President's Message

The Wizard of Oz (or "Good Faith and Swiss Law")

I have lost count of the number of times that I have sat, groaning, listening to speakers at international conferences engaging in presentations of allegedly "comparative" law, waiting (with a mixture of resignation, exasperation and resentment) for the inevitable cliché to arrive. My foreboding is rarely misplaced, and (far) more often than not, at some point, the (non-Swiss) speaker will utter the inevitable commonplace, "*And, well, Swiss law being based on 'good faith', it's all very unpredictable*."

The frequency with which this cliché is disseminated, combined with the fact that it is spectacularly off the mark, reminds me of "*The Wizard of Oz*." The eponymous character of both the famous 1939 silver screen classic starring Judy Garland and of the 1900 children's book by L. Frank Baum ("*The Wonderful Wizard of Oz*") has much in common with the role of good faith in Swiss law as perceived by some. For the inhabitants of the Land of Oz (in particular for the denizens of Munchkinland), the Wizard of Oz is an all-powerful creature with magical powers, perched in his castle in the far-away Emerald City, seen by none, feared and revered by all because of the wonderful things he does. Yet, when, after a long and eventful journey down the Yellow Brick Road, the tale's heroine Dorothy draws back the curtain behind which the Wizard sits, she discovers that he is nothing more than a rather ordinary and somewhat wimpy man, sporting (as certain other self-overrated political bigwigs in our times do) an extremely bizarre hair-do, and whose magical powers were nothing more than smoke and mirrors aimed at overawing the common-folk (a comparison with current affairs again springs to mind).

Coming back to the place of good faith in Swiss law, it would appear that it too is viewed (figuratively, since it is not actually *seen*) by many as some kind of overarching principle of magical potency, which, because of its haziness and fuzziness, trumps (no pun intended) the black letter of both the law and of the contract, rendering impossible any *ex ante* legal analysis or risk assessment.

The time has come for this long-suffering conference attendee to rebel, to imitate Dorothy, to draw back the curtain and to expose this cliché for the humbug it is. Given the limited space available in a President's Message, I shall proceed on a sample basis.

Contract interpretation

One particularly fertile breeding ground for the good faith = The Wizard of Oz cliché is the matter of contract interpretation.

To be fair, the formulation used by the Swiss Supreme Court and Swiss legal commentary, under which contract terms must, when the actual intent of the parties cannot be ascertained on the basis of factual evidence, be interpreted in accordance with the "*principle of trust and in accordance with the rules of good faith*", is not very engaging. The abstruseness of the label, however, is no excuse for not looking at what is in the package. What it means is that, where the actual common intent of the parties cannot be established as a matter of fact, a court or arbitral tribunal must take the contract terms and concomitant statements of the parties and give them the meaning that a person placed in similar circumstances, having a similar background as that of the parties, would reasonably do. Where the contract uses ordinary language, that language should be given its ordinary meaning. Where the contract uses technical legal terms, those terms should be given their usual technical legal meaning. Where the parties have previously entered into similar contracts, the contract terms should be given the meaning the parties had given them in their previous dealings.

None of this sounds particularly wizardly or impenetrable. And the best proof of this rather unexceptional conclusion is the number of practitioners who, when interpreting a contract under a law other than Swiss law, arrive at exactly the same conclusion that Swiss law would have led to, albeit sometimes by following a different path.

Abuse of right

Another Exhibit-A for the cliché-spreaders is "abuse of right." The offending provision is Article 2 of the Swiss Civil Code, which, in the unofficial English translation found on the website of the Swiss Confederation, reads as follows:

> *B. Scope and limits of legal relationships*
>
> *I. Acting in good faith*
>
> *Article 2*
>
> *[1] Every person must act in good faith in the exercise of his or her rights and in the performance of his or her obligations.*
>
> *[2] The manifest abuse of a right is not protected by law.*

Again, the formulation may not be altogether congenial for the non-Swiss legal practitioner. In addition, the concept of "abuse of right" is found in other legal systems than Swiss law, and its precise meaning may vary from

one jurisdiction to another; this does not make things easier. However, and also again, this does not mean that one should simply stop at one's own incomprehension.

To summarise, and this summary relates only to Swiss law, Article 2(1) of the Swiss Civil Code establishes an overarching principle under which parties should act to a minimum standard of decency and honesty, including in business. The sanction is set out in Article 2(2), under which behaviour that violates the general duty is "not protected." Thus, an "abuse of right" relates to cases where a party has a right under the law or the contract, but seeks to enforce that right in a way that "manifestly" offends the minimum standards of decency and honesty to which all parties are held.

Explained in these general terms, the concept remains very hazy. That said, in terms of regulating the interactions between members of a given society, it is hardly exceptional. To take one example, the fact that equity developed in the Courts of Chancery was to correct inequities to which the application of the law could lead.

Moreover, when one analyses the concrete examples in which Swiss courts have made a finding of "abuse of right", the concept becomes rather familiar and certainly not difficult to grasp. Examples include *venire contra factum proprium* (a good example being the reliance on the formal invalidity of a long-term contract of which the performance had been accepted for a significant time). Another example is the case where a party exercises a right, but in a manner that is incompatible with the reason why that right is afforded in the first place (for example, purely vexatious (mis)use of land ownership rights in vicinal relations).

And, finally, one must not lose sight of the requirement that the abuse of right be "manifest." In other words, Swiss law operates on the assumption that a party does not need to justify why it is exercising a right. In order to paralyse the exercise of the right, or to mitigate the consequences of the right being exercised, the other party must prove that the case passes a very high threshold. Thus, cases where "abuse of right" is argued successfully are few and far between. For that matter, most Swiss practitioners see this defence as a last resort – as in the famous etching by Honoré Daumier on courtroom antics, recommending that when a case seems irretrievably lost, the only thing left for the advocate is to feign sudden illness in the courtroom. And Swiss and non-Swiss practitioners would be well-advised to bear in mind that the reflexive first instinct of courts or arbitral tribunals is to harbour suspicion that an "abuse of right" defence is actually the refuge of a scoundrel.

Conditions precedent or subsequent and "prevention"

A final example of the not-so-difficult-to-understand and the not-so-internationally-exceptional operation of "good faith" in Swiss law is Article 156 of the Swiss Code of Obligations. Taking again the unofficial translation from the website of the Swiss Confederation, this provision reads as follows:

> *C. Joint provisions*
>
> *II. Prevention in bad faith*
>
> *Article 156*
>
> *A condition is deemed fulfilled where one of the parties has prevented its fulfilment by acting in bad faith.*

The reference to "bad faith" here is another source of incomprehension. It should not be. The provision means that, while (unless agreed otherwise) a party has no duty to take actions that would lead to the fulfilment of a condition precedent (or a condition subsequent), it may not undermine the parties' agreement by taking positive actions (or making deliberate omissions) that would prevent the condition from materialising. A good example applies to pay-if-paid clauses. If, for example, there is a pay-if-paid provision in a subcontract under which the subcontractor is paid only if and when the main contractor is paid by the owner, the main contractor cannot stymie the subcontractor's right to receive payment by neglecting to make payment demands from the owner. If the main contractor makes no such efforts without any justification, the payment condition will be deemed to be fulfilled. Similar principles apply when a contract provides that party A must pay to party B only if and to the extent that party A receives indemnity payments from its insurer; in that case, if party A makes no demands, the insurance payment is deemed to have occurred.

Once more, this is not exceptional. On the contrary, it is very similar to the Common law doctrine of prevention, with which it obviously shares an unsurprising policy goal.

Goodbye Yellow Brick Road?

At the start of The Wizard of Oz, after the house has been sucked up into the vortex of the volcano and deposited in a faraway land, Dorothy remarks to her dog, "*Toto, I have a feeling we're not in Kansas anymore*." This (without the eerie background music or the Munchkins peeping through the greenery, and having replaced "Kansas" with "Switzerland") is the feeling I get so often when "good faith" and Swiss law are discussed at certain conferences. Although this President's Message takes only a few examples, it is hoped that the reader will understand why I get that

impression, and perhaps even agree that it is time to choose more realistic descriptions instead of another stroll down the Yellow Brick Road.

ELLIOTT GEISINGER

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