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FAIRNESS OF CONTRACT TERMS IN EUROPEAN AND SERBIAN LAW

Abstract

Pursuant to its 2008 Stabilization and Association Agreement governing the process of EU integration Serbia is obliged to align its consumer protection standards with those of the EU. As part of this process in 2010 it adopted a new Consumer Protection Act that, inter alia, implements the Unfair Contract Terms Directive. This article compares the Serbian and European fairness regimes laid down in the tests of fairness, highlighting the advantages of the Serbian test. It argues that the Serbian test is preferable particularly because it resolves the saga on the relation between substantive and procedural fairness, and it allows the application of the test during performance of the contract. As a final note the paper highlights the potential dangers that may undermine the positive effects of the test and leave consumers unprotected.

Key words: unfair contract terms, consumer protection, European law, Serbian law

I. INTRODUCTION

In 2008 Serbia signed and ratified the Stabilization and Association Agreement (hereinafter: SAA), thereby formally commencing the process of European integration. The SAA provides a conditional guarantee of membership of the European Union (hereinafter: EU), subject to fulfilment of a number of conditions, including harmonization of the economic law of Serbia with that of the EU, including consumer protection standards.¹

When the SAA was signed, the then-existing *Consumer protection act of 2005*² that represented the first attempt at harmonization³ was not in line with *EU consumer acquis*.⁴ It

¹ See for more: G. Papović, A. Feješ (Fejős), “The Role of Stabilization and Association Agreement in Consumer Protection” (Uloga Sporazuma o stabilizaciji i pridruživanju u zaštiti potrošača), *Izazovi evropskih integracija*, 1/2008, 45-60.

² Zakon o zaštiti potrošača, *Official Gazette of the Republic of Serbia*, No. 79/2005. This act replaced the first “modern” consumer protection act, the Consumer Protection Act of 2002 (Zakon o zaštiti potrošača), *Official Gazette of the Federal Republic of Yugoslavia*, No. 37/2002.

³ T. Jovanić, “Consumer Protection Law and Policy in Serbia: The Current State and Projections for the Future”, *The Yearbook of Consumer Law* (eds. C. Twigg-Flesner *et al*), Ashgate, Aldershot 2008, 467.

⁴ J. Czuczai, *Final Report on Assessment of EU Consistency of Serbia/Montenegro Regulatory Framework for Consumer Protection*, PLAC, Belgrade-Podgorica, 2006, 18-21. Cf *Ibid*.

left out, *inter alia*, the regulation of unfair contract terms. Protection against unfair terms in consumer contracts was provided for by a set of general clauses protecting the weaker party, and by special provisions on standard contract terms in the *Law of obligations act of 1978* (hereinafter: LOA).⁵⁶

The creation of a legal and institutional framework for consumer protection intensified after signing the SAA and a completely new *Consumer protection act of 2010* (hereinafter: CPA)⁷ was adopted. The CPA is a comprehensive act, containing both substantive and procedural rules. Modeled after France and Italy⁸ it is *lex specialis* for B2C contracts, whereas the LOA continues to apply as *lex generalis*. The CPA is in line with the *EU consumer acquis*.⁹ Among the 15 EU directives it also implements the *Directive on unfair terms in consumer contracts*¹⁰ (hereinafter: UCTD). Importantly, the CPA for the first time specifically regulates unfair terms in consumer contracts in Serbian law.¹¹

Taking advantage of the minimal character of the UCTD (Article 8 UCTD), the CPA took a wider approach to the regulation of unfair terms than suggested by the UCTD.¹² The objective of the paper is to compare the Serbian and European fairness regimes laid down in the tests of fairness, and particularly to highlight the advantages of the Serbian test in the CPA compared to the European test in the UCTD.

⁵ Zakon o obligacionim odnosima, *Official Gazette of the Socialist Federative Republic of Yugoslavia*, Nos. 29/78, 39/85, 45/89, 57/89; *Official Gazette of the Federal Republic of Yugoslavia*, No. 31/93; *Official Gazette of the Republic of Serbia*, No. 1/03.

⁶ For an analysis of the LOA from the angle of consumer protection see: M. Đurđević, Protection of consumers by general rules of contract conclusion (Zaštita potrošača prema opštim pravilima o zaključenju ugovora), *Pravo i privreda*, 1-4/2009, 271-286.

⁷ Zakon o zaštiti potrošača, *Official Gazette of the Republic of Serbia*, No. 73/10. The English translation of the CPA is available at: <http://www.zapotrosace.rs/CMS/download/law-on-consumer-protection-republic-of-serbia.pdf>, last visited 27 September 2013.

⁸ M. Karanikić Mirić, „What is new in Serbian consumer (contract) law?“ (Šta je novo u Srpskom (ugovornom) potrošačkom pravu?), *5 Legal capacities of Serbia for European integrations* (Pravni kapacitet Srbije za evropske integracije) (ed. S. Lilić), Faculty of Law, Belgrade 2010, 129.

⁹ See for analysis: A. Fejős, The Reform of Consumer Legislation in Serbia (Reforma potrošačkog zakonodavstva u Srbiji), *Social Challenges of European Integrations: Serbia and Comparative Experiences*, (Društveni izazovi evropskih integracija – Srbija i uporedna iskustva), Faculty of Legal and Business Studies, Novi Sad 2010, 128-147.

¹⁰ Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, *Official Journal of the European Communities*, No. L 95/29, 21 April 1993, 29–34.

¹¹ It should be noted that in September 2013 the *Ministry of Foreign and Internal Trade and Telecommunications* responsible for consumer protection put forward the draft of the new CPA for public discussion. The test of fairness in the draft remains unchanged. See: <http://mtt.gov.rs/vesti/javna-rasprava-o-naertu-zakona-o-zastiti-potrosaca/?lang=lat>, last visited 27 September 2013.

¹² The test of fairness in Article 46(2) CPA is modelled after Article 24(1) Consumer Protection Act of the Republic of Slovenia (Zakon o varstvu potrošnikov, *Official Gazette of the Republic of Slovenia*, No. 20/98, 23/99, 110/02, 14/03, 51/04, 98/04, 46/06, 126/07, 86/09, 78/11). Personal conversation with M. Karanikić-Mirić, 12 April 2012.

II. THE CONCEPT OF (UN)FAIRNESS IN SERBIAN AND EUROPEAN LAW

The Serbian test of fairness in Article 46(2) CPA, says that: “A contract term is unfair if it: 1) results in a significant imbalance in contractual obligations of the parties to the detriment of the consumer; 2) causes the execution of a contract to be burdensome to the consumer without a justifiable reason; 3) causes the execution of a contract to be substantially different from what the consumer legitimately expected; 4) violates the transparency requirements of the business; 5) violates the principle of good faith.

This provision implements the European test of fairness set out in Art. 3(1) UCTD: “A contractual term which have not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”

At first sight it can be noticed the test of fairness in the CPA is broader than the test in the UCTD. In both tests contract terms are unfair for being contrary to the principle of good faith, and causing a significant imbalance in the parties’ rights and obligations; although the paper will show that the problem with the UCTD (but not the CPA) is that it is not clear what the relationship is between these two general. Moreover, the CPA goes further than the UCTD and explicitly provides that terms may be unfair for being contrary to what the consumer legitimately expected under the contract; making the performance unjustifiably burdensome for the consumer; or for not being transparent. The paper further analyzes these points separately.

II.1. GOOD FAITH AND SIGNIFICANT IMBALANCE IN THE PARTIES’ RIGHTS AND OBLIGATIONS

The basic concept of unfairness in the UCTD is determined by reference to general clauses of good faith and significant imbalance in the parties’ rights and obligations. Besides difficulties in determining the precise meaning of the two clauses, the most important question under the UCTD is the relation of the general clauses to each other.

Brownsword et al highlight at least four different interpretations: 1) a term is unfair if it causes i) a significant imbalance ii) to the detriment of the consumer. In this interpretation the significant imbalance defines violation of good faith, so the latter is not a separate

requirement; 2) a contract term is unfair if it causes i) a significant imbalance, ii) to the detriment of the consumer; iii) it is contrary to the requirement of good faith. Here, the requirement of good faith is an independent, *procedural* condition. 3) a contract term is unfair if it causes i) a significant imbalance, ii) to the detriment of the consumer; iii) it is contrary to the requirement of good faith. The requirement of good faith is an independent, *substantive* condition. 4) a contract term is unfair if it causes i) a significant imbalance, ii) to the detriment of the consumer; iii) it is contrary to the requirement of good faith. The requirement of good faith is an independent, substantive *and* procedural condition.¹³

The correct answer to the above question is that there is no good answer. As the UCTD is a result of a compromise between Member States with different contract law traditions, the clause leaves room for interpretation. For example one key issue is whether the two criteria are completely separate or whether the “significant imbalance” is part of the general criteria of good faith, and national courts approach this differently. Italian courts are inclined to assimilate good faith into significant imbalance. A common formula used in decision making is that a term is unfair because it creates a significant imbalance in the parties’ rights and obligations and which is sufficient to render the term unfair.¹⁴ On the contrary, the House of Lords in *First National Bank v. Director General of Fair Trading* took the view that the two principles are connected but separate requirements.¹⁵

Consensus is also absent among academics. There is a view that good faith is not an independent criterion.¹⁶ Consequently, significant imbalance automatically triggers the violation of good faith.¹⁷ This view relies on the idea that the key reason for good faith being part of the test was to reflect those national traditions that were tied to the good faith concept. In this regard good faith can be viewed simply as a label that “explains” to these national traditions what is meant by the significant imbalance.¹⁸ Nevertheless, as Willett points out, this standpoint is difficult to uphold. Recital 16 UCTD contains explicit and separate

¹³ R. Brownsword, G. Howells, T. Wilhelmsson, “Between Market and Welfare: Some Reflections on Article 3 of the EC Directive on Unfair Terms in Consumer Contracts”, *Aspects of Fairness in Contract* (ed. C. Willett), Blackstone, London 1996, 31-32.

¹⁴ P. Nebbia, *Unfair Contract Terms in European Law: A Study in Comparative and EC Law*, Hart Publishing, Oxford-Portland-Oregon 2007, 151.

¹⁵ *First National Bank v. Director General of Fair Trading*, 25 October 2001, [2001] 3 WRL 1297. Lord Bingham at 1307-8. For analysis see: C. Willett, *Fairness in Consumer Contracts: The Case of Unfair Terms*, Ashgate, Aldershot 2007, 177-216.

¹⁶ M. Teneiro, “The Community Directive on Unfair Terms and National Legal Systems”, *European Review of Private Law*, 2/1995, 273, 279.

¹⁷ C. Willett, “The functions of transparency in regulating contract terms: UK and Australian approaches”, *International and Comparative Law Quarterly* 2/2011, 363.

¹⁸ *Ibid.*

guidelines on good faith.¹⁹ It follows that the violation of good faith is at least to some extent an independent requirement (whether independent from significant imbalance or, with the same practical result, playing some independent role in determining when an imbalance is “significant”).²⁰ This interpretation seems to be confirmed by the Court of Justice of the European Union (hereinafter: CJEU). In *Aziz v Catalunyaacaixa*²¹ the CJEU ruled that in order to determine if a term causes “significant imbalance” the default rules of the applicable national law should be taken into account.²² However, as derogation from default rules will not in itself automatically make contract terms unfair, according to the CJEU, in order to assess if the *significant imbalance* arises “contrary to the requirement of good faith”, it must be determined whether the business could reasonably assume that the consumer would have agreed to the term if the term would be subject of individual negotiations.²³ In other words, the CJEU confirmed good faith is at least to some extent a separate requirement playing some independent role in determining when an imbalance is “significant.”

The issue on the relation between the two general clauses also raises the question of the relationship between procedural and substantive fairness.

“*Substantive fairness*” relates to fairness of the contract terms themselves, fairness of the substance of the terms.²⁴ One way of starting to analyze substantive fairness of a contract term would be unfair if it deviates from the default rules and from reasonable expectations of the consumer.²⁵

“*Procedural fairness*” means fairness in the process leading up to the agreement.²⁶ It is connected to fair and open dealing, and is in place to prevent unfair surprise and lack of choice.²⁷ The concept of procedural fairness is broader than the legibility and other transparency aspects of the terms of the contract. It encompasses choice between alternative terms offered and bargaining power. Therefore, the assessment of procedural fairness includes an evaluation as to whether a consumer had a reasonable opportunity to get acquainted with the contract term, if it was presented in plain and intelligible language, if the consumer

¹⁹ *Ibid.*, 364.

²⁰ *Ibid.*

²¹ C-415/11, *Mohamed Aziz v Caixa d’Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa)*, 11 March 2013, [ECR] I-00000 (not reported)

²² *Ibid.*, 68.

²³ *Ibid.*, 69.

²⁴ C. Willett, (2007), 2.

²⁵ *Ibid.*, 49.

²⁶ *Ibid.*, 2.

²⁷ R. Brownsword, G. Howells, T. Wilhelmsson, 33, 40.

understood the term, if the consumer was able to influence it, and if the consumer had a choice between different alternative terms.²⁸

One element of the test, the significant imbalance in the parties' rights and obligations relates to substantive fairness,²⁹ but the other, good faith, can have both procedural and substantive aspects. Namely, according to Recital 16 UCTD the principle criteria for determining the unfairness of a term is the "overall evaluation of the different interests involved" which could imply procedural and substantive fairness. However, while making the assessment of good faith "particular regard shall be had" to different circumstances in relation to the contract conclusion (e.g. strength of bargaining positions). This arguably implies procedural fairness. The provision goes further, saying that the requirement of good faith *may be satisfied* when the business "deals fairly and equitably" with the consumer. This could be said to include transparency (procedural fairness) as a basic requirement.³⁰ However, as transparency is not mentioned in the recital, good faith plausibly also refers to (building on the significant imbalance/detriment question) unfairness in substance.³¹ Hence, Recital 16 UCTD most likely suggests that the good faith is concerned with both procedural and substantive fairness. It is unclear if the CJEU confirms this interpretation. In *Aziz v CatalunyaCaixa*, the only case expressly ruling on the meaning of the two general clauses in the test of fairness, the CJEU gave a more substantive meaning to good faith. The fact that the CJEU failed to expressly comment on procedural aspects of good faith can lead to two opposing conclusions. One is that as the CJEU specifically mentions the phrase "dealing fairly and equitably" and the process of contract conclusion, the CJEU impliedly included procedural fairness into the scope of good faith. The other is, failing to expressly point out procedural aspects of good faith, bringing the principle only in connection to significant imbalance, the CJEU sees good faith as a principle contributing only to enquiries into substantive fairness. On this latter reading, as both general clauses aim toward substantive fairness, it could be inferred that the UCTD is primarily concerned with substantive fairness, i.e. the contract term should be fair in its substance.

Therefore, we can see that the issue remains unclear, yet it is an important issue. If significant imbalance was the only requirement (violation of good faith being part of it) it is fairly clear that the contract term would only need to be unfair in its substance in order to be

²⁸ P. Nebbia, 149. On the difference between procedural fairness and *culpa in contrahendo* see: H. Beale *et al*, *Cases, Materials and Texts on Contract Law*, Hart publishing, Oxford-Portland-Oregon 2002, 237-240.

²⁹ H. Collins, „Good Faith in European Contract Law”, *Oxford Journal of Legal Studies*, 1994, 249.

³⁰ This is the standpoint of UK courts, but the view is present in other jurisdictions as well, e.g. France. See: C. Willett, (2007), 112-113.

³¹ C. Willett, (2011), 364.

declared unfair, and the issue of the relationship between procedural and substantive fairness would not arise. But, if significant imbalance and violation of good faith are separate requirements (what seems to be suggested by the CJEU in *Aziz v Catalunya Caixa*), then the questions are: can the lack of procedural fairness make a term unfair where, otherwise, there would be no sufficient unfairness in substance; and can procedural fairness legitimize substantive unfairness. These issues will be further tackled when talking about the role of transparency.

In Serbia, both the “significant imbalance” and “good faith” are present as overarching principles of Serbian contract law. The “predecessor” of “significant imbalance”, the principle of equality of contractual rights and obligations in Article 15 LOA goes into the heart of contracts. It aims to establish the contractual balance between the parties’ rights and obligations, and is concretized by more specific legal institutions like *laesio enormis*, usury and *clausula rebus sic stantibus*.³² The principle therefore without a doubt has a substantive meaning. The equivalent of the principle of good faith is laid in Article 12 LOA, according to which provision, the parties must act respecting the principle of good faith and honesty in concluding and performing contracts. This could imply both procedural and substantive fairness, i.e. acting fairly and honesty in the process of contract conclusions and in the process of its performance, but also incorporating terms into the contract that are substantively fair. Hence, the principle of good faith sets objective standards of ethical behaviour, in accordance with good morals, fairness and justice, which most probably has both substantive and procedural aspects.³³

Contrary to the UCTD, the CPA solves the saga of the relationship between the two general clauses, and sets “good faith” and “significant imbalance” as separate bases for determining the fairness of contract terms, in Articles 46(2)(5) and 46(2)(1) respectively. The potential problem with the CPA may be that the test is not clear as to whether the conditions laid down in Article 46(2) CPA should be read alternatively or cumulatively. Most probably even though cumulation is possible, e.g. terms that cause significant imbalance in the parties’

³² For analysis see: J. Szalma (Salma), „The principle of equivalence and *laesio enormis* in contracts” (Načelo ekvivalentnosti i prekomerno oštećenje u obligacionopravnim ugovorima), *Zbornik radova Pravnog fakulteta u Novom Sadu*, 1977, 273-282; J. Szalma (Salma), *Law of Obligations – general part, main principles, contracts and delicts* (Obligaciono pravo – opšti deo, osnovna načela, ugovori i prouzrokovanje štete), Faculty of Law, Novi Sad 2009, 367-383.

³³ See on meaning of good faith: J. Szalma (Salma), „The principle of good faith” (Načelo savesnosti i poštenja), *Glasnik advokatske komore Vojvodine*, 5/1982, 1-31, 1982, p. 23-29; see also: M. Szűcs (Sič), “Eternal values of Roman Law” (Trajne vrednosti rimskog prava), *Zbornik radova Pravnog fakulteta u Splitu*, 3-4/2006, 393-397; Commentary on Article 12, *Commentary on Law of obligations act, Book 2* (Komentar Zakona o obligacionim odnosima, Knjiga 2) (ed. S. Perović), Savremena administracija, Belgrade 1995.

rights and obligations are also contrary to the principle of good faith, it is not (or it should not be) the correct reading of the test. Cumulative interpretation would significantly narrow down the scope of the test, as in order to find terms to be unfair a number of conditions would have to be satisfied, both substantive and procedural. Moreover, the model of the CPA expressly sets the conditions alternatively.³⁴ Hence, if the test is read alternatively, it is enough if terms are in conflict with one of the principles, i.e. if they cause significant imbalance in the parties' rights and obligations *or* are contrary to the principle of good faith. Having the principles as separate basis shows the probable intention of the drafters that no matter how the principle of good faith is interpreted, i.e. if it is given a more procedural or a more substantive meaning, procedural fairness is not capable of legitimizing substantive fairness, and procedural unfairness alone is capable of making the contract term unfair.

II.2. PERFORMANCE SUBSTANTIALLY DIFFERENT FROM LEGITIMATELY EXPECTED

Closely linked to the principles of good faith and significant imbalance is the concept of legitimate expectations of a consumer regarding the performance of the contract (Article 46(2)(3) CPA). This concept is not expressly present in the UCTD, although it was incorporated in its earlier drafts.³⁵ Hence, as Willett points out, it must have been anticipated by the drafters of the current version of the UCTD that the concept of legitimate expectations would be relevant.³⁶

Legitimate expectations, as an English law concept, arose from administrative law where it applies the principles of fairness and reasonableness to the situation where a person has an expectation or interest in a public body retaining a long-standing practice or keeping a promise.³⁷ Similarly, in private law, Micklitz and Wilhelmsson developed a “right to the protection of legitimate expectations” that should be implemented by mandatory contract or tort law rules.³⁸

³⁴ Article 24 Consumer Protection Act of the Republic of Slovenia

³⁵ Article 3(1) Amended Proposal for a Council Directive on Unfair Terms in Consumer Contracts, COM (1992) 66 final SYN 285.

³⁶ C. Willett, (2007), 269.

³⁷ P. P. Craig, “Substantive Legitimate Expectations in Domestic and Community Law”, *Cambridge Law Journal*, 1996, 290.

³⁸ N. Reich, “The Consumer as Citizen – the Citizen as Consumer – Reflections on the Present State of the Theory of Consumer Law in the EU”, 10, http://www.iaclaw.org/Research_papers/melangescalais2ok.pdf, last visited 29 June 2013. As the *Treaty on the Functioning of the European Union* does not expressly provide this right, consumers right to legitimate expectations is provided by reading together secondary and primary law, by

The concept of legitimate expectations is based on mutual rights of contracting parties, and their optimal balance. On one hand, businesses have a right to access to free trade, the right to use freedom of contract to shape their position in contractual relations, on the other hand, consumers have a right to be fully informed of their rights, to be able to withdraw from the contract, and to have the necessary remedies to secure the enforcement of their rights.³⁹

As Willett points out⁴⁰ legitimate or reasonable expectations might relate to the content and aim of the contract, in cases where consumers have certain expectation regarding performance. This might be relevant where terms allow, e.g. variation of price or performance, i.e. variations from what the consumer reasonably expected.

Hence, the concept of legitimate expectations has both substantive and procedural dimensions. On one hand, it encompasses a right to have information on rights and remedies (procedural dimension); on the other, in performance of contracts consumers should be guaranteed the “headline” performance that they reasonably expect, and not receive a varied performance allowed for by standard terms (substantive dimension).

Explicitly incorporating legitimate expectations into the test of fairness raises the level of protection. As the concept was unknown to Serbian contract law until the CPA it is essential to determine the necessary preconditions for the operation of this concept.

First, it is important that that performance is substantially different from what is expected. What “substantially” means is a practical question, but minor discrepancies would not be sufficient.

Second, it is important that the expectation of the consumer is based on the default rules of the law, or the “headline” performance that they reasonably expect.

Third, the limits of the consumer’s expectations are set by reasonableness. What is reasonable will be determined by the help of the two closely linked principles, the principle of contractual balance in the parties’ rights and obligations and the principle of good faith.

interpretation. H.-W. Micklitz, N. Reich, P. Rott, *Understanding EU Consumer Law*, Intersentia, Antwerp-Oxford-Portland 2009, 27-28.

³⁹ H.-W. Micklitz, “Social Justice in European Private Law”, *Yearbook of European Law*, 1/1999, 178.

⁴⁰ *Ibid.*

II.3. PERFORMANCE BURDENSOME WITHOUT JUSTIFIABLE REASON

Closely linked to the above forms of unfairness, there is a ground for unfairness in Article 46(2)(2) CPA stipulating that a contract term will be unfair if it causes the *execution* of the contract to be burdensome to the consumer without a justifiable reason. This base for finding terms unfair is not present in the UCTD. Moreover, the UCTD is limited in its application at the time of contract conclusion (Article 4(1) UCTD). If circumstances change after the contract is concluded, they will be irrelevant to the test of fairness. Therefore, the UCTD is not flexible to accommodate the new concept in contract law, the concept of “*social force majeure*”, as emerged in some Nordic countries.⁴¹ *Social force majeure* means “social obstacles to performance” obstacles emerging due to changed circumstances like unemployment or illness, which are although not completely unforeseeable, are not attributable to the consumer’s fault. The following cumulative conditions have to be fulfilled for the operation of this concept:

- 1) the consumer is affected by some special occurrence affecting its family life, health, employment or anything else;
- 2) there is a causal connection between the occurrence of a special event and the consumer’s payment difficulties (problems in performance of the contract);
- 3) the consumer was not in a position to foresee the occurrence of the event;
- 4) the occurrence of the event cannot be attributed to the consumer’s fault.⁴²

Although the concept was developed primarily in the context of financial services and overindebtedness, according to Wilhelmsson it might lead in the future to a more open-ended interpretation of the test of fairness, allowing an additional reassessment of the fairness of the contract term at a later point, during performance of the contract, taking into account social values and general consumer welfare.⁴³

The CPA does not mention the moment for assessing fairness within the test of fairness, despite being familiar with it.⁴⁴ Moreover, Article 46(3) CPA took the circumstances

⁴¹ T. Wilhelmsson, „’Social Force Majeure’: A New Concept in Nordic Consumer Law”, *Journal of Consumer Policy*, 1990, 3-7.

⁴² *Ibid.*, 7-8.

⁴³ This is already the case in Nordic Countries. T. Wilhelmsson, Control of Unfair Contract Terms and Social Value: EC and Nordic Approaches, *Journal of Consumer Policy*, 3-4/1993, 450.

⁴⁴ Conformity of goods (Article 51 CPA); package travel (Article 99 CPA).

to be taken into account when interpreting the test of fairness from Article 4(1) UCTD, although not following the UCTD in insisting on focusing on the moment of contract conclusion. Therefore, the conclusion would be that the moment of contract conclusion is not a decisive for applying the test of fairness in Serbian law. Nevertheless, Karanikić-Mirić asserts, taking into account the UCTD and the internal logic of absolute nullity in the LOA, the time for determining fairness should be the moment of contract conclusion.⁴⁵ However, even if this view is accepted, there are exemptions from the rule.

The wording of Article 46(2)(2) CPA exactly suggests the provision relates to terms which do not look unfair on their face, or were not unfair at the moment of contract conclusion, but become such during their application. Therefore, this ground for determining the fairness of contract terms comes into play *during the performance*. Additionally, traditional contract law tools of *force majeure*⁴⁶ and *clausula rebus sic stantibus*⁴⁷ could be of help in accommodating *social force majeure*.

⁴⁵ M. Karanikić-Mirić, (2010), 144.

⁴⁶ The LOA does not incorporate the *force majeure* as a separate legal principle, but at certain instances it does refer to special circumstances that could not have been foreseen, avoided or eliminated (e.g. Article 684 LOA). In legal theory *force majeure* is considered different from *casus* (circumstances that could not have been foreseen, and therefore avoided). It is a qualified *casus*, the emphasis being on extraordinary character of circumstances, and not so much on their foreseeability. The important is that the circumstances could not have been objectively and absolutely avoided, even if foreseeable. Force majeure makes the performance of the contract impossible or extremely difficult, and frustrates the contract. See for more: J. Radišić, *Law of Obligations – general part* (Obligaciono pravo-opšti deo), Nomos, Belgrade, 2006, 230-232; S. Jakšić, *Law of Obligations –general part* (Obligaciono pravo, opšti deo), Veselin Masleša, Sarajevo 1953, 242; I. Babić, *Fundamentals of civil law – introduction to civil law and property law* (Osnovi imovinskog prava – uvod u građansko pravo i stvarno pravo), Službeni glasnik, Belgrade, 2008, p. 110; *Commentary on Article 137, Commentary on Law of obligations act, Book 2* (Komentar Zakona o obligacionim odnosima, Knjiga 2) (ed. S. Perović), Savremena administracija, Belgrade 1995.

⁴⁷ *Clausula rebus sic stantibus* is laid down in Article 133 LOA. It allows for a rescission of the contract or exceptionally the modification of a contract term if after the conclusion of the contract circumstances occur (unforeseeable at the time of contract conclusion) that make difficult the execution of the contract for one party, or make the contractual aim unrealizable, to an extent that it ceases to be in line with what the parties expected under the contract and it would generally be unfair to uphold the contract. See for more: *Commentary on Article 133, Commentary on Law of obligations act, Book 2* (Komentar Zakona o obligacionim odnosima, Knjiga 2) (ed. S. Perović), Savremena administracija, Belgrade 1995; M. Mićović, „Clausula rebus sic stantibus: De lege lata and de lege ferenda” (Kluzula rebus sic stantibus: de lege lata i de lege ferenda), *Pravni život*, 11/2008, 445-455; O. Antić, *Law of obligations* (Obligaciono pravo), Službeni glasnik, Belgrade 2009, 416. *Force majeure* and *clausula rebus sic stantibus* can be applied interchangeably. For example economic circumstances that make the performance extremely expensive, but not impossible, are not a sufficient reason for declaring performance impossible, they may be enough to modify or rescind the contract due to changed circumstances. See: *Commentary on Article 137, Ibid.*

II.4. THE ROLE OF TRANSPARENCY

When talking about the role of transparency, the first question is what transparency means, the second, can transparency or procedural fairness legitimise substantive unfairness, and the third, can the breach of transparency rules alone make the contract term unfair.

Regarding the meaning of transparency, Willett summarizes, that “terms are transparent when they are available at the point of contract; there is a reasonable opportunity to become acquainted with them; they are in clear, jargon free language and decent sized print; the sentences, paragraphs and overall contract are well structured; and appropriate prominence is given to particularly important terms”.⁴⁸ As the ultimate aim of transparency is to enable the consumer to make an informed decision on entering into the contract and choosing the right product, Willett asserts that transparency has to ensure for consumers a *real chance to understand* the content of the terms.⁴⁹ Since understanding depends on a number of additional factors like education and intelligence,⁵⁰ transparency means terms should be formulated and explained in such matter that provide an *opportunity* for understanding of particular terms, and to allow the overall estimation of a contractual position of the consumer (regardless whether actual understanding is achieved). In this sense it is clear that businesses are obliged to disclose some information and actually other matters. Sometimes general presentation of the terms might not be enough, but businesses have to take additional steps, and specifically draw the attention of the *particular consumer* to a *particular term*.

The principle of transparency is laid down in Article 5 UCTD, according to which: “[i]n 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.” Due to the formulation of the provision, the reach of the principle and its content is uncertain. At first sight it suggests a purely formal control i.e. clear and comprehensible language of contract terms, without any further obligation of the business towards a consumer in order to ensure the consumer had real opportunity to understand the terms. However, if Article 5 UCTD is read together with Article 3(1) UCTD, where transparency relates to procedural fairness as part of the general requirement of good faith and the test of fairness, this would mean more than clear and comprehensible language. Talking about the function of transparency, the European

⁴⁸ C. Willett, (2011), 357.

⁴⁹ *Ibid.*, 384.

⁵⁰ Experience shows that information is more utilized by “affluent, well-educated, middle-class consumers.” G. Howells, “The Potential and Limits of Consumer Empowerment by Information”, *Journal of Law and Society*, 3/2005, 356.

Commission (hereinafter: Commission) seems to confirm this position. First, by reading Article 5 UCTD together with Recital 20 UCTD, according to which, the consumer should have “actually be given an opportunity to examine all the terms” of the contract, transparency is seen as a way of vetting contractual terms at the time of contract conclusion.⁵¹ Terms that are not transparent, will not even become part of the contract. Second, reading together Article 5 UCTD and Article 3(1) UCTD the principle of transparency relates to the control of the content of the contract.⁵² The Commission further emphasizes transparency also means consumers should be able to obtain the necessary pre-contractual information to make an informed decision.⁵³ The CJEU seems to largely confirm the Commission’s interpretation. Going above plain and intelligible language, the CJEU interpreted Article 5 UCTD in connection with Recital 20 UCTD as relating to pre-contractual information on the terms of the contract and on the consequences of concluding the contract.⁵⁴ Therefore, although the final reach of transparency remains undetermined, both the Commission and the CJEU seem to be inclined towards giving a wider meaning to transparency than plain and intelligible language. However, any wider meaning can only be achieved by interpretation.

The principle of transparency is given large significance in the CPA where it is implemented in a much wider manner. Transparency is part of the test of fairness (Article 46 (2)(4) CPA), it is listed as a circumstance that should be taken into account in interpreting the test (Article 46(3)(4) CPA), and is a vetting rule (Article 44(3) CPA). Regarding the meaning of transparency Article 44(1) CPA asserts: “a contract term is binding for a consumer if it is laid down in a simple, clear and understandable language and if it would be understandable for a reasonable man of the consumers’ knowledge and experience.” Hence, the CPA expressly insists on a real opportunity of a consumer to understand the terms of the contract. Since understanding depends on factors like education and intelligence, the threshold of clarity and simplicity of language is determined compared to a benchmark consumer. The benchmark consumer in the CPA is such that there is a higher level of protection than the general European benchmark. Namely, in the absence of a specific reference in the UCTD the general benchmark established by the CJEU in *Gut Springenheide* as “an average consumer

⁵¹ *Report on the Implementation of Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts*, COM (2000) 248 final, 27 April 2000, 17.

⁵² *Ibid.*

⁵³ *Ibid.*

⁵⁴ C-92/11, *RWE Vertrieb AG v Verbraucherzentrale Nordrhein-Westfalen e.V.*, 21 March 2013, [ECR] I-00000 (not reported), 44.

who is reasonably well-informed and reasonably observant and circumspect”⁵⁵ applies. This objective standard however fails to take into account the needs of vulnerable consumers.⁵⁶ Moreover, the standard may not even work with “average” consumers as it was established in relation to commercial communication and achieving understanding of contract terms require deeper information seeking and a certain level of knowledge for an informed decision.⁵⁷ In contrast, the CPA does take into account special vulnerability of certain group of consumers. Whether the terms communicated to the consumer were transparent will be determined taking into account the group of consumers, the “class” to which a particular consumer belongs. Hence, instead of an “absolutely objective” standard it relies on a “relatively objective” standard that might be above or below the “average”. This “relatively objective” standard is an exception in Serbian contract law, where the obligations of the parties are traditionally measured against an objective standard, standard of a reasonable man, or standard of reasonable businessmen.⁵⁸ The fact that the standard of the reasonable man as a standard of behaviour for consumers is not mentioned, might suggest, that the intention of the drafters was exactly to prevent any attempt to make an objective estimation (as much as possible) of how the consumer was suppose to understand the communication of the business, fearing that courts would be too harsh in ruling on transparency, and aiming to develop a special sensitivity of courts towards consumers and their protection.

Article 44(2) CPA further provides the business is obliged to provide a real opportunity for the consumer to get acquainted with the terms of the contract, with due regard to the means of communication used. This provision also seems wider than Article 5 UCTD. It insists on the result to be achieved, rather than the means used. A real opportunity to get acquainted with the terms of the contract is probably wider than plain and understandable language of the contract. This provision most probably obliges the business to make further steps in drawing the attention of consumers to the terms of the contract than just laying them

⁵⁵ C-210/96, *Gut Springenheide GmbH and Rudolf Tusky v Oberkreisdirektor des Kreises Steinfurt - Amt für Lebensmittelüberwachung*, 16 July 1998, [ECR] 1998, I-04657, 37.

⁵⁶ On the contrary, the Directive 2005/29/EC of the European Parliament and of the Council concerning unfair business-to-consumer commercial practices in the internal market, *Official Journal of the European Communities*, No. L 149, 11 June 2005, 22–39, implements the standard developed in *Gut Springenheide* in Article 5(2) but is also familiar with the notion of a vulnerable consumer in Article 5(3). In case of vulnerable consumers the benchmark is an average consumer from the vulnerable consumers’ group (Recital 19). The UCTD does not allow for such distinctions, but the differentiation should be extended to it. See: Simon Whittaker, “Language or Languages of Consumer Contracts?”, *Cambridge Yearbook of European Legal Studies*, 2005-2006, 244.

⁵⁷ *Cf* C. Willett, (2007), 113-115

⁵⁸ These standards are specifically referred to in the LOA (Articles 581, 662, 714, 751).

down in plain and simple language. Indeed, it may well oblige the business to draw the attention of a particular consumer to a particular term.

The second issue related to transparency is whether it can legitimize substantive unfairness. If the answer is yes, this means, substantively unfair terms are considered fair just because they are communicated in a transparent, i.e. procedurally fair, manner. However, procedural fairness should not be capable of legitimizing substantive unfairness. First, consumers often choose not to read the contract.⁵⁹ Second, even if they read the contract they cannot process the information adequately to make an informed decision.⁶⁰ Third, even if they read and understand the terms of the contract, the research of behavioural economics has shown that an informed decision is not guaranteed as consumers are not rational in making choices.⁶¹ Therefore, transparency as an overriding, legitimizing factor leaves the door wide open for businesses to include substantively unfair terms, especially among standard terms and conditions. It is not clear how the UCTD solved the issue. The more protective reading of the test of fairness is that it primarily intends to regulate substantive unfairness, which consequently, cannot be legitimized by procedural fairness, but this is not the only reading of the UCTD. If violation of good faith is a separate requirement under UCTD (see debate above), then it might be argued that, if there is transparency, there is good faith, and therefore no unfairness, no matter the degree of substantive unfairness.⁶² Although the CPA does not deal specifically with the issue, a transparent term self-evidently does not violate the “lack of transparency” unfairness section, if such a term is substantively unfair it clearly violates other sections such as “significant imbalance” or “unjustifiably burdensome”, which are focussed on substantive (un)fairness.

Finally, the third issue is whether transparency alone is capable of making a contract term unfair. Under the UCTD there is no explicit sanction for breach of transparency. According to the Commission, the infringement of the principle of transparency is not penalised in the strict sense of the word. The intention of the UCTD is to maintain the contract with the help of the *contra proferentem* rule, i.e. the interpretation most favourable for the consumer.⁶³ However, taking the wider meaning of transparency, a contract term that

⁵⁹ O. Ben-Shahar, “The Myth of the ‘Opportunity to Read’ in Contract Law”, *European Review of Contract Law*, 1/2009, 7-9; for possible reasons for not reading the contract see also: Willett, (2011), 359.

⁶⁰ S. Grundmann, “Information, Party Autonomy and Economic Agents in European Contract Law”, *Common Market Law Review*, 2002, 269-270; G. Howells, (2005), 350.

⁶¹ M. G. Faure, H. A. Luth, “Behavioural Economics in Unfair Contract Terms, Cautions and Considerations,” *Journal of Consumer Policy*, 2011, 337, 343-345, 348-349.

⁶² C. Willett, (2011), 372.

⁶³ *Report on the Implementation of Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts*, COM (2000) 248 final, 27 April 2000, 19.

is not communicated in a transparent manner will not become part of the contract (Article 5 UCTD read with Recital 20 UCTD), or it will make the term unfair and therefore null and void (Article 5 UCTD read together with Article 3(1) UCTD). This is however subject to interpretation, and the only explicit sanction is the *contra proferentem* interpretation. On the contrary, in Article 46(2)(4) CPA transparency is part of the test of fairness; hence, a non transparent term alone is capable to make the contract term unfair. It follows, under the CPA procedural fairness is a valid ground for making contract terms unfair.

III. CONCLUSION

The CPA for the first time introduced the notion of unfair contract terms in consumer contracts into Serbian contract law, and provides reasonably comprehensive regulation. The paper compared the Serbian and European tests of fairness, and highlighted the advantages of the Serbian test. Based on the analysis it can be concluded the Serbian test in the CPA is much more protective than the European test in the UCTD.

First, it is much clearer in Serbia than under the European test that (a) terms can be unfair purely on the basis of procedural unfairness, including a lack of transparency and (b) terms can be unfair purely on the basis of substantive unfairness, i.e. that procedural fairness is not capable of legitimizing substantive unfairness.

Further, it is possible in Serbian law, but not European law, for a term that is fair based on circumstances existing at the time of contract conclusion, to be found to be unfair based on (changes to) circumstances during performance. This means that there is great potential to accommodate the newly emerged concept of *social force majeure*.

Finally, the Serbian regime is clearly more protective in not containing important exemptions from the test of unfairness, such as terms defining the price or main subject matter.⁶⁴

Therefore, it can be said, the test of fairness in CPA is an almost perfect legislative solution. It is very much fairness oriented, providing both for substantive fairness and procedural fairness apparently leaving very little room for the businesses' freedom of contract and provides for a very high level of protection for consumers. However, there remain key questions as to how the test will be applied in practice. First, all of the above described

⁶⁴ See Article 4(2) UCTD and the significant reduction in protection that can be caused if, as in the UK, the price exclusion is interpreted to include virtually all charges under the contract no matter how peripheral (*Office of Fair Trading v Abbey National Plc.* [2009] UKSC 6, [2010] 1 AC 696).

potential for independent regulation of substantive, procedural and post contractual (or performance oriented) fairness can all be undermined by judges setting low levels of (substantive, procedural or post-contractual) fairness.⁶⁵ Finally and vitally, without adequate enforcement mechanisms and tools good substantive law rules stay “letters on the paper,” and consumers remain unprotected.⁶⁶

⁶⁵ See C. Willett, “General Clauses and the Competing Ethics of European Consumer Law in the UK”, *Cambridge Law Journal*, 2/2012, 419-422 on the *First National Bank* case where the House of Lords decided that there would be “significant imbalance” against a bank if it could not continue to add contractual interest to a judgement debt awarded against a consumer (despite the argument that most consumers would reasonably believe that they would be clear of responsibility, as long as they paid the full amount ordered by the court over the required period, only to discover that a large amount of interest was still owed on top of this).

⁶⁶ See for problems with enforcement in Serbia: A. Fejős, “The Impact of EU Norms and Policies on Consumer Protection Enforcement in Serbia”, *Journal of Consumer Policy*, 2013, 250-263.