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UNFAIR CLAUSES IN INSURANCE CONTRACTS AND DRAFT SERBIAN CIVIL CODE

REVIEW ARTICLE

Abstract

The author analyses the provision of the Draft Serbian Civil Code on unfair clauses in insurance. After the explanation of the term and of the importance of unfair clauses, the author presents the arguments in favour of this institute in the field of insurance. The subject provision of the Draft is analysed in the largest part of this paper. The author firstly points out the shortcomings in terminology used in the Draft, and subsequently analyses the provision. Despite her positive attitude to the attempts at creating the regulations on unfair clauses, the author highlights different arguable questions and the issue of non-compliance with the effective regulation on consumer protection. The author argues that unless the analysed deficiencies are remedied in the proposed manner, the efficient protection of the weaker contracting party will be challenged.

Key words: *Unfair clauses, Insurance Contract, Consumer, Law on Consumer Protection, Draft Civil Code.*

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1. Introduction

Unfair clauses are, without a doubt, one of the institutes of consumer contract law which has created high expectations since the adoption of the Directive on Unfair Terms in Consumer Contracts.[2] A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.[3] Unfair clauses are part of the consumer contracts.[4] In addition, they are not always the consequence of abuse of economic power of one party, but the result of its economic supremacy over the other party or better knowledge in the field in which it specialises.[5] This is derived from the fact that the terms are drafted in advance by a stronger party, that is, by a professional. Unfair terms relate to all contracts between professionals and consumers, regardless of their nature and subject.[6] The fact that there are special rules applying to a contract (e.g.: insurance contract, loan agreement) does not preclude the application of general consumer protection rules.[7]

The application of unfair clauses is not only reserved for concluded contracts but also relates to the model contracts and standard contracts.[8] This may be any contract term in writing. A contract term does not necessarily have to be contained only in the contract but also in the annex to the contract, invoice, etc. In

[2] *Directive 93/13 concernant clauses abusives dans les contrats conclus avec les consommateurs.* This is the Directive which introduces *de minimis* harmonization. Unlike the Directive 93/13, the Directive on Consumer Rights 2008/83 of 8 October 2008 adopts the principle of maximum harmonization. However, this Directive has not brought material changes regarding unfair terms. Even after the adoption of the Directive 2008/83, the Directive 93/13 has actually remained unchanged. The change introduced by the Directive 2008/83 relates to the obligation of the member states to regularly inform the Commission of any change in the regime of unfair terms of consumer contracts, particularly if such changes extend the unfairness assessment to individually negotiated contractual terms and to the terms on the subject matter and price, as well as to the content of the list of unfair terms (Article 32).

[3] For more detail on unfair clauses refer to: V.: Nataša Petrović Tomić, *Protection of Consumers of Insurance Services – Analysis and Proposal of Promotion of Regulatory Framework,* Faculty of Law in Belgrade, Belgrade 2015, 304-380.

[4] The scope of application of the Directive 93/13 is restricted to B2C contracts, that is, the contracts or contractual clauses unilaterally defined by the trader. Actually, the Directive requires that each clause is examined separately. In addition, it is not mandatory that the contract is in writing or contained in a single document. Also: Silvija Petrić, „O problemu nepravednih odredaba potrošačkih ugovora u pravu Evropske Zajednice i pravu Bosne i Hercegovine", *Collection of Papers of the Faculty of Law in Mostar*, no. XV/2002, 208.

[5] Marko Đurđević, „Primena pravila o nepravičnim odredbama opštih uslova formularnih ugovora posle donošenja Zakona o zaštiti potrošača", Harmonisation of Serbian Business Law with the EU Law (2012), Beograd 2012, 382.

[6] Jean Calais-Auloy, Henri Temple, *Droit de la consommation*, Dalloz, Paris 2010, 216.

[7] Ibidem.

[8] Ibidem.

terms of the nature of the clause, it may relate to the payment method or delivery of goods, division of risks, limitation of liabilities or guarantees, terms of performance or cancellation of the contract, etc.[9] However, the provisions on unfair clauses are not applied to the definition of contract subject or the amount of price.[10] They also do not apply to the contract in its entirety.

Despite the fact that today, consumer protection is an important objective of any legal and social system, some authors consider it unnecessary in the area of insurance contracts. In their opinion, the protection provided for in the regulation on insurance is sufficient and excludes the application of regulations on unfair clauses.[11] According to a reputable French theoretician, the battle against unfair clauses under insurance law is an old and continuous battle, and is fought by the set of imperative provisions of a legal or reglementary character. The application of a new branch of law and rules regulating unfair clauses cannot be analysed in the same way in the presence of special regulations on insurance contracts which are well familiar with the protective norms, and in the presence of the fields where such rules do not exist.[12] In addition to this quite radical attitude, there are authors who think that the regulations on unfair clauses are applied to the insurance contracts only in a subsidiary manner.[13]

However, despite the opposed theories, today, it is a common knowledge that insurance consumers enjoy the protection of special laws intended for consumer protection - even more so when had in mind that the insurance law does not exclude the application of general norms on unfair clauses contained in the consumer legislation. The application of unfair terms to an insurance contract is justified by the very nature of that contract. In the majority of cases, insurance contract is an adhesion contract.[14] Thus, the insurance consumer, who has no technical and legal expertise or economic power to negotiate the terms of the contract pre-formulated by the insurer, is in need of protection against the unfair clauses.[15] The protection of insureds against unfair clauses is justified for the following reasons: 1) due to special legislative technique of a complex contract; 2) due to the subject matter of the contract which should ensure the safety of private

[9] Jean Calais-Auloy, Henri Temple, 217.

[10] Ibidem.

[11] Jerôme Kullmann, „Clauses abusives et contrat d'assurance", *Revue Générale du Droit des Assurances*, 1996, 11.

[12] „ The unfair clauses' virus cannot infect insurance law, for it periodically receives legal and reglementary vaccines or court treatments for which the contractual imbalance between the rights and obligations of the contracting parties is rarely seen in this domain." J. Kullmann, 40.

[13] André Favre-Rochex, Guy Courtieu, *Le droit du contrat d'assurance terrestre,*L. G. D. J., Paris 1998, 21.

[14] French Cassation Court stressed that the fact that one clause is existing in the adhesion contract is not sufficient to regard it as unfair. Cass. Civ. 1er, 16 janvier 2001.

[15] Yvonne Lambert-Faivre, Laurent Leveneur, *Droit des assurances,* 13 édition, Dalloz, Paris 2011, 107.

life; 3) due to economic power of insurance company writing insurance contracts as „mass consumption products " and 4) due to factual state of affairs (presence of unfair terms in insurance contracts).

In the application of unfair clauses, however, the nature of insurance contracts represents problems. Even though this contract basically binds the insurer to pay the insurance indemnity upon the occurrence of the insured event, the insured, unlike the insurer, has numerous obligations in addition to the key obligation to pay the insurance premium (to report the change in risks and relevant circumstances, to take preventive measures, to report the occurrence). Thus, it is not easy to establish whether a particular clause causes imbalance between the rights and obligations of the parties to insurance contract. Being sensitive to these problems, the French Cassation Court is of the view that *when establishing an unfair character of the term of an insurance contract, a judge should compare the advantages and benefits received by the insurer and the disadvantages suffered by the insured.*[16]

Another problem in connection with the application of unfair clauses to the insurance contract is the limited scope of their application. Unfair terms relate only to consumer insurance contracts. The norms on unfair terms cannot be applied to the contracts written by the professionals. This is what we consider as the major limitation of the regulation on the unfair clauses. An insured/professional is in need of protection from unfair terms as well as the insured/consumer. The third problem occurring in connection with the application of unfair clauses is the definition of terms which may be declared unfair. Can all the terms of insurance contract be unfair, or some of them have a „privileged" status and cannot be declared unfair? The answer to these questions will determine the efficiency of protection provided to insurance service consumers by the regulation on unfair terms.

2. Analysis of Draft Civil Code

We commend the authors of the Draft Civil Code (hereinafter: Draft CC) for intending to incorporate therein an extremely important provision on unfair clauses in insurance contracts. This represents an attempt to adopt an institute which, in a small number of EU member states, specially covers insurance contracts. Actually, the authors were inspired by the Principles of European Insurance Contract Law (hereinafter: Principles) in which this idea is represented.[17]

The question is raised as to what is the aim of regulating unfair clauses in the Draft CC if the provision thereof already existed in the Civil Procedure Law? What

[16] Cass. Civ. 1er, 12 mars 2012.

[17] Principles of European Insurance Contract Law.

will be the relationship between the rules contained in these two regulations? We are of the opinion that the adoption of the CC i.e. the provision regulating unfair clauses in insurance contract will not completely exclude the application of the Civil Procedure Law. This law will remain effective for all (other) matters of insurance consumer protection. In the area of insurance consumer protection, there is a special norm defining the term of unfair clauses. This represents a step forward towards the provision of a better protection of insurance consumers, which is likely to encourage consumers to more frequently initiate proceedings for annulment of unfair terms.

We support the introduction of special regulations on unfair clauses in insurance contracts for minimum two reasons. The first is the *recognition of specific nature of insurance contracts* i.e. of contractual terms to which this important institute will be applied. Unfair clauses in the Civil Procedure Law were drafted as an institute to be applied to all consumer contracts. To that extent, deviation from the general regime of unfair clauses regulated by the Civil Procedure Law should be understood as the recognition of the specific nature of insurance contract, on the one hand, and personality of insurance consumers, on the other. The second reason is the *possibility to apply the institute of unfair clauses in all insurance contracts*. In addition, this institute can and must play a particular role in connection with observing the principles of equivalence of mutual considerations in commercial insurance contracts. Unfair clauses in the Civil Procedure Law can be used only in terms of consumer contracts. When it comes to the other, non-consumer contracts, the Civil Procedure Law is not applied. Since the Draft does not limit the application of unfair clause institute to consumer contracts, there is no reason precluding the said provision to be used for the purpose of protection of commercial insurance policyholders.

This proposal is in compliance with the Principles. Namely, according to the Principles, beneficiary *of protection is any policyholder, insured, and insurance service beneficiary, regardless of whether he is a consumer or a professional*. This specifies the protection against unfair clauses and adjusts it to the specific nature of the insurance contracts. The Principles recognise the argument that all insureds, be they consumers or professionals, have the need to be covered by the protective function of unfair clauses. As pointed out in theory, the insurance contract is marked with imbalance which is inherent to its nature. Thus, the capacity of contracting parties is a secondary criterion for identification of unfair clauses.[18] Therefore, the Principles adopt *the objective concept of identifying unfair terms*, because they refer to the subject of such terms and not to the capacity of the

[18] C. Lisanti,„La polise des clauses abusives dans les principes du droit européen du contrat d'assurance", Les principes du droit européen du contrat d'assurance (séminaire), *Revue Générale du Droit des Assurances,* No. 3/2009, 1012.

parties.[19] This is a considerable difference in comparison to the Directive 93/13 and national legislations of EU member states which adopt a subjective criterion for identification of unfair clauses.

Regarding the very name of the institute, we consider that the title first proposed is too broad and evokes the institute of misuse of rights. Despite the fact that unfair clauses are indisputably the expression of prohibition of misuse of rights in a broader sense, today they have a clearly defined meaning and scope of application. The term « unfair clauses » was firstly used by Berlioz in his doctoral dissertation as a legal expression of the idea of the abuse of economic power, which was reflected on the very name of the clauses (Eng.: *unfair clauses*; French: *les clauses abusives;* German: *Missbräuchliche Klauseln*). What is even more important is the fact that there is a consensus regarding terminology: they are called unfair or dishonest clauses. Other names are less common.[20]

How did the authors of the Draft CC define unfair clauses? This is a clause which was not the subject of special negotiations and which, contrary to the requirement of good faith and fair dealing, creates a considerable inequality in the contractual rights and obligations, to the detriment of insurance consumers, insureds, or insurance beneficiaries, taking into account the type of insurance contract, terms of the contract, and circumstances prevailing at the moment of contract conclusion. Generally speaking, the authors of the Draft based the text on the achievements of comparative law in the area of unfair clauses.[21] To better explain this institute, we will analyse both elements separately.

2. 1. Term which has not been Individually Negotiated

According to the Directive 93/13 and the Principles, the first element of an unfair clause is the lack of individual negotiations: entirely or regarding particular contractual provisions.[22] The term which has not been individually negotiated is the term drafted in advance and the consumer was not able to influence the substance

[19] Ismail Alkhalfan, La protection contre les clauses abusives du contrat d'assurance, Université Montpellier I, 2012, 301.

[20] In addition to these terms, other terms are also used to denote the clauses which make contractual imbalance to the detriment of one party: „unreasonable terms", „unjust terms", „dishonest terms". The term „unreasonable terms" is used by a reputable professor Jelena Vilus (Jelena Vilus, „Nekorektne klauzule u ugovorima sa potrošačima", Foreign Legal Life, no. 1-3/1996, 131-145). We are of the opinion that the term *unfair clauses* is best suited to the spirit of the Serbian language and substance of the institute. This is because the Directive 93/13 sanctions only considerable contractual imbalance to the detriment of consumers, which frustrates the principle of fairness.

[21] This definition largely "resembles" the definition found in the Principles (Article 2: 304).

[22] The Directive actually considers the contracts which are most commonly concluded in practice based on the permanent and general proposal. The same applies to oral agreements between the parties, if their content has not been negotiated. Also: Nevenko Misita, „Uz desetogodišnjicu Direktive 93/13 o nepravičnim ugovornim odredbama", *Proceedings of the Law Faculty in Rijeka*, Vol. 25, No. 1/2004, 24.

of the term. This also includes the provisions which are not the part of standard contracts or primary contracts, however, they are contracted for a particular contract without leaving the possibility for the consumer to negotiate them.[23] The fact that particular terms of consumer contract were subject to individual negotiations does not influence the possibility to declare other contractual terms unfair, if based on the overall analysis of the contract it can be seen that it is a pre-formulated standard contract.[24] In other words, the selection of several terms or set of terms does not constitute negotiations.[25]

Regarding the circumstance that "special negotiations" have not occurred, the Draft defines that a clause is considered non-negotiated when it is drafted in advance by the insurer and therefore the policyholder could not influence its content, particularly in the context of application of general terms of a formulated contract (standard insurance terms and conditions). Thus, *the presumption of non-negotiation* is applied to all clauses of insurance terms and conditions. This facilitates the evidencing of one element of the term *unfair clause*, which is very useful for enhanced insurance consumer protection. There is one more rule in connection with the answer to the question if the negotiations have occurred. Namely, the fact that certain aspects of the clause or one particular term of the contract were specially negotiated does not preclude the application of the rule of this article to the remaining part of the contract.[26] The fact that a particular clause or its part is the result of bargaining does not mean that the evidence cannot be provided that other clauses are not the result of negotiations.

The question is posed as to who has the burden of proof that a particular contractual term was individually negotiated? If a trader claims that the contractual term in the pre-formulated standard contract was negotiated individually, he is obliged to present the evidence thereof. In other words, there is a presumption that

[23] Katarina Ivančević, *Consumer Legal Protection of both Insurance and Bank Service*, Doctoral dissertation thesis, Faculty of Law of Union University, Beograd 2010, 254; Nevenko Misita, 30.

[24] The focus is on the lack of negotiations regarding an individual contractual term and not regarding the entire contract. Thus, for the application of the Directive, it is not necessary to stress that all contractual terms were not negotiated. It is sufficient that there is the lack of negotiations on individual terms. In: Mario Tenreiro, Elena Ferioli, „Examen comparatif des législations nationales transposant la directive 93/13/CEE", The „Unfair Terms" Directive, Five Years On, Evaluation and Future Perspectives, Brussels Conference, 1999, 14.

[25] The point is that professionals are mainly not willing to enable the consumers to discuss the provisions which are drafted in advance. Even if they agree to certain „negotiations", they are mostly reduced to bargaining about the elements of particular contractual terms. The fact that one or several clauses are the result of negotiations does not mean that the bargaining positions are equal. For more details refer to: A. Malcom Clarke, *The Law of Insurance Contracts,* Informa Law, 2006, 592; Ana Keglević, „Pre-contractual Information Duty and Unfair Contract Terms – Open Questions and Dilemmas" – *Insurer's Precontractual Information Duty*, Turkish Chapter of AIDA, Istanbul 2013, 83.

[26] These rules are taken over from the Principles (Article 2: 304).

a contractual term, which was drafted in advance, was not subject to negotiations and that the consumer did not participate in its copy editing. However, the practice has shown that the initial premise of the Directive about the warranty of fairness through individual negotiation is not sufficiently precise. This is because soon the traders „thought of "how to frustrate the said provision. Namely, they have developed the practice of concluding consumer contracts by means of standard contracts, with the clause in which the consumer confirms that he has „negotiated and expressly accepted "standard insurance contract and particular contractual terms.[27]

Unlike the Directive 93/13, Serbian Law on Consumer Protection deviates from this term and provides for the possibility to analyse each contractual term through the prism of unfair clauses, and not only that which was not subject to negotiations,.[28] This definition has its good and bad sides. Its good side lies in the fact that its application is not limited only to the provision of standard contracts, but is also applied to the provisions which were negotiated. Despite the fact that this represents the deviation from the Directive's provision, we consider it useful. It will prevent the disputes in connection with drawing the line between standard provisions and special contractings which member states face. For the legal system which is just beginning to adopt the concept of consumer protection, and notably for the courts which apply this concept, this will represent a considerable benefit.

As rightly pointed out by the French Cassation Court, the fact that the term is contained in the adhesion contract does not mean *ipso facto* that it is unfair.[29] The lack of negotiations as a phase before the conclusion of a contract is not necessarily a sign that the position of the party entering into the adhesion contract is exploited.[30] Similarly, in the field of unfair terms, it is not justified to *a priori* eliminate the clauses from the individually negotiated contracts. Even the negotiated contracts may contain unfair terms based on the dominant position of one party or due to the ignorance of the other party.

Therefore, there is a mismatch between the definition of unfair terms provided in the LCP and the definition of unfair clauses in the insurance contracts

[27] In this way, the application of the provisions of the Directive is frustrated, to the detriment of the consumers. In: Nevenko Misita, 25.

[28] According to the Law on Consumer Protection (*Official Gazette of RS*, no. 62/2014 and 6/2016; hereinafter: LCP), unfair clause is any contractual term of a consumer contract, including special contracting the content of which was or could be negotiated between the consumer and the trader, and general provisions the content of which was drafted in advance by the trader or a third party which, contrary to the requirement of good faith, results in a considerable imbalance between the rights and obligations of the contracting parties to the detriment of the consumer (LCP, Article 43 paragraph 2).

[29] „Le seul fait qu'un contractant relève da le catégorie des contrats d'adhésion ne suffit pas à démontrer que telle clause particulière a été imposée par un abus de puissance économique", Cass. Civ. 1re, 12. mars 2002.

[30] Ismail Alkhalfan, 77.

provided in the Draft. If the proposal for the Draft is adopted, there will be one (general) regime of unfair clauses, which will be applied to all consumer contracts (and which will legitimately deviate from the EU *acquis*!), and the other (special) regime, anticipated only for insurance contracts. Even though at first glance the differences between the effective LCP and proposal for our legislation *de lege ferenda* seem unjustified and prejudicial for legal safety, this is actually not the case. The solution proposed in the Draft is generally accepted in the EU member states and in the instruments of further harmonisation of insurance contract law. We have already stressed that the CPL deviates from the provisions of the Directive 93/13 which, at this point, we evaluated as meaningful deviation. However, having in mind that the insurance contracts are largely concluded according to the standardised terms and contracts, the keeping of the term on the lack of negotiations results in excluding from the field of unfair terms the application *rationae materiae* of only those contracts which cover so-called major risks, and not all commercial insurance lines.

2. 2. Considerable Imbalance between Rights and Obligations to the Detriment of Consumers

Key element of unfair clauses is the creation of a considerable imbalance between the contractual rights and obligations. The concept of imbalance is analysed by taking into account *the relationship between rights and obligations of the contracting parties*.[31] "Rights and obligations of consumers are compared with the rights and obligations of the trader. Contracting situation of each contracting party should be considered globally and only comparable elements should be compared."[32] The two and the same types of rights and obligations should be considered in parallel (e.g.: the terms on cancellation of the contract by the consumer, and by the trader) or different rights and obligations should be analysed where there is an intellectual correlational relationship (e.g.: the clause on limitation of liability and the clause on price).[33] However, not any type of imbalance is taken into account. Instead, it is required that the imbalance is considerable. *Imbalance is considerable when there is an obvious disproportion between the rights and obligations of the parties.*[34] *A contario*, a simple absence of balance, that is,

[31] Unlike the French and English version of the Directive which contain the term „considerable imbalance", the German translation contains the term „considerable and unjustified imbalance".
[32] Claire-Marie Peglion Zika, *La Notion de Clause Abusive*, Thèse de doctorat, Université Panthéon-Zika, École doctoral de droit privé, 2013, 302.
[33] Claire-Marie Peglion Zika, 302-303.
[34] Ana Keglević, „Zaštita osiguranika pojedinca kod ugovora o osiguranju", *Proceedings of the Law Faculty in Rijeka,* no. 1/2013, 222.

the absence of economic equivalence between the rights and obligations of contracting parties does not mean a considerable imbalance.

Neither the Directive nor the Principles define the disturbance of contractual balance between the rights and obligations. They also do not define what is considered to be to the detriment of consumers' interests. Both of these sources only require that the disturbance of contractual balance is considerable. It is left to the case law in member states to „deal with" the definition of these terms when it comes to particular cases.[35] This, in itself, sufficiently speaks of the achievements made in member states regarding the harmonization of contract law. The interpretation of the general clause by the courts of different member states leaves room for too many interpretations.[36]

It should be noted that the term "inequality" is not the same as "imbalance". As pointed out in theory, the principle of equality between contractual rights and obligations (Article 15 of the Law of Contracts and Torts) is a „predecessor" of a considerable imbalance. Equality of rights and obligations exists when in the conclusion of the contract, the principle of good faith was observed, but also if the contract terms are the expression of the same principle.[37] Plain disproportion between rights and obligations to the detriment of a consumer does not mean unfairness! *The meaning of the principle of equivalence between mutual considerations does not lie in the simple (line) equality of mutual considerations but in the observance of the nature of a particular contract*. This is even more so when had in mind that the insurance contract represents a typical aleatory contract. Therefore, the terminology requires adjustment for the purpose of avoiding disputes and clarification of situations to which the said provision potentially relates. If the term « inequality » was to be kept, this would leave room for potential misuse of this institute by the insurance service consumers.

[35] This is a legal standard comprising of two elements which require interpretation. The fact that the battle against unfair terms is based on a legal standard represents the ace up consumers' sleeve for it increases their odds to subject a particular form of imbalance to the test of unfairness. Semantically speaking, the imbalance should be understood as "lack of proportion ", "inequality", "disparity". To sanction inequality with unfairness, the former should be considerable. The term "considerable" firstly indicates that this is not just any form of inequality of contractual considerations. Underlying a considerable imbalance between the contractual rights and obligations there is a significance, severity, and seriousness of disproportion between parties' rights and obligations. See: Claire-Marie Peglion Zika, 245- 256.

[36] A term proclaimed fair by courts of a country may be proclaimed unfair in another member state. This does not resolve the problem of different level of consumer protection in particular countries, which induced the adoption of numerous „consumer" directives.

[37] V.: Andrea Fejös, „Fairness of Contract Terms in European and Serbian Law", *Strengthening Consumer Protection in Serbia*, Liber Amicorum Svetislav Tabaroši, Thierry Bourgoignie, Tatjana Jovanić (ur.), Faculty of Law of the University of Belgrade, Beograd 2013, 192.

2. 3. Criteria for the Assessment of Unfair Clauses

We commend the fact that when defining the term of unfair clauses it was referred to the type of insurance contracts and terms of the contracts. This deviates from the criteria that the LCP prescribes for consumer contracts (the LCP recognises subjective and objective criteria). Based on the assessment of these circumstances, the court establishes if there is a disproportion between the contractual rights and obligations or any other form in which the unfairness is manifested. For the protection of insurance service consumer it is important that unfair clauses may be contained not only in the contract itself (policy), but also in the insurance terms and conditions. Actually, the majority is derived from the interpretation of insurance terms and conditions. The same cannot be said about the reference to the circumstances at the moment when the contract is concluded. This is because the principle of contractual (im)balance is assessed not only based on the circumstances existing at the moment of contract conclusion, but also based on the circumstances occurring at the moment of performance of contractual obligations.

As pointed out in theory, it is much easier to achieve contractual balance when concluding the contract instead of trying to strike it subsequently, at the moment of its performance.[38] Since the fairness is assessed by taking into account the type of goods or services and all other criteria which were relevant at the time of the contract conclusion, the Directive 93/13 does not take into account the circumstances which may occur after its conclusion. This solution is not in accordance with the consumers' interests. The protection from unfair clauses should be achieved in both contractual phases, modelling upon certain foreign laws.[39] The protection in the phase of contract conclusion is achieved by eliminating unfair clauses from the contract, following the activities of a consumer association or court decision. As for the performance of the contracts, courts have the power to declare the clauses null and void, not only in the proceedings initiated by consumers, but also ex officio.[40]

The assessment of unfair character of clauses must be made in the light of the principle of good faith.[41] Court practice and legal theory have developed the *criterion of reasonableness of a clause* as a key criterion for the assessment of its compliance with the principle of good faith. The consumer needs to be protected against sudden situations. Bargaining positions are of particular importance.

[38] Ismail Alkhalfan, 23.

[39] Benoît Moore, „Les clauses abusives: Dix ans après", *Revue du Barreau,* Tome 63, 2003, 71-72.

[40] Ismail Alkhalfan, 24.

[41] In the preamble of the Directive 93/13 it is stated that in making an assessment of good faith, particular regard shall be had to the strength of the bargaining positions of the parties, whether the consumer had an inducement to agree to the term and whether the goods or services were sold or supplied to the special order of the consumer.

Namely, it is important whether the contracting parties are equal. Courts pay close attention to understanding the transaction of a consumer and if a consumer had a choice in assuming contractual obligations.[42] Therefore, a key issue is whether the consumer was able to obtain an alternative information considering the available time and costs.[43] This doctrine also introduces additional criteria which may be used when reasonableness of a clause is analysed: whether another contract can be concluded without a disputable clause and what is the consumer's understanding of the clause. If the consumer had a choice and was able to conclude another contract without such a clause, or he knew our could have reasonably known about the existence of the provisions, the clause will not be declared unfair.

2. 4. Legal Consequences

As regards legal consequences of deciding on an unfair clause, the Draft specifies that such a clause does not bind the policyholder, insured or insurance beneficiary. This is about the wording which is taken over from the Principles.[44] In this way, the nature of the sanction is not specified. It can be both nullity and inopposability. The contract shall continue to bind the parties if it is capable of continuing in existence without the unfair term. If not, the unfair term shall be substituted by a term which reasonable parties would have agreed upon had they known the unfairness of the term.[45] This is a completely new and original sanction, which is not known to the Directive 93/13 and national laws. The substitution of an unfair clause by another clause is one of the options for the court. Reference to the „clause which the parties would reasonably adopt " represents a possible course which a court may take in considering the redrafting of the clause.[46]

Thus, there are two possible scenarios. The first is that the insurance contract may be legally effective without an unfair term. In such case, the contract remains effective without any additional modification. However, if the contract is not capable of continuing in existence without an unfair term, *such term shall be substituted by a term which reasonable parties would have agreed upon had they known the unfairness of the term*. Therefore, the amendment to the contract

[42] Ana Poščić, „Nepravična klauzula u potrošačkim ugovorima", *Collected Papers of the Faculty of Law in Split*, 2/2006, 181.
[43] Ana Poščić, 183.
[44] The Principles specify that an unfair term „shall not be binding on the policyholder, insured, or the beneficiary".
[45] The Principles specify that: „The contract shall continue to bind the parties if it is capable of continuing in existence without the unfair term. If not, the unfair term shall be substituted by a term which reasonable parties would have agreed upon had they known the unfairness of the term." (Principles, Article 2: 304).
[46] Alkhalfan, 2012, 307.

is proposed as the second option by incorporating another clause based on the principle of reasonable expectations. Currently, it can be polemicized about the willingness of our insurance law and judicial system to apply this, basically Anglo-Saxon principle.[47] The principle of protecting reasonable expectations notably relates to the insured, that is, the consumer of insurance services who is provided protection by entering the clause in the contract the application of which the consumer would have negotiated had he known that the relevant clause is unfair. Thus, the Draft wording that the unfair term shall be substituted with the term the parties would have agreed upon had they known the unfairness of such term should be understood in this very sense.

The unfair term, which is declared null according to the LCP is not binding upon the consumer. However, the nullity affects only the contract term which is unfair (or not in accordance with transparency requirements as per Article 44 of the LCP), and not the entire contract. If the consumer contract can survive even without the unfair term, it shall be legally effective.[48] If the contract cannot survive without the challenged term, it shall also share the fortune of such unfair term and shall become null and void. For the consumer, no obligation may arise from a null contract. However, if the parties have performed the obligations under a null contract, the rules of the Law of Contracts and Torts shall apply.[49]

Despite the fact that legal consequences of unfair terms in insurance contracts are regulated in a quite new and more demanding manner, which will certainly present a challenge for the courts, the underlying idea is to maintain the insurance contract in force. Since the insurance contract in the twenty first century is one of the basic contracts within the portfolio of contracts concluded by an individual, this idea is fully justified. The court must not stop at the recognition that the insurance contract is not capable of continuing in existence. Instead, it must keep it in force by finding a clause which matches the reasonable expectations of the parties.

[47] The starting point of the doctrine of reasonable expectations is to observe reasonable expectations of the policyholder, since he is the one usually taking out the insurance cover relying on the insurance companies or agents, for he does not possess the knowledge which would enable him to analyse insurance policy. When establishing reasonable expectations of insureds, a particular focus should be placed on whether the insurer has reasonably and in detail informed the insured of the insurance terms and conditions or exclusions, and whether, in that particular case, the issue is widely known. The most common situation for the application of this theory is when the insurer misrepresents the content of insurance or misleads the insured. For more details: Nataša Petrović Tomić, 300-301.

[48] This does not exclude the obligation of a party at fault for the conclusion of the null and void contract to compensate the other party for the loss suffered due to the nullity of the contract, if the latter was not aware or, according to circumstances, was not supposed to be aware of the existence of the cause of nullity (Law of Contracts and Torts; Article 108).

[49] Law of Contracts and Torts, Article 104.

2. 5. Exclusions from Application

The Draft prescribes that the mentioned Article shall be applied to the clauses which limit or alter the cover, however, it shall not be applied to: adequacy of the sum insured and premium, or the clauses containing essential description of the cover granted (accepted) or stipulated premium, provided that the clause is in plain and intelligible language.[50] The Directive 93/13 also has exceptions from the application of the institute of unfair terms in insurance contracts.[51] Instead of the term « subject matter of the contract » (which is rather of a theoretical nature[52] and leaves room for interpretations) the Draft speaks of the non-application of unfair terms to the terms relating to "essential description of the cover granted". The exceptions from the application of the institute of unfair clauses can be acceptable only if the subject clause is in plain and intelligible language.

As we have pointed out on numerous occasions, such choice considerably limits the outreach of fairness test. The terms on the subject and price of the contract cannot be qualified as unfair, for this would influence the contract structure. These are the terms which make the core of the contract, „legal and economic commitment *ratio*."[53] As these are the terms which comprise the core of the contract, it is clear that for a consumer they are of the utmost importance. Paradoxically, the most important clauses are excluded, whereas less important ones are subjected to control. Actually, the application of fairness test remains reserved for so-called satellite clauses: like those relating to term and termination of the contract; reporting of an insured event; loss of rights, providing evidence and jurisdiction for resolution of insurance disputes. Such solution is, in its concept, *contradictio in adiecto*. If the aim is to preserve the contractual balance between rights and obligations, control of fairness is more focused on essential elements of the contract. Deviation is partly minimised by the fact that the Directive 93/13 stipulates that the terms on the subject and price shall be taken into account when assessing the unfairness of other contract terms. The importance of deviation is even greater when had in mind that the disturbance of contract balance may be proved based on the combination of clauses defining the main subject matter of the contract, or the price and other clauses ".[54]

[50] Similarly: Principles, Article 2. 304.

[51] „The terms which clearly define or circumscribe the insured risk and the insurer's liability shall not be subject to the assessment of unfair character, since these restrictions are taken into account in calculating the premium paid by the consumer."

[52] For more detail refer to: Nataša Petrović Tomić, 320-323.

[53] Silvija Petrić, 220; Marc Bruschi, „La protection des consommateurs contre les clauses abusives dans la contrat d'assurance", La protection du consommateur d'assurance: entre permanence et nouveautés (Dossier), *RGDA*, No. 6/, 2014, 366.

[54] Nataša Petrović Tomić, 321-322.

Therefore, there are two categories of clauses that cannot be declared unfair in insurance contracts: 1) clauses on the cover. The Directive justifies the exclusion of the clause which defines the subject by the fact that in insurance contracts, premium is usually calculated by taking into account the subject of cover and circumstances relevant for the risk. In addition, this exclusion is justified, because the laws regulating contractual matters of insurance require transparency of the primary insurance contracts, clearness and precision, and define the content of the contract in advance, and there are standard definitions of terms and clauses of the contract.[55] 2) clauses relating to the adequacy of the price of goods and services. The purpose of this exclusion is to prevent the consumers from abusing the institute of unfair clauses for the purposes of challenging goods or services. From the interpretation of the term relating to the price, it can be concluded that the adequacy (appropriateness) of the price, as consideration for the benefits arising from the agreement, cannot be the subject of control.[56] Other elements of the agreed price – like the method of calculation, method of payment, possibilities and terms for changing the price– shall be subject to fairness test.[57]

When it comes to the insurance contract, this exclusion can apply to the clauses introducing the upper limit of insurer's liability per any one insured event, or a deductible. These clauses limit insurance cover in terms of its extent. They do not define the subject matter of the contract but more closely determine the extent of cover.[58] The Directive 93/13 assumes that such limitations were taken into account when calculating insurance premium.[59] *A contrario*, if such limitations result in the limitation of cover to such an extent that it seems proportional to the amount of outstanding premium, they may be challenged by reference to the unfair character.[60] It should be noted that not all terms relating to the amount of insurance premium are outside the field of application of unfair clauses. The consumer right does not lose in its topicality in the clauses relating to the manner of defining or changing the premium or payment method.[61] Naturally, provided

[55] Therefore, there is a previous legal intervention in the field of insurance contractual relationship which enables the application of the said exclusions from the unfair clauses. In.: Katarina Ivančević, 253.

[56] Nevenko Misita, „Uz desetogodišnjicu Direktive 93/13.., 28.

[57] Recitals 19 of the Directive 93/13 takes an example of insurance contract. Its terms on insured risks and liability of insurer are not subject to control only if the amount of outstanding premiums corresponds to the scope of insurer's liability. This provides an example that the terns on the amount of price are also within the scope of application of the Directive, and are connected with other contractual terms.

[58] Ismail Alkhalfan, 87.

[59] This exclusion also protects the technical organisation of insurance which is the basis of a sound functioning in the insurance industry.

[60] Ismail Alkhalfan, 87.

[61] For the purposes of clarification: clauses describing the insured risk or circumstances under which the insurer is obliged to pay the indemnity to the insured are not analysed in the context of contract

that by evoking the unfair character, the evaluation of ratio between premium adequacy and cover provided is not affected.[62]

Unlike the Directive and the Draft, in the LCP, the Serbian legislator did not anticipate that the control of fairness of the contract term does not relate to the subject matter of the contract and also whether a proportionate price i.e. consideration was agreed for the goods or services. Serbian courts, therefore, pay attention *ex officio* to the fairness and nullity of contractual provisions of consumer contracts relating to the subject of the contract and adequacy of the agreed consideration. We consider that this should be applied in connection with the insurance contract. In addition, the European Court of Justice is of the view that national legislation can authorise judicial control of unfair character of contract clauses relating to the definition of the contract subject and price, even if such clauses are edited in clear and eligible manner.[63]

3. Conclusion

Generally speaking, Article 1399 of the Draft represents an attempt at creating the regulations on unfair clauses, which are adjusted to insurance contracts. We consider that this idea is basically good and quite modern. Namely, provided that it does not dismiss the proposed Article, upon the adoption of the CC, Serbia will be among those rare countries whose regulatory insurance framework contains special provisions dealing with the issue of unfair clauses in insurance contracts. Despite the fact that the subject Article is largely the result of *copy-paste* approach, we consider that our law regulating insurance contracts, which was traditionally extensively covered within the general source of contractual relationships, will be completed by entering the provision on unfair clauses into the CC.

Drawing on our knowledge of comparative law and practice relating to unfair clauses, we consider that the mentioned provision should be corrected, as follows: Firstly, it requires the corrections in terminology. The first term should be erased (clauses on abuse) and the second term should remain (unfair clauses). Although, if one wishes a consensus in terminology regarding the institute which, for a long time now, has been adopted as *lex specialis* in the area of consumer protection, the authors of the Draft would have to opt for a

fairness. However, the main subject matter of the contract and price/quality ratio can be taken into account when assessing the fairness of other contract clauses. V.: Angelo Borselli, „Cognosceat emptor: on obligation of the insurer to provide information to a potential insured in Europe", *European Insurance Law Review,* 2/2012, 30.

[62] Ismail Alkhalfan, 88.

[63] V.: Jérôme Bonnard, 31.

widely used term of unfair clause. Secondly, one more change in terminology is required, which will have an essential effect. Instead of considerable inequality, a considerable imbalance should be introduced. Considerable inequality to the detriment of a weaker party to the consumer contract is a constitutive element of all definitions of unfair clauses. The term «inequality » used in the Draft is not used by any law or Directive. This is because the idea of protection from unfair clauses is based on the idea to prevent the exploitation of contract imbalance to the benefit of a stronger contracting party, and not on the idea that (some kind of) hypothetical equality in rights and obligations should be preserved. Thirdly, the third paragraph of the mentioned Article should be deleted. Despite the fact that deviations from the application of fairness test are generally accepted in the EU *acquis*, and even in the Principles, we consider that there are no essential reasons to deviate from the solution provided for in the LCP. Namely, the Serbian law does not prescribe this deviation which is subjected to harsh criticism of the European theoreticians. The major objection is that the introduction of the exception from the application of the unfair clauses represents the concession for the insurers and thereby *de facto* the application of this important institute is reduced only to| irrelevant clauses of the insurance contract. Fourthly, modelling upon the comparative law, the Draft could have included the list of unfair clauses which are most commonly used in insurance contracts. This is because only some of the clauses from the black and grey list of the LCP are applicable to insurance contracts. Having in mind the ignorance of courts in connection with insurance law in general, this would be in the interest of a more efficient protection of insurance service consumers.

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