of a non-Member country as the law applicable to the contract if the latter has a close connection with the territory of the Member States.

Article 7

1. Member States shall ensure that, in the interests of consumers and of competitors, adequate and effective means exist to prevent the continued use of unfair terms in contracts concluded with consumers by sellers or suppliers.

2. The means referred to in paragraph 1 shall include provisions whereby persons or organizations, having a legitimate interest under national law in protecting consumers, may take action according to the national law concerned before the courts or before competent administrative bodies for a decision as to whether contractual terms drawn up for general use are unfair, so that they can apply appropriate and effective means to prevent the continued use of such terms.

3. With due regard for national laws, the legal remedies referred to in paragraph 2 may be directed separately or jointly against a number of sellers or suppliers from the same economic sector or their associations which use or recommend the use of the same general contractual terms or similar terms.

Article 8

Member States may adopt or retain the most stringent provisions compatible with the Treaty in the area covered by this Directive, to ensure a maximum degree of protection for the consumer.

Article 9

The Commission shall present a report to the European Parliament and to the Council concerning the application of this Directive five years at the latest after the date in Article 10 (1).

Article 10

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive no later than 31 December 1994. They shall forthwith inform the Commission thereof.

These provisions shall be applicable to all contracts concluded after 31 December 1994.

2. When Member States adopt these measures, they shall contain a reference to this Directive or shall be accompanied by such reference on the occasion of their official publication. The methods of making such a reference shall be laid down by the Member States.

3. Member States shall communicate the main provisions of national law which they adopt in the field covered by this Directive to the Commission.

Article 11

This Directive is addressed to the Member States.

Done at Luxembourg, 5 April 1993.

For the Council

The President
N. HELVEG PETERSEN

(1) OJ No C 73, 24. 3. 1992, p. 7.

(2) OJ No C 326, 16. 12. 1991, p. 108 and OJ No C 21, 25. 1. 1993.

(3) OJ No C 159, 17. 6. 1991, p. 34.

(4) OJ No C 92, 25. 4. 1975, p. 1 and OJ No C 133, 3. 6. 1981, p. 1.

ANNEX

TERMS REFERRED TO IN ARTICLE 3 (3) 1. Terms which have the object or effect of:

(a) excluding or limiting the legal liability of a seller or supplier in the event of the death of a consumer or personal injury to the latter resulting from an act or omission of that seller or supplier;

(b) inappropriately excluding or limiting the legal rights of the consumer vis-à-vis the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him;

- (c) making an agreement binding on the consumer whereas provision of services by the seller or supplier is subject to a condition whose realization depends on his own will alone;
- (d) permitting the seller or supplier to retain sums paid by the consumer where the latter decides not to conclude or perform the contract, without providing for the consumer to receive compensation of an equivalent amount from the seller or supplier where the latter is the party cancelling the contract;
- (e) requiring any consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation;
- (f) authorizing the seller or supplier to dissolve the contract on a discretionary basis where the same facility is not granted to the consumer, or permitting the seller or supplier to retain the sums paid for services not yet supplied by him where it is the seller or supplier himself who dissolves the contract;
- (g) enabling the seller or supplier to terminate a contract of indeterminate duration without reasonable notice except where there are serious grounds for doing so;
- (h) automatically extending a contract of fixed duration where the consumer does not indicate otherwise, when the deadline fixed for the consumer to express this desire not to extend the contract is unreasonably early;
- (i) irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract;
- (j) enabling the seller or supplier to alter the terms of the contract unilaterally without a valid reason which is specified in the contract;
- (k) enabling the seller or supplier to alter unilaterally without a valid reason any characteristics of the product or service to be provided;
- (l) providing for the price of goods to be determined at the time of delivery or allowing a seller of goods or supplier of services to increase their price without in both cases giving the consumer the corresponding right to cancel the contract if the final price is too high in relation to the price agreed when the contract was concluded;
- (m) giving the seller or supplier the right to determine whether the goods or services supplied are in conformity with the contract, or giving him the exclusive right to interpret any term of the contract;
- (n) limiting the seller's or supplier's obligation to respect commitments undertaken by his agents or making his commitments subject to compliance with a particular formality;
- (o) obliging the consumer to fulfil all his obligations where the seller or supplier does not perform his;
- (p) giving the seller or supplier the possibility of transferring his rights and obligations under the contract, where this may serve to reduce the guarantees for the consumer, without the latter's agreement;

(q) excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract.

2. Scope of subparagraphs (g), (j) and (l)

(a) Subparagraph (g) is without hindrance to terms by which a supplier of financial services reserves the right to terminate unilaterally a contract of indeterminate duration without notice where there is a valid reason, provided that the supplier is required to inform the other contracting party or parties thereof immediately.

(b) Subparagraph (j) is without hindrance to terms under which a supplier of financial services reserves the right to alter the rate of interest payable by the consumer or due to the latter, or the amount of other charges for financial services without notice where there is a valid reason, provided that the supplier is required to inform the other contracting party or parties thereof at the earliest opportunity and that the latter are free to dissolve the contract immediately.

Subparagraph (j) is also without hindrance to terms under which a seller or supplier reserves the right to alter unilaterally the conditions of a contract of indeterminate duration, provided that he is required to inform the consumer with reasonable notice and that the consumer is free to dissolve the contract.

(c) Subparagraphs (g), (j) and (l) do not apply to:

- transactions in transferable securities, financial instruments and other products or services where the price is linked to fluctuations in a stock exchange quotation or index or a financial market rate that the seller or supplier does not control;
- contracts for the purchase or sale of foreign currency, traveller's cheques or international money orders denominated in foreign currency;

(d) Subparagraph (l) is without hindrance to price-indexation clauses, where lawful, provided that the method by which prices vary is explicitly described.

Appendix 3: Unfair Terms in Consumer Contracts Regulations 1999

THE UNFAIR TERMS IN CONSUMER CONTRACTS REGULATIONS 1999

Whereas the Secretary of State is a Minister designated for the purposes of section 2(2) of the European Communities Act 1972 in relation to measures relating to consumer protection:

Now, the Secretary of State, in exercise of the powers conferred upon him by section 2(2) of that Act, hereby makes the following Regulations:-

1. Citation and commencement

These Regulations may be cited as the Unfair Terms in Consumer Contracts Regulations 1999 and shall come into force on 1st October 1999.

2. Revocation

The Unfair Terms in Consumer Contracts Regulations 1994 are hereby revoked.

3. Interpretation

(1) In these Regulations-

"the Community" means the European Community;

"consumer" means any natural person who, in contracts covered by these Regulations, is acting for purposes which are outside his trade, business or profession;

"court" in relation to England and Wales and Northern Ireland means a county court or the High Court, and in relation to Scotland, the Sheriff or the Court of Session;

"Director" means the Director General of Fair Trading;

"EEA Agreement" means the Agreement on the European Economic Area signed at Oporto on 2nd May 1992 as adjusted by the protocol signed at Brussels on 17th March 1993;

"Member State" means a State which is a contracting party to the EEA Agreement;

"notified" means notified in writing;

"qualifying body" means a person specified in Schedule 1;

"seller or supplier" means any natural or legal person who, in contracts covered by these Regulations, is acting for purposes relating to his trade, business or profession, whether publicly owned or privately owned;

"unfair terms" means the contractual terms referred to in regulation 5.

(2) In the application of these Regulations to Scotland for references to an "injunction" or an "interim injunction" there shall be substituted references to an "interdict" or "interim interdict" respectively.

4. Terms to which these Regulations apply

(1) These Regulations apply in relation to unfair terms in contracts concluded between a seller or a supplier and a consumer.

(2) These Regulations do not apply to contractual terms which reflect-

(a) mandatory statutory or regulatory provisions (including such provisions under the law of any Member State or in Community legislation having effect in the United Kingdom without further enactment);

(b) the provisions or principles of international conventions to which the Member States or the Community are party.

5. Unfair Terms

(1) 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.

(2) A term shall always be regarded as not having been individually negotiated where it has been drafted in advance and the consumer has therefore not been able to influence the substance of the term.

(3) Notwithstanding that a specific term or certain aspects of it in a contract has been individually negotiated, these Regulations shall apply to the rest of a contract if an overall assessment of it indicates that it is a pre-formulated standard contract.

(4) It shall be for any seller or supplier who claims that a term was individually negotiated to show that it was.

(5) Schedule 2 to these Regulations contains an indicative and non-exhaustive list of the terms which may be regarded as unfair.

6. Assessment of unfair terms

(1) Without prejudice to regulation 12, the unfairness of a contractual term shall be assessed, taking into account the nature of the goods or services for which the contract was concluded and by referring, at the time of conclusion of the contract, to all the circumstances attending the conclusion of the contract and to all the other terms of the contract or of another contract on which it is dependent.

(2) In so far as it is in plain intelligible language, the assessment of fairness of a term shall not relate-

(a) to the definition of the main subject matter of the contract, or

(b) to the adequacy of the price or remuneration, as against the goods or services supplied in exchange.

7. Written contracts

(1) A seller or supplier shall ensure that any written term of a contract is expressed in plain, intelligible language.

(2) If there is doubt about the meaning of a written term, the interpretation which is most favourable to the consumer shall prevail but this rule shall not apply in proceedings brought under regulation 12.

8. Effect of unfair term

- (1) An unfair term in a contract concluded with a consumer by a seller or supplier shall not be binding on the consumer.
- (2) The contract shall continue to bind the parties if it is capable of continuing in existence without the unfair term.

9. Choice of law clauses

These Regulations shall apply notwithstanding any contract term which applies or purports to apply the law of a non-Member State, if the contract has a close connection with the territory of the Member States.

10. Complaints - consideration by Director

- (1) It shall be the duty of the Director to consider any complaint made to him that any contract term drawn up for general use is unfair, unless-
 - (a) the complaint appears to the Director to be frivolous or vexatious; or
 - (b) a qualifying body has notified the Director that it agrees to consider the complaint.
- (2) The Director shall give reasons for his decision to apply or not to apply, as the case may be, for an injunction under regulation 12 in relation to any complaint which these Regulations require him to consider.
- (3) In deciding whether or not to apply for an injunction in respect of a term which the Director considers to be unfair, he may, if he considers it appropriate to do so, have regard to any undertakings given to him by or on behalf of any person as to the continued use of such a term in contracts concluded with consumers.

11. Complaints - consideration by qualifying bodies

- (1) If a qualifying body specified in Part One of Schedule 1 notifies the Director that it agrees to consider a complaint that any contract term drawn up for general use is unfair, it shall be under a duty to consider that complaint.
- (2) Regulation 10(2) and (3) shall apply to a qualifying body which is under a duty to consider a complaint as they apply to the Director.

12. Injunctions to prevent continued use of unfair terms

- (1) The Director or, subject to paragraph (2), any qualifying body may apply for an injunction (including an interim injunction) against any person appearing to the Director or that body to be using, or recommending use of, an unfair term drawn up for general use in contracts concluded with consumers.
- (2) A qualifying body may apply for an injunction only where-
 - (a) it has notified the Director of its intention to apply at least fourteen days before the date on which the application is made, beginning with the date on which the notification was given; or
 - (b) the Director consents to the application being made within a shorter period.

(3) The court on an application under this regulation may grant an injunction on such terms as it thinks fit.

(4) An injunction may relate not only to use of a particular contract term drawn up for general use but to any similar term, or a term having like effect, used or recommended for use by any person.

13. Powers of the Director and qualifying bodies to obtain documents and information

(1) The Director may exercise the power conferred by this regulation for the purpose of-

- (a) facilitating his consideration of a complaint that a contract term drawn up for general use is unfair; or

- (b) ascertaining whether a person has complied with an undertaking or court order as to the continued use, or recommendation for use, of a term in contracts concluded with consumers.

(2) A qualifying body specified in Part One of Schedule 1 may exercise the power conferred by this regulation for the purpose of-

- (a) facilitating its consideration of a complaint that a contract term drawn up for general use is unfair; or

- (b) ascertaining whether a person has complied with-

- (i) an undertaking given to it or to the court following an application by that body, or

- (ii) a court order made on an application by that body,

as to the continued use, or recommendation for use, of a term in contracts concluded with consumers.

(3) The Director may require any person to supply to him, and a qualifying body specified in Part One of Schedule 1 may require any person to supply to it-

- (a) a copy of any document which that person has used or recommended for use, at the time the notice referred to in paragraph (4) below is given, as a pre-formulated standard contract in dealings with consumers;

- (b) information about the use, or recommendation for use, by that person of that document or any other such document in dealings with consumers.

(4) The power conferred by this regulation is to be exercised by a notice in writing which may-

- (a) specify the way in which and the time within which it is to be complied with; and

- (b) be varied or revoked by a subsequent notice.

(5) Nothing in this regulation compels a person to supply any document or information which he would be entitled to refuse to produce or give in civil proceedings before the court.

(6) If a person makes default in complying with a notice under this regulation, the court may, on the application of the Director or of the qualifying body, make such order as the court thinks fit for requiring the default to be made good, and any such order may provide that all the costs or expenses of and incidental to the application shall be borne by the person in default or by any officers of a company or other association who are responsible for its default.

14. Notification of undertakings and orders to Director

A qualifying body shall notify the Director-

- (a) of any undertaking given to it by or on behalf of any person as to the continued use of a term which that body considers to be unfair in contracts concluded with consumers;
- (b) of the outcome of any application made by it under regulation 12, and of the terms of any undertaking given to, or order made by, the court;
- (c) of the outcome of any application made by it to enforce a previous order of the court.

15. Publication, information and advice

(1) The Director shall arrange for the publication in such form and manner as he considers appropriate, of-

- (a) details of any undertaking or order notified to him under regulation 14;
- (b) details of any undertaking given to him by or on behalf of any person as to the continued use of a term which the Director considers to be unfair in contracts concluded with consumers;
- (c) details of any application made by him under regulation 12, and of the terms of any undertaking given to, or order made by, the court;
- (d) details of any application made by the Director to enforce a previous order of the court.

(2) The Director shall inform any person on request whether a particular term to which these Regulations apply has been-

- (a) the subject of an undertaking given to the Director or notified to him by a qualifying body; or
- (b) the subject of an order of the court made upon application by him or notified to him by a qualifying body;

and shall give that person details of the undertaking or a copy of the order, as the case may be, together with a copy of any amendments which the person giving the undertaking has agreed to make to the term in question.

(3) The Director may arrange for the dissemination in such form and manner as he considers appropriate of such information and advice concerning the operation of these Regulations as may appear to him to be expedient to give to the public and to all persons likely to be affected by these Regulations.

SCHEDULE 1
QUALIFYING BODIES

Regulation 3

PART ONE

1. The Information Commissioner.
2. The Gas and Electricity Markets Authority.
3. The Director General of Electricity Supply for Northern Ireland.
4. The Director General of Gas for Northern Ireland.
5. The Director General of Telecommunications.
6. The Director General of Water Services.
7. The Rail Regulator.
8. Every weights and measures authority in Great Britain.
9. The Department of Enterprise, Trade and Investment in Northern Ireland.
10. The Financial Services Authority.

PART TWO

11. Consumers' Association.

SCHEDULE 2

**INDICATIVE AND NON-EXHAUSTIVE LIST OF TERMS WHICH MAY BE
REGARDED AS UNFAIR**

Regulation 5(5)

1. Terms which have the object or effect of-

(a) excluding or limiting the legal liability of a seller or supplier in the event of the death of a consumer or personal injury to the latter resulting from an act or omission of that seller or supplier;

(b) inappropriately excluding or limiting the legal rights of the consumer vis-à-vis the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him;

(c) making an agreement binding on the consumer whereas provision of services by the seller or supplier is subject to a condition whose realisation depends on his

own will alone;

(d) permitting the seller or supplier to retain sums paid by the consumer where the latter decides not to conclude or perform the contract, without providing for the consumer to receive compensation of an equivalent amount from the seller or supplier where the latter is the party cancelling the contract;

(e) requiring any consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation;

(f) authorising the seller or supplier to dissolve the contract on a discretionary basis where the same facility is not granted to the consumer, or permitting the seller or supplier to retain the sums paid for services not yet supplied by him where it is the seller or supplier himself who dissolves the contract;

(g) enabling the seller or supplier to terminate a contract of indeterminate duration without reasonable notice except where there are serious grounds for doing so;

(h) automatically extending a contract of fixed duration where the consumer does not indicate otherwise, when the deadline fixed for the consumer to express his desire not to extend the contract is unreasonably early;

(i) irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract;

(j) enabling the seller or supplier to alter the terms of the contract unilaterally without a valid reason which is specified in the contract;

(k) enabling the seller or supplier to alter unilaterally without a valid reason any characteristics of the product or service to be provided;

(l) providing for the price of goods to be determined at the time of delivery or allowing a seller of goods or supplier of services to increase their price without in both cases giving the consumer the corresponding right to cancel the contract if the final price is too high in relation to the price agreed when the contract was concluded;

(m) giving the seller or supplier the right to determine whether the goods or services supplied are in conformity with the contract, or giving him the exclusive right to interpret any term of the contract;

(n) limiting the seller's or supplier's obligation to respect commitments undertaken by his agents or making his commitments subject to compliance with a particular formality;

(o) obliging the consumer to fulfil all his obligations where the seller or supplier does not perform his;

(p) giving the seller or supplier the possibility of transferring his rights and obligations under the contract, where this may serve to reduce the guarantees for the consumer, without the latter's agreement;

(q) excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract.

2. Scope of paragraphs 1(g), (j) and (l)

(a) Paragraph 1(g) is without hindrance to terms by which a supplier of financial services reserves the right to terminate unilaterally a contract of indeterminate duration without notice where there is a valid reason, provided that the supplier is required to inform the other contracting party or parties thereof immediately.

(b) Paragraph 1(j) is without hindrance to terms under which a supplier of financial services reserves the right to alter the rate of interest payable by the consumer or due to the latter, or the amount of other charges for financial services without notice where there is a valid reason, provided that the supplier is required to inform the other contracting party or parties thereof at the earliest opportunity and that the latter are free to dissolve the contract immediately.

Paragraph 1(j) is also without hindrance to terms under which a seller or supplier reserves the right to alter unilaterally the conditions of a contract of indeterminate duration, provided that he is required to inform the consumer with reasonable notice and that the consumer is free to dissolve the contract.

(c) Paragraphs 1(g), (j) and (l) do not apply to:

- transactions in transferable securities, financial instruments and other products or services where the price is linked to fluctuations in a stock exchange quotation or index or a financial market rate that the seller or supplier does not control;
- contracts for the purchase or sale of foreign currency, traveller's cheques or international money orders denominated in foreign currency;

(d) Paragraph 1(l) is without hindrance to price indexation clauses, where lawful, provided that the method by which prices vary is explicitly described.