

# THE ECONOMICS OF CIVIL LAW CONTRACT AND OF GOOD FAITH

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## SUMMARY

In his 1993 book on the Limits of Freedom of Contract, Michael Trebilcock acknowledged the difficulties of trying to set criteria for correcting informational asymmetries. Informational asymmetries are one opening for opportunism and it has been generally acknowledged that one of the fundamental objectives of legal systems is to curtail opportunism. A civil-code based legal system has the ambition of being closed, i.e. covering all difficulties in private relationships within its purview. To accomplish this, it has to rely on open-ended concepts that can be used in unforeseen circumstances; yet legal certainty requires that such concepts be used sparingly and that recurrent circumstances calling for their application be particularised into more specific concepts having their own more detailed legal regime. The paper seeks to make the case that good faith in civil law systems is the exact opposite of opportunism; that it is one of the residual open-ended concepts 'closing' the system; and that it is particularised in a number of civil code concepts. These developments allow us to illustrate the difficulties Michael foretold in his book.

## INTRODUCTION

Michael Trebilcock is truly the founding father of law and economics in Canada. He brought it here in the mid-1970s and has made law and economics programme at the University of Toronto the lighthouse for law and economics in the country. Over the years he has inspired generations of lawyers to take an active interest in the approach. He has published widely himself and his work has had spin-offs in many publications by others. One of these spin-offs is the first French-language treatise of law and economics, which Stéphane Rousseau and I published in 2008 and in which we acknowledge our debt to Michael.<sup>1</sup> What has struck both of us are the breadth of scholarship and the non-doctrinaire approach Michael brought to the field. We have wanted to carry this spirit over into civil law systems.

Civil law countries have been slower than common law countries to take to law and economics, but currently there is a lively interest in the German and Dutch-speaking countries as well as in Italy. Interest in these countries is comparable to that in Canada, Britain, Australia and New Zealand. The United States remains the country in which law and economics has had by far the most enthusiastic reception: the American exception. Amongst civil law countries, France has been amongst the slowest to take to law and economics: the French exception..

For a long time, French scholarship took it as axiomatic that law and economics, being policy-oriented, had nothing to say to civil law thinking, based as it was held to be on moral judgement and the interpretation of Codes. Most of the older French scholars did not read English. They would frown upon theses engaging in comparative law and would make sure that young prospective colleagues at the *concours d'agrégation* (a national vetting procedure for future professors) would not stray from received wisdom. Writings by economists attempting to set out law and economics to French lawyers were dismissed as *corpora extranea*. There was little that could disturb this inward-looking view. All quiet on the Western front ...

Recently there have been signs of a change of mentality, perhaps induced by pan-European initiatives in contract and tort law where law and economics and English are the languages in which comparison and harmonisation is conducted.

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<sup>1</sup> Mackaay/Rousseau 2008, XXII.

In writing our book, Stéphane Rousseau and I wanted to be part of that change, but were also keenly aware of the constraints we faced particularly in the French market, France being the centre of gravity in the French-speaking world.<sup>2</sup> We consciously aimed for a text that would be understandable to lawyers and legal scholars in all French-speaking countries, the Quebec market being simply too small. We wrote as lawyers for (French-speaking) lawyers in their own language using Code articles and cases drawn from civil-law systems to argue that law and economics has as much to say to civil lawyers as it has to their common law colleagues. The reactions to the book suggest that the message is now being received in France.<sup>3</sup>

## PRELIMINARY THOUGHTS: ON CIVIL LAW SYSTEMS

It is interesting to reflect for a moment on the special features of civil law systems: they will have to be accounted for in a law and economics perspective. What sets civil law systems apart from common law systems, besides differences in vocabulary, is that their core rules are set out in codes drafted with the aim of covering in principle all relationships within the field of law they govern. All legal problems arising within that field are deemed to be soluble by reference to, and through interpretation of, one or more articles of the Code.

Codes consolidate the solutions found to a great many practical problems that have arisen over time; but it would be illusory to expect them to provide ready-made solutions to all conceivable problems. To cope with novel or imperfectly foreseen problems, all the while maintaining the claim to complete coverage, Codes must resort to some open-ended concepts to fashion appropriate solutions to such problems on the fly. Good faith and abuse of rights are two such concepts.

One of the main objectives of codification in civilian legal systems is to make law accessible: all the law for a given field is in principle to be found in one place – the Code – rather than in a proliferation of individual judicial decisions. Codes should make it easier for citizens to know their rights and obligations. To

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<sup>2</sup> Mackaay 2008.

<sup>3</sup> See in particular Chérot/Bergel 2008.

accomplish this, the codes need to be relatively compact. The formulas used have to be concise and often abstract, condensing large arrays of practical solutions. The code's articles should be interpreted on the premise that they form a coherent and seamless whole.

One should not be misled by the abstract character of Code articles or by the idea of the Code as a system. Codes are not systems of abstract logic unconnected with the real world; they are meant to reflect consolidated experience. To work effectively with such tools, civil lawyers need to be (made) aware of the variety of actual cases each code article is meant to capture as much as common lawyers need to be cognizant of all the judicial decisions on a particular point of law.

Once these general characteristics are taken into consideration, the economic analysis of law should have as much to tell lawyers in civil law systems as it has those in common law systems, and in the American legal system in particular. The Legal Origins movement has put forth the thesis that common law systems are more conducive to economic growth than civil law systems,<sup>4</sup> but this conclusion has been contested<sup>5</sup> and a very recent paper has highlighted how the imposition of the institutions of the French Revolution, including its civil code, on other European nations helped to clear rent-seeking barriers to trade.<sup>6</sup> On the whole, the jury seems to be still out on the comparative virtues of different legal families.

## I. THE GENERAL FUNCTION OF CONTRACT LAW

Of the many fields Michael touched upon in his writings, it is contract law I want to take a closer look at. Michael's major contribution to that field is *The Limits of Freedom of Contract*, published in 1993 and still widely cited. Early in the book four major functions of contract law are identified as:

- Containing opportunism in Non-Simultaneous Exchanges
- Reducing Transaction Costs
- Filling Gaps in Incomplete Contracts

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<sup>4</sup> La Porta et al. 1998; 1999; 2008.

<sup>5</sup> Dam 2006; Roe 2006; Milhaupt/Pistor 2008; survey: Mackaay 2009.

<sup>6</sup> Acemoglu et al. 2009.

- Distinguishing Welfare-Enhancing and Welfare-Reducing Exchanges.<sup>7</sup>

Similar lists of functions appear in the standard textbooks. Posner sees five distinct economic functions:

- (1) to prevent opportunism
- (2) to interpolate efficient terms either on a wholesale or a retail basis (gap-filling versus ad hoc interpretation)
- (3) to punish avoidable mistakes in the contracting process
- (4) to allocate risk to the superior risk bearer
- (5) to reduce the costs of resolving contract disputes.<sup>8</sup>

Cooter and Ulen list six purposes:

1. to enable people to cooperate by converting games with noncooperative solutions into games with cooperative solutions.
2. to encourage the efficient disclosure of information within the contractual relationship.
3. to secure optimal commitment to performing
4. to secure optimal reliance
5. to minimize transaction costs of negotiating contracts by supplying efficient default terms and regulations
6. to foster enduring relationships, which solve the problem of cooperation with less reliance on the courts to enforce contracts.<sup>9</sup>

Such diverging shopping lists would strike civil lawyers, trained as they are to mull over abstract principles, as untidy. Can we bring all these functions on a common denominator, using the tools of law and economics? That is a first question to look at, in this section (I). On closer inspection, the lists raises another problem. Do we know what we mean by opportunism that law is meant to contain? That turns out to be less trivial than one might have thought (II).

On an economic view, contract is an open-ended institution by which individual actors can exchange resources to their mutual advantage, thereby moving them to higher-valued uses. In the consensualist conception of contract,

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<sup>7</sup> Trebilcock 1993, 16-17.

<sup>8</sup> Posner 2007, 99 (§ 4.1).

<sup>9</sup> Cooter/Ulen 2007, 232.

parties can do this essentially in any form they see fit. What then is the role of contract *law*? Parties need no encouragement to enter into profitable deals. But the law may be called upon to avoid mishaps in the contracting process or to reduce their seriousness: for instance, one party being taken advantage of by the other, at the time of contracting or later, as a result of unforeseen circumstances; or a division of tasks or risks between the parties which experience suggests is less than optimal.

The first defence against mishaps falls to the parties themselves. Economic theory predicts that to avoid mishaps in the contracting process each party, being a rational actor, will take all precautions whose cost is lower than the trouble so avoided, discounted by the probability of its occurrence. This is the logic of accident avoidance, which forms the basis of the economic analysis of accident law. The idea can be expressed equivalently as each party seeking to minimise the sum of the costs of precautions it takes to prevent mishaps and those of the mishaps that it could not profitably prevent and hence must simply absorb. This sum are the transactions costs for that party. Rational actors will only enter into a contract if these transaction costs are more than offset by the gains the contract promises.

Both parties will seek the optimal set-up from their own point of view. They will inform themselves on the prospective contracting partner, on the product contemplated and on the terms on which it is offered. If the information collected on prospective contracting partners is too sketchy for comfort, a party may limit dealings to a smaller circle of people on which more information can be gleaned or who particularly inspire confidence, for instance because of ethnic ties. Where the performance of a contract looks uncertain, a party may insist on being given security or a guarantor or again an express warranty that the product will meet specific requirements. Of course providing securities or guarantees entails a cost, which must be covered by the gains the party providing them expects to realise by the contract. If these or similar precautions are not viable or too costly, given what is at stake, or if they leave too high a margin of residual risk of mishap, a party may take the ultimate precaution not to contract at all. This entails the opportunity cost of the net gains of the contract foregone, which, one may surmise, the abstaining party considers to be negative.

During their negotiations, parties may further reduce the risk of mishaps or non-optimal arrangements by exchanging information and shifting burdens or risks between them, allocating them to the one that can take care of them at the

lowest cost. When you order a book at Amazon, they will look after the shipping, even though you pay for it: Amazon has access to very considerable scale economies in these matters.

Parties arrive thus at the best arrangement they can fashion between themselves. This may still leave a substantial margin of risks of mishaps and a considerable level of precautions to avoid them. Can contract law improve upon this, leading parties to 'lower their guard'?

Corrective intervention through contract law is justified whenever the cost of the intervention is more than offset by the savings in transaction costs it generates compared to what the contracting parties could themselves achieve, in other words whenever it allows parties so to lower their guard that their savings are greater than the cost of the measure itself. Wittman states this idea by the simple formula that

'[i]n a nutshell, the role of contract law is to minimize the cost of the parties writing contracts + the costs of the courts writing contracts + the cost of inefficient behavior arising from poorly written or incomplete contracts.'<sup>10</sup>

This amounts to saying that contract law aims at minimising the overall cost of mishaps and their prevention in contract.

Of the three terms of the Wittman test, the first and the third have already been looked at in the discussion of the role of contracting parties, with the difference that they are here to be taken at the level of society as a whole, for all contracting parties together. The first term refers to measures taken by the parties themselves, individually and in negotiation, to find the best arrangement – for instance in allocating risks or other burdens – and to avoid bad surprises. The third term refers to mishaps that the parties have been unable to avoid, that is arrangements that contrary to expectations turn out to be non-optimal or bad surprises that looked too costly to prevent beforehand and whose cost must be absorbed afterwards, for instance the opportunistic exploitation of a gap left in the contract.

The middle term indicates that public intervention is worthwhile if it reduces the sum of the three terms, that is if its own cost is lower than the savings to which it gives rise in the other two terms. These considerations apply to all contracting parties taken together, rather than at their individual level. Admittedly, the test is not immediately operational; it points nonetheless to what should be

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<sup>10</sup> Wittman 2006, 194.

weighed in asking what the law should and should not tackle.

Consider, by way of example, the court system allowing contracts to be enforced. In the absence of such a system, breach of a contract can certainly be punished or avoided up front, by a private system based on arbitration and community sanctions such as blacklisting or exclusion. In such a private set-up, actors only contract with persons they know or against whom community sanctions will be effective. Putting in place a system of public enforcement means betting on substantial gains resulting from people daring to do business with a larger circle of persons: the gains from more numerous and more widely distributed contracts plus the savings in self-protection measures contracting parties would normally take are sufficient to offset the fixed cost of the public enforcement system plus the variable costs of contracting parties using its services. Of course, the very presence of a public enforcement system, even where people do not generally have recourse to it, casts its shadow on the temptation of contracting parties to behave opportunistically and this in itself represents a saving.

To take another example, by instituting a regime of mandatory warranties in the sale of manufactured goods, one is implicitly betting that the savings generated for a large proportion of consumers in lowered self-protection and bad surprises avoided largely offset the losses resulting for a smaller proportion of consumers of contracts that are no longer feasible or, because of the inflexibility of the general rule, have to be entered into on less advantageous terms than parties would have liked. Empirically, it may turn out that numbers are different from what proponents of the measure had in mind, as Priest discovered in early studies of mandatory warranties.<sup>11</sup>

What are the costs of a legal rule? They vary depending on whether one is dealing with a mandatory rule (public order – parties cannot opt out of it) or with a suppletive or default rule (parties may agree otherwise). A public order rule seeks to counter opportunism; by providing a fixed and enforceable rule, it is designed to allow a substantial proportion of citizens to lower the level of self-protection they consider required in given circumstances, but at the cost of reducing the negotiation space for all, which will particularly hamper those who were willing to assume greater risk in exchange for more advantageous terms, especially price.

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<sup>11</sup> Priest 1978; 1981.



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The costs of a public order or mandatory rule (*ius imperativum*) include:

1. the cost of framing the rule legislatively or judicially, including the risk of capture by interest groups (rent-seeking) in the case of the political process;
2. the cost for the parties of enforcing their rights using public procedures the rule points to;
3. the opportunity cost of 'sharper deals' foregone because they are prohibited by the rule;
4. the cost of the rule turning out on experience to be ill-suited for the problem it was designed to regulate.

Taken together these costs must be more than offset by the gains the rule generates in terms of people 'lowering their guard' (reducing self-protection), contracting with a wider circle of persons and absorbing residual risk.

In the case of a default or suppletive rule (*ius dispositivum*), the stakes are slightly different because parties are now free to put it aside, but must take the trouble (and expense) of doing so. Essentially of the four factors listed, the third factor falls away under a suppletive rule. However, this may be illusory if the cost of opting out and framing one's own rule is practically prohibitive, in which case the rule has to all intents a public order character. Since citizens are free to opt out, the fourth factor should now be called 'undue reliance' on a rule that turns out to be ill suited. Usually, default rules propose a solution that experience suggests parties would have chosen had they taken the time to contract about it explicitly.

Any rule that promises gains from more ample contracting and savings in transactions costs of private parties in excess of its own cost as just specified – net gains, in other words – has a proper place in the law of contract; the Wittman test implies that where several competing rules are conceivable for the same subject matter, the one promising the highest net gain should have preference. In this light, it is easy to agree with Michael's observation that structural problems in contracting be handled by regulation or antitrust laws, situational problems by fine tinkering that courts can engage in.<sup>12</sup> One must expect such gains where public authorities have access to greater scale economies in framing and enforcing rules than are open to private actors. A broad principle reflected in many rules is to attribute a burden to the party who can best or most cheaply

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<sup>12</sup> Trebilock 1993, 101

influence the occurrence or cost of a mishap. Calabresi has proposed the term ‘cheapest cost avoider’ for this principle.<sup>13</sup> A good deal of civil contract law appears explicable as applications of the ‘cheapest cost avoider’ principle.<sup>14</sup>

The Wittman test seems to express the logic underlying the more detailed objectives of contract law listed above, such as preventing opportunism, reducing transaction costs, interpolating efficient terms, punishing avoidable mistakes in the contracting process, allocating risk to the superior risk bearer and reducing the costs of resolving dispute.

## II. OPPORTUNISM AND GOOD FAITH

### A. *Opportunism*

The term opportunism appears regularly in the economic literature. Specific forms of it are:

- *free riding* – where a result can be brought about only by the contribution of all but it is not feasible to supervise everyone, the free rider abstains from contributing, yet shares in the spoils;<sup>15</sup>
- *shirking* in a labour relationship, where the employee gives the employer a lesser performance than promised;<sup>16</sup>
- *agency problems* also reflect supervision difficulties – where one must pursue one’s plans by relying on other persons’ good offices without being able to fully supervise them, the other persons may pursue their own interests at one’s expense;
- *moral hazard* – originally in insurance contracts, but with wider application – is also a supervision problem – where the insured, once the insurance contract is written, behaves less carefully than promised or demonstrated when the premium was set.
- *holdout* behaviour is a different kind of opportunism – where a collective project will go forward only with everyone’s consent, the hold-out suspends his consent in the hope of securing more than his

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<sup>13</sup> Calabresi 1970, 139 f.; Calabresi/Melamed 1972, 1118 f.

<sup>14</sup> De Geest et al. 2002.

<sup>15</sup> de Jasay 1989.

<sup>16</sup> Buechtemann/Walwei 1999, at 172.

proportional share of the spoils. The opportunism stems here not from an information (supervision) problem, but from the monopoly power conferred by the veto;

- *hold-up* situations are those in which one party is able to force the hand of the other to get more than its promised or fair share of the joint gains of the contract (Shavell 2007).

Although these specific forms of opportunism have attracted a good deal of attention, one would be hard-pressed to find a proper definition of opportunism in general.<sup>17</sup> Neoclassical economic theory paid little attention to the notions of transaction costs and opportunism, preferring to study markets as if transactions occurred in principle without friction. In contrast, for so-called “institutionalist” economists, these notions play a central role, often in specific reference to the Coase Theorem. Williamson, who has done much to clarify the concept in economic thought, defines it as ‘self-interest seeking with guile.’<sup>18</sup> He contrasts opportunism with trust and associates it with selective or partial disclosure of information and with ‘self-disbelieved promises’ about one’s own future conduct. Dixit adds that it refers to a class of actions that may look tempting to individuals but will harm the group as a whole.<sup>19</sup> George Cohen defines opportunistic behaviour in general as ‘any contractual conduct by one party contrary to the other party’s reasonable expectations based on the parties’ agreement, contractual norms, or conventional morality.’<sup>20</sup>

To sum up, a party to a contract may be said to act opportunistically where it seeks, by stealth or by force, to change to its advantage and to the detriment of the other party or parties the division of the contract’s joint gains that each party could normally look forward to at the time of contracting. It tries, in other words, to get ‘more than its share,’ an undue advantage.<sup>21</sup> Opportunism may involve getting a party to enter an agreement it would not willingly have signed if it had been fully informed (*ex-ante* opportunism); it may also involve later exploiting unforeseen circumstances the contract does not provide for in order to change the division of gains implicitly agreed upon when the contract was entered into

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17 Cohen 1992, at 954.

18 Williamson 1975, 26 and later works: 1985; 1996.

19 Dixit 2004, 1.

20 Cohen 1992, at 957.

21 Art. 3.10 of the Unidroit *Principles of International Commercial Contracts* (1994) speaks of an ‘excessive advantage’.

(*ex-post* opportunism). In acting opportunistically one party significantly exploits an asymmetry in the relationship amongst the parties to the detriment of the other party or parties. In a prisoner's dilemma game, it would correspond to defection where the other party or parties choose cooperation.

For opportunism to arise, there must be an asymmetry between the parties, of which one takes advantage at the expense of the others. Asymmetry itself does not necessarily signal opportunism: you rely on professionals of various sorts for services they specialise in; life would be difficult without it. The problem arises when one party exploits the asymmetry significantly to change the division of quasi-rents of the contracts in his favour.

Opportunism can take an infinity of forms. Its variants are coextensive with opportunities for making profit and (not) sharing it. Each new development in communication technology – the latest being the internet – brings its lot of new openings for opportunism. Responses to it must develop apace. To accommodate such an open-ended arsenal of responses to opportunism, law needs a flexible concept, which is nonetheless compatible with the rule of law.

Where the law steps in to allow redress to victims of opportunistic behaviour, for some actors this will lower the expected likelihood of falling prey to opportunistic acts and allows them to lower the level of precautions they would otherwise have adopted. They will increase their trust in potential contracting partners. More contracts will be entered into than would otherwise be the case. The downside of such intervention is that some parties will be prevented from setting up as sharp a deal as they think they can handle and this entails a loss in the form of foregone opportunities. The intervention would be justified if the gains under the first heading would be judged sufficient to offset the losses under the second (Wittman test). This amounts to judging that public authority has access to significant scale economies in preventing opportunism.

Not all forms of opportunism call for public corrective intervention. According to the Wittman test, intervention would not be worthwhile for minor forms, which are best dealt with by persons being normally on their guard: self-protection is cheaper than the constraints a public mandatory rule inevitably imposes on all actors. The law makes opportunism actionable only where one party takes advantage of an asymmetry to a significant degree, i.e beyond a certain threshold of seriousness. This explains why puffing and minor exaggerations (*bonus dolus*) are not actionable. The impediments to the functioning of markets would seem here to exceed savings in self-protection.

### **B. Good faith**

Good faith is a key principle in civil legal systems.<sup>22</sup> It played a major role in late Roman law and in pre-codification French law.<sup>23</sup> Within the modern civil law family, it still plays an important role in French law (arts 1134 and 1135 of the French Civil Code in particular) and a central role in German civil law (*'Treu und Glauben'*)<sup>24</sup>. In Dutch law, the recodification towards the end of the twentieth century recognised as fundamental principles of civil law the subjective notion of good faith as justifiable ignorance of title defects in the law of property, and the objective notion of good faith as loyalty in contractual dealings, for which the distinctive term 'reasonableness and equity' (*redelijkheid en billijkheid*) was introduced.<sup>25</sup> The Quebec Civil Code of 1994 has given good faith a substantially larger place than it had under the old Code of 1866. In all, 86 articles in the new code use the term good faith. Amongst these, the following stand out:

6. Every person is bound to exercise his civil rights in good faith.

7. No right may be exercised with the intent of injuring another or in an excessive and unreasonable manner which is contrary to the requirements of good faith.

1375. The parties shall conduct themselves in good faith both at the time the obligation is created and at the time it is performed or extinguished.

The Unidroit *Principles of International Commercial Contracts* of 1994 provide in art. 1.7 that 'each party must act in accordance with good faith and fair dealing in international trade' and that 'the parties may not exclude or limit this duty.'<sup>26</sup>

Good faith is used in two distinct meanings, one in property law, the other in contract law, which we shall deal with mainly. In property law ('subjective good faith'), it applies, for instance, to the purchaser of stolen goods and to the possessor non-owner of goods who acquires ownership through prescription. Good faith refers here to justifiable ignorance of facts or legal status, in particular defects in one's title. This notion, too, lends itself to an economic analysis, in which one compares the precautions that could have been taken to ascertain the accurate state of affairs to the risk and cost of acting on an erroneous assessment.<sup>27</sup>

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<sup>22</sup> Survey: Litvinoff 1997; Hesselink 2004.

<sup>23</sup> Charpentier 1996.

<sup>24</sup> Art. 242 BGB (German Civil Code).

<sup>25</sup> Haanappel/Mackaay 1990.

<sup>26</sup> Unidroit 1994.

<sup>27</sup> Mackaay 2001.

To capture the meaning of good faith in contract law ('objective good faith'), legal scholarship resorts to terms such as 'fairness, fair conduct, reasonable standards of fair dealing, decency, reasonableness, decent behavior, a common ethical sense, a spirit of solidarity, community standards of fairness' and 'honesty in fact'<sup>28</sup> and their French equivalents: '*loyauté*',<sup>29</sup> '*honnêteté*', '*intégrité*',<sup>30</sup> '*fidélité*', '*droiture*', '*véracité*'<sup>31</sup>, '*comportement loyal*', '*souci de coopération*', '*absence de mauvaise volonté*', '*absence d'intention malveillante*'<sup>32</sup>; the absence of good faith signals 'unconscionable' behaviour<sup>33</sup>, which in French is characterised as '*blâmable*', '*choquant*', '*déraisonnable*'<sup>34</sup>. In pre-revolutionary French law, good faith was considered to require 'that consent is valid, that parties abstain from trickery, violence, any dishonesty or fraud; but also that it was plausible and reasonable; and finally that the contract not be contrary to divine law, to good morals, nor to the 'common weal' (*profit commun*)'<sup>35</sup>.

All these formulae, intuitively plausible though they may seem, merely translate one general term into other general terms. A formula closer to translation into operational tests is given by Pineau *et al.*: 'one should not profit from the inexperience or vulnerability of other persons to impose on them draconian terms, to squeeze out advantages which do not correspond to what one gives them'<sup>36</sup>. Acting in this way corresponds to opportunism, as we explained the term above. Bad faith is the legal term for opportunism. To act in good faith is to abstain from behaving opportunistically in circumstances that lend themselves to it.

Acting in bad faith can now be specified in law as requiring three tests:

- an asymmetry of information or coercive power between the parties
- exploited by one to its advantage and to the detriment of the other(s)
- to such a degree that it might provoke significant self-protective measures amongst the latter for the future

We tested this three-pronged test on a set of cases raising good faith issues

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<sup>28</sup> Keily 1999), at 17-18.

<sup>29</sup> Charpentier 1996, 305.

<sup>30</sup> Pineau *et al.* 2001, 35.

<sup>31</sup> Rolland 1996, 381.

<sup>32</sup> Cornu 2000, V<sup>o</sup> Bonne foi.

<sup>33</sup> Keily 1999, at 17.

<sup>34</sup> Pineau *et al.* 2001, 44.

<sup>35</sup> Ourliac/de Malafosse 1969, 83, n<sup>o</sup> 67.

<sup>36</sup> Pineau *et al.* 2001, 44.

in international trade and found that it could readily account for the elements the courts took into consideration.<sup>37</sup> In Michael's book, the exploitation of informational asymmetries must lead to 'significantly' or 'substantially' inferior results for the victim, which seems to correspond to the third prong of the test.

In a very general sense, one might say that the core of contract law is that all contracts must be performed in good faith and that the task of the courts is to sanction the absence of it. But this would leave far too much discretion to the courts and too much uncertainty for citizens. Hence good faith has had to be particularised in Civil Codes into a number of more specific concepts, each with its own legal tests. Whittaker and Zimmerman provide the following list for civilian systems: *culpa in contrahendo*; *obligations d'information*; *laesio enormis*; the abuse of rights; personal bar; interpretation of the parties' intentions (whether standard or 'supplementary'); the doctrine of 'lawful contact'; laches; unconscionability; *Verwirkung*; *purgatio morae* and *purgatio poenae*; doctrines of change of circumstances or 'erroneous presuppositions'; the notion of a 'burden' (*Obliegenheit*); *force majeure*; *exceptio doli*; mutual mistake; liability for latent defects; the legal consequences associated with the maxims *nemo auditor turpitudinem suam allegans* and *dolo agit qui petit quod statim redditurus est*, and *venire contra factum proprium*.<sup>38</sup>

Since all these concepts are derivative of good faith, one would expect the three general features – asymmetry; exploitation; beyond a certain threshold – identified above to shine through all particularisations. We found this to be so in the concepts of fraud (*dolus*), warranties and lesion we looked at.<sup>39</sup> Good faith remains as a residual concept with which to fashion new remedies where no existing one is appropriate (as one may expect for some cyberspace contracts).

## CONCLUSION

The law and economics Michael introduced into Canadian legal scholarship has produced significant benefits. In this paper I have attempted to illustrate this in looking at the foundations of contract law and at the open-ended concept of good faith, which civil law systems use as one of the moulds with which to

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<sup>37</sup> Mackaay et al. 2003.

<sup>38</sup> Whittaker/Zimmerman 2000, 676; also Zimmerman 2001, 172.

<sup>39</sup> Mackaay et al. 2003.

fashion remedies against novel forms of opportunism.

Precisely what role law and economics plays here is an intriguing question. It is not a wholesale replacement of legal scholarship, nor a novel theory of law, but more like a sounding board setting out base line constraints that all legal theories have to respect. It also provides an “impact calculus” for determining what the most important consequences of a change of rule would be.

Consider Michael’s paper on the inequality of bargaining power.<sup>40</sup> The paper shows how a variety of arguments the House of Lords considered for supporting its conclusion of a significant inequality justifying corrective intervention simply do stand up in the light of the evidence we then had about the functioning of the music market. The paper also predicted the effects of the decision: it will be harder for unknown singers to be signed on.

The *Limits of freedom of contract* prolong this approach in looking at what various theories, such as feminism or critical legal studies, have to say about different aspects of contract. The book follows along, in an open-minded and non-doctrinaire fashion, with the concerns these theories embody for improving the human lot; but it also submits them to a reality check, the elements of which are provided by law and economics. This critical doctrinal function of law and economics ought to be congenial to civil law scholarship. In the attempts now underway in Europe to express the common frames of reference for contract and tort law, law and economics is used in just this role: as a language in which to compare legal systems and as a tool to think the unthinkable – how else the law might be framed. That is a significant contribution to legal scholarship. Thanks, Michael!

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<sup>40</sup> Trebilcock 1976.



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