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# Restitution of Performances after Avoidance of Contracts under the CESL and Estonian Law

## 1. Introduction

In October 2011, the European Commission issued a proposal for a regulation of the European Parliament and of the Council on a common European Sales Law<sup>\*1</sup> (CESL). The aim of the future regulation is to improve the establishment and the functioning of the internal market by facilitating the expansion of cross-border trade for business and cross-border purchases for consumers. The CESL rules would apply only upon express agreement of the parties to a cross-border contract. It is contended that the rules of a CESL should maintain or improve the level of protection that consumers enjoy under European Union consumer law.<sup>\*2</sup>

In academic circles, the CESL has already received much attention<sup>\*3</sup>, including suggestions as to how the proposed rules should be redrafted.<sup>\*4</sup> The present article focuses on the text of the proposed CESL as it stands and compares certain aspects of the CESL and Estonian civil law. It has been found in Estonian legal literature that, with regard to contractual remedies and standard terms, the CESL rules provide for more favourable treatment of a consumer than does Estonian law.<sup>\*5</sup> This article focuses on the rules on restitution of performances, with particular stress on the avoided contracts. The rules of Part VII of the proposed CESL on restitution (Articles 172–177) are compared to those of Estonia's Law of Obligations Act<sup>\*6</sup> (LOA)

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<sup>1</sup> COM(2011) 635 final.

<sup>2</sup> Proposed CESL, Recital 11.

<sup>3</sup> See, for example, the bibliography compiled by Ewoud Hondius: E. Hondius. Common European Sales Law: If it does not help, it won't harm either(?). – *European Review of Private Law* 2013/1, pp. 1–12.

<sup>4</sup> Statement of the European Law Institute on the Proposal for a Regulation on a Common European Sales Law COM(2011) 635 final, 2012. Available at [http://www.europeanlawinstitute.eu/fileadmin/user\\_upload/p\\_eli/Publications/S-2-2012\\_Statement\\_on\\_the\\_Proposal\\_for\\_a\\_Regulation\\_on\\_a\\_Common\\_European\\_Sales\\_Law.pdf](http://www.europeanlawinstitute.eu/fileadmin/user_upload/p_eli/Publications/S-2-2012_Statement_on_the_Proposal_for_a_Regulation_on_a_Common_European_Sales_Law.pdf) (most recently accessed on 8.4.2013).

<sup>5</sup> K. Sein. Tarbija õiguste kaitse Euroopa müügiõiguse eelnõus: kas kõrgem tase Eesti tarbija jaoks? ['Protection of consumer rights in the draft of the European Sales Law: A step ahead for Estonian consumers?']. – *Juridica* 2013/1, p. 73 (in Estonian).

<sup>6</sup> Võlaõigusseadus. – RT I 2001, 81, 487; RT I, 8.7.2011, 6 (in Estonian). Available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (most recently accessed on 8.4.2013).

and their application in Estonian legal practice. The aim for the article is to identify the similarities and differences of the two regimes and to evaluate the results from the consumer's point of view, asking which of the two offers a greater level of protection for the consumer.

## 2. Scope of analysis: Avoided contracts

### 2.1. The meaning of avoidance

Article 172 (1) of the proposed CESL provides for application of the rules of restitution in cases wherein a contract covered by the CESL<sup>7</sup> is avoided or terminated by either party. Pursuant to Article 54 (1) of the proposed CESL (hereinafter 'CESL' if not otherwise specified), a contract that may be avoided is valid until avoided but once avoided is retrospectively invalid from the beginning. Similarly the Estonian General Part of the Civil Code Act<sup>8</sup> (GPCCA) provides that a transaction that is avoided is invalid from its inception (§90 (1)). This means that the two sets of regulations agree on the *ex tunc* effect of the avoidance. To avoid the contract, a party must give notice to the other party (CESL, Art. 52 (1); GPCCA, §98 (1)). The rules of Part VII of the CESL do not apply to contracts that are null and void *ab initio* on some other grounds. For example, matters related to invalidity of a contract arising from lack of capacity, illegality, or immorality are excluded from the CESL's scope and thus left within the area of application of the existing rules of the relevant Member State's civil law.<sup>9</sup>

Besides the avoided contracts, the CESL's Articles 172–177 apply to restitution of contracts that are terminated—e.g., ineffective *ex nunc*. In contrast, Estonian law recognises two regimes of restitution of contracts. On one hand, a special set of norms (LOA, §§188–194) is provided for unwinding the contracts after termination. On the other hand, restitution of contracts that are void or avoided is subject to rules of unjustified enrichment. As a legal consequences of the two regimes being somewhat different, it may be relevant under Estonian law whether a party has chosen to withdraw from or instead avoid the contract.<sup>10</sup>

The present article focuses on restitution of contracts in cases of avoidance. This means that it first considers under which conditions a contract may be avoided pursuant to Estonian law and the CESL. Second, the CESL's Articles 172–177 will be compared to the LOA's §§1028–1036, as the latter is the set of rules determining the legal consequences of avoidance.

### 2.2. Criteria for exercise of avoidance

At first sight, the grounds for avoidance of contracts under the CESL and Estonian law seem to coincide: both systems allow a party to a contract to avoid the contract in the case of a mistake (CESL, Art. 48; GPCCA, §92), fraud (CESL, Art. 49; GPCCA, §94), or threats (CESL, Art. 50; GPCCA, §96). A closer look, however, reveals some differences, of which the most important has to do with the issue of unfair exploitation.

Article 51 of the CESL gives a party the right of avoidance if three prerequisites are met: 1) that party was dependent on, or had a relationship of trust with, the other party; was in economic distress or had urgent needs; and/or was improvident, ignorant, or inexperienced; 2) the other party knew or could be expected to have known this; and, 3) in light of the circumstances and purpose of the contract, said party exploited the first party's situation by taking excessive benefit or unfair advantage. Under Estonian law, such a situation is considered to be in contradiction with good morals (GPCCA, §86 (2)) and thus null and void *ab initio*; in other words, no activity is required from the parties in order for the contract to be held to be void. Before May 2009, unfair exploitation was regulated in §97 of the GPCCA as grounds for avoidance. Because of social and political pressure and the social need, the definition of good morals in the GPCCA

<sup>7</sup> The CESL applies to cross-border sales contracts and contracts for the supply of digital content (see its Articles 4 and 5).

<sup>8</sup> Tsiviilseadustiku üldosa seadus. – RT I 2002, 35, 216; RT I, 6.12.2010, 1 (in Estonian). Available in English at <http://www.legaltext.ee/en/andmebaas/ava.asp?m=022> (most recently accessed on 8.4.2013).

<sup>9</sup> CESL, Recital 27. For a critical view, see R. Zimmermann. *Perspektiven des künftigen österreichischen und europäischen Zivilrechts*. – *Juristische Blätter* (134)/1, January 2012, p. 9.

<sup>10</sup> For a detailed analysis in this respect, see K. Saare, K. Sein, M.A. Simovart. *The buyer's free choice between termination and avoidance of a sales contract*. – *Juridica International* 2008 (XIV)/ 2, pp. 43–53.

was specified so as to include unfair exploitation. The objective of said amendment was to protect consumers from overindebtedness resulting from unreasonably high loan percentage rates (especially in SMS loan contracts).<sup>\*11</sup> This means that when the parties have opted for the CESL and the trader has unfairly exploited the consumer, the contract is not void and must be fulfilled unless the consumer gives notice to the other party within one year after becoming aware of the relevant circumstances or becoming capable of acting freely (CESL, Art. 52 (2) (b)). It may, therefore, be concluded that in this respect the CESL is less advantageous for the consumer than the Estonian regulation.

If the reason for avoidance is mistake, the regulation of the CESL resembles that in the GPCCA to a great extent, but there are some differences too. Firstly, the apparent difference in wording regarding the notion of mistake may be pointed out—‘mistake of fact or law’ in the CESL’s Article 48 (1) and ‘an erroneous assumption related to existing facts’ in the language of §92 (1) of the GPCCA. The latter might suggest that Estonian law offers less protection to the consumer, who in reality is often unaware of the relevant provisions of the law. However, recent Estonian legal literature refers to the notion of legally relevant mistake as including an erroneous assumption as to the legal consequences of the transaction.<sup>\*12</sup>

The second difference is more substantial. Pursuant to the GPCCA, it is only a **fundamental mistake** that justifies the avoidance (§92 (2)), and it is necessary that the other party have caused the mistake, made the same mistake, or known or had cause to have known of the mistake and that leaving the mistaken party in error was contrary to the principle of good faith (§92 (3)). Whereas the Estonian regulation clearly refers to the principle of reasonableness for decision on the fundamentality of the mistake<sup>\*13</sup>, the CESL does not apply this criterion.<sup>\*14</sup> It may be concluded that under the CESL, the decision on the relevance of a mistake must be taken on the basis of subjective criteria, with account taken of various factors related to the very person seeking avoidance. This approach of the CESL may in general be more advantageous for the consumer, but, on the other hand, this advantage is immediately ‘balanced’ by the requirement in Article 48 (1) (a) that the other party have known or could be expected to have known **this**. So what is it that the other party ought to know? Under the Estonian regulation, it is enough if the other party knew or should have known of the **mistake** (§92 (3) 2)). If a consumer has agreed to application of the CESL, the wording of Article 48 (1) (a) suggests that the other party (e.g., the trader) should have known of the **fundamentality** of the mistake for **that particular** consumer. It is hard to see how that can be proved at all, especially when the contract has been concluded over the Internet and the parties have never actually met.

Pursuant to Estonian law, the person relying on fraud as grounds for avoidance does not need to show the fundamentality of the mistake.<sup>\*15</sup> But, whilst the regulation of the CESL on fraud is comparable with the relevant provisions in Estonian law (GPCCA, §§94–95), it favours the defrauded party in that the time window within which notice of avoidance may be given (pursuant to Art. 52 (2) (b) is one year after said party becomes aware of the fraud, in comparison to the six months specified in §99 2) of the GPCCA). Accordingly, the defrauded consumer may expect better protection under the CESL. The same applies to contracts concluded under threat (CESL, Art. 50). On the other hand, it is difficult to see why the CESL refers only to threats and not to violence (as is the case in §96 of the GPCCA). It would only be justified if the scope of application of the CESL were to be limited only to those contracts concluded over the Internet or via other means of modern communication.

<sup>11</sup> For general discussion, see K. Saare, K. Sein, M.A. Simovart. Protection of consumer rights in SMS loan agreements. – *European Review of Private Law* 2010/18, pp. 129–142; P. Varul, I. Kull, V. Kõve, M. Käerdi. *Tsiviilseadustiku üldosa seadus. Kommenteeritud väljaanne* [‘General Part of the Civil Code Act, Commented Edition’]. Tallinn: Juura 2010, p. 275 (in Estonian).

<sup>12</sup> P. Varul et al. *Tsiviilseadustiku üldosa* [‘General Part of the Civil Code’]. Tallinn: Juura 2012, p. 155 (in Estonian).

<sup>13</sup> GPCCA, §92 (2): ‘A transaction is entered into under the influence of a relevant mistake if upon entry into the transaction the mistake was of such importance that a **reasonable person** similar to the person who entered into the transaction would not have entered into the transaction in the same situation or would have entered into the transaction under materially different conditions’ (emphasis added).

<sup>14</sup> Article 48 (1) (a) reads: ‘[T]he party, but for the mistake, would not have concluded the contract or would have done so only on fundamentally different contract terms.’ Article 5 (2) states that ‘[a]ny reference to what can be **expected** of or by a person, or in a particular situation, is a reference to what can reasonably be expected’ (emphasis added).

<sup>15</sup> For a detailed analysis, see K. Saare, K. Sein, M.A. Simovart. Differentiation of mistake and fraud as grounds for rescission of transaction. – *Juridica International* 2007 (XII), pp. 142–151.

## 3. Legal consequences of avoidance: Restitution

### 3.1. The principle of unjustified enrichment as a starting point

It has been maintained that, although Part VII of the CESL in its explicit wording does not refer to unjustified enrichment, the principle of preventing unjustified enrichment can be considered nonetheless to be the underpinning of the rules on restitution.<sup>\*16</sup> In most legal systems in continental Europe, unjustified enrichment law is a traditional part of the law of obligations<sup>\*17</sup>, regulating situations in which one person has received something (i.e., been enriched) to the disadvantage of another person without legal basis. On the other hand, the regulation of issues related to unjustified enrichment law is almost absent from European Union consumer directives<sup>\*18</sup>; therefore, it is difficult, if not impossible, to satisfy the demand that the rules of the CESL maintain or improve the level of protection that consumers enjoy under Union consumer law<sup>\*19</sup> in this respect.

In Estonia, as in other Continental legal systems, nullity of contract is a typical example of this 'absence of legal basis' prerequisite. Thus, unwinding of void or avoided contracts represents a typical area of application of unjustified enrichment law. In line with §84 (1) of the GPCCA, that which is received on the basis of a void transaction shall be returned pursuant to the provisions pertaining to unjustified enrichment unless the law provides otherwise. The LOA's §1028 (1) states that if a person (the recipient) receives anything from another person (the transferor) for the performance of an existing or future obligation, the transferor may reclaim it from the recipient if the obligation does not exist or is not created or if the obligation ceases to exist later. The objective of reversal is to put the parties in such a position as if the contract had never existed. This means that the parties must return or compensate for what has been received under contract, including the fruits and use of the object received.

### 3.2. Rules in particular

#### 3.2.1. The recipient's state of mind

It is widely accepted in Continental legal systems that the recipient's state of mind plays a role in decision over the extent of his liability in restitution. The recipient in good faith enjoys certain privileges, although not all of the systems' notions of good faith necessarily overlap.<sup>\*20</sup> Estonian enrichment law, which to a great extent is based on the theory and practice of German enrichment law<sup>\*21</sup>, also differentiates between recipients in good and in bad faith. Section 139 of the GPCCA states that if legal consequences are bound to good faith by law, good faith shall be presumed unless the law provides otherwise. A person acting in good faith does not or need not know certain circumstances that could influence the legal consequences of a transaction (and, on the contrary, bad faith means that the person knows or must know the facts).

<sup>16</sup> P. Sirena. The rules about restitution in the Proposal on a Common European Sales Law. – *European Review of Private Law* 2011 (19)/6, p. 983.

<sup>17</sup> R. Zimmermann. *Grundstrukturen des Europäischen Bereicherungsrechts*. Tübingen: Mohr Siebeck 2005, p. 21. For general discussion, see P. Schlechtriem. *Restitution und Bereicherungsausgleich in Europa*. Bd 1–2. Tübingen: J.C.B. Mohr (Siebeck) 2001; J. Beatson, E. Schrage (eds). *Cases, Materials and Texts on Unjustified Enrichment*. Oxford: Hart Publishing 2003.

<sup>18</sup> As an exception, Directive 97/7/EC lays down the principle that in the case of inertia selling to the consumer, a sender engaged in economic and professional activities has no claims against the consumer. See Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts. – OJ L 144, 4.6.1997, pp. 0019–0027.

<sup>19</sup> CESL, Recital 11.

<sup>20</sup> K. Zweigert, H. Kötz. *Einführung in die Rechtsvergleichung*. Tübingen: Mohr Siebeck 1996, p. 621.

<sup>21</sup> In fact, a recognisable model for systematisation of the provisions of Chapter 52 of the Law of Obligations Act is the draft proposed by D. König for reforming unjustified enrichment law in the German Civil Code. See D. König. *Empfehlenswert, das Bereicherungsrecht im Hinblick auf seine Weiterentwicklung in Rechtsprechung und Lehre durch den Gesetzgeber neu zu ordnen? – Bundesminister der Justiz (Hrsg.). Gutachten und Vorschläge zur Überarbeitung des Schuldrechts*. Bd II. Köln: Verlag Bundesanzeiger 1981, pp. 1515–1590. English translation of the König draft is available in R. Zimmermann. *Unjustified enrichment: The modern civilian approach*. – *Oxford Journal of Legal Studies* 1995 (15)/3, pp. 425–429.

The Supreme Court of Estonia has found that a person is considered to be in bad faith from the moment that he became or ought to have become aware of the circumstances that give reason for restitution.<sup>\*22</sup> If the enriched person acted in good faith, his liability for the reversal of the performance is restricted to the reversal of that which was transferred (or provision of compensation, in the case of destruction) and the gains. The main advantage to the recipient in good faith is the availability of defence of disenrichment (LOA, §1033). The recipient in bad faith may not rely on the fact that he is disenriched, and he is also obliged to transfer the gains derived from that which is received, pay interest to the extent provided by law for any money received, and compensate for any profits not gained from that which is received that the recipient could have gained by adhering to the rules of regular management (LOA, §1035).

Although the CESL's Part VII does not refer to good or bad faith *expressis verbis*, the rules on restitution refer to the parties' state of mind in certain articles, which mostly serve to the detriment of the party who knew or could be expected to have known of the grounds for avoidance or termination (see Articles 173 (5), 174 (1), 174 (2), and 175 (2)).

### 3.2.2. The general principle of restitution *in natura*

Article 172 (1) of the CESL specifies that where a contract is avoided or terminated by either party, each party is obliged to return what that party ('the recipient') has received from the other party. This means that the primary obligation is aimed at return of the received item or benefit in kind.<sup>\*23</sup> Similarly, §1028 (1) of the LOA obliges the debtor to return that which is received. The principle of restitution *in natura* corresponds to the traditions of most European national legal systems.<sup>\*24</sup>

Money and movables are the classic examples of transferable assets that can be returned. If the value of a thing received has changed (for example, the value of a painting has increased because the painter has become famous) and the debtor is still in possession of it, the change in value does not matter from the angle of restitution. The debtor may not rely on the fact that the object he received has no value for him and he is not enriched and thus is not liable for restitution, nor may the creditor choose to claim compensation for the object at its new, higher value.

Article 173 (1) of the CESL contains an amendment to the principle of reversal *in natura*, stating that where return is possible but would create unreasonable effort or expense, the recipient may choose to pay the monetary value, provided that this would not harm the other party's proprietary interests.<sup>\*25</sup> At first sight, this approach seems to favour the consumer, enabling him to choose between restitution and compensation. On the practical side, it must be noted that it remains in the hands of the courts, with the aid of the CESL's Article 5, to establish the ceiling to what is regarded as 'reasonable' efforts and expenses.<sup>\*26</sup> Following the principle that restitution should not put the recipient in a worse position<sup>\*27</sup>, the LOA in its §1033 (3) provides that the transferor shall bear the costs of restitution. The CESL does not address the issue of restitution costs; it even leaves open whether the trader has to collect the goods at the buyer's location or, instead, the buyer must send them back.<sup>\*28</sup> That said, Article 173 (1) receives a different meaning. Now it seems to suggest that the restitution costs must be borne by the recipient—why else does it use the expression 'unreasonable expense'? Taking into account that, especially in cases of cross-border transactions, returning goods to the trader can mean considerable efforts and costs, most consumers would probably abandon a plan to send the goods back to the seller. Accordingly, the non-existent regulation of costs of restitution in the CESL is to be evaluated as unfavourable to the consumer.

<sup>22</sup> CCSCd 16.6.2008, 3-2-1-54-08, para. 12; CCSCd 28.4.2009, 3-2-142-09, para. 18.

<sup>23</sup> R. Schulze (ed.). *Common European Sales Law (CESL): Commentary*. Baden-Baden: Nomos 2012, p. 680.

<sup>24</sup> C. von Bar, S. Swann. *Principles of European Law: Unjustified Enrichment*. Munich: Sellier 2010, pp. 452–455.

<sup>25</sup> This principle is also referred to in the Article VII.-5:101 (2) of the DCFR.

<sup>26</sup> On the notion of 'reasonableness' in general and in Estonian law: M.A. Simovart. The standard of reasonableness in the Estonian Law of Obligations. – I. Kull (ed.). *Developments of Estonian Contract and Company Law in the Context of the Harmonized EU Law*. Tartu: Tartu University Press 2007, pp. 65–86.

<sup>27</sup> P. Varul et al. *Võlaõiguseadus III. Kommenteeritud väljaanne* ['Law of Obligations III. Commented Edition']. Tallinn: Juura 2009, p. 598 (in Estonian).

<sup>28</sup> See also C. Wendehorst. *Restitution in the Proposal for a Common European Sales Law*. European Parliament 2012. Available at <http://www.europarl.europa.eu/committees/fr/studiesdownload.html?languageDocument=EN&file=75251> (most recently accessed on 8.4.2013).

The CESL's Article 173 (1) stipulates that the recipient of digital content—irrespective of whether it was supplied via a tangible medium—must pay its monetary value. This is another deviation from the principle of restitution *in natura*. Estonian law does not contain a comparable provision. If the consumer has downloaded a song, purchased an e-book via the Internet, or listened to streaming music, restitution in kind is in principle possible in some cases but is not consistent with the unjustified enrichment approach, because the seller may get back the electronic file while the consumer has already received the benefit of listening, playing, reading, etc.<sup>\*29</sup> Traders will probably welcome this approach, and it must be said that this provision constitutes reasonable modification of rules of restitution. However, if the digital content is supplied through a tangible medium, such an all-or-nothing rule might not be justified, particularly when the digital content has not been used at all. It is quite common practice that consumers may return computer and video games if the package has not been opened. Therefore, it is difficult to see why a defrauded, exploited, or threatened consumer is refused the right to make a return even if return is possible and he has not used the goods; this may lead to a forced exchange. As stated above, Estonian law does not compel the buyer of digital content to compensate for its value instead of returning it in an unopened package; thus it may be concluded that the buyer of digital content is in a better position under Estonian law.

### 3.2.3. Substitutes and value

It is often the case that the performance received under contract cannot be returned, either because it has been destroyed, sold, or similar or on account of its nature (in the case of services, for example). In this situation, the question of substitutes and value arises.

In its §1032 (1), the LOA stipulates that in the event of the destruction or consumption of, damage to, or seizure of the transferred object, the transfer of that which is acquired in compensation for said object may be demanded. This means that, for example, an insurance indemnity or compensation for damage received in the case of destruction or damage of the object of the enrichment must be reversed to the transferor. The CESL's Article 173 (5) similarly provides for the principle of returning the substitute but combines it with the choice of compensation for the value of the substitute, whereas the right to choose may be exercised either by the recipient or by the giver, depending on the recipient's state of mind. It follows that the understanding of what constitutes a 'substitute' differs between Estonian law and the CESL. Under the LOA, the substitute is a monetary claim for damages or insurance indemnity. When the recipient has sold the object or bartered it for another object, money or another object received is not considered a substitute and may not be claimed by the creditor. He may instead demand that the recipient compensate for the value of the goods.<sup>\*30</sup> In contrast, Article 173 (5) of the CESL has been interpreted as extending the claim to both objects and the price received for goods or digital content.<sup>\*31</sup> This approach is nothing new, as it is present in unjustified enrichment laws of many European jurisdictions.<sup>\*32</sup> The CESL goes even further by recognising the monetary value of the substitute as the content of a claim. The effect of Article 173 (5) is that if a buyer who is in good faith has bartered the received goods against some other, less expensive goods as a substitute, he may choose between giving up the substitute and compensating for its value. This means that the buyer's liability in the situations described may be lower than the value of the original goods he received from the seller. That solution puts the buyer in a better position than he would hold under Estonian law.

When a buyer in bad faith has received a substitute for the goods, it follows from the CESL's Article 173 (5) that now the seller has the right to choose between a claim for giving up of the substitute and one for the value thereof. This provision has been interpreted as a rule on disgorgement of profits.<sup>\*33</sup> However, Article 173 (5) creates some advantages for the seller only if the buyer has made a good bargain—for example, if he has earned profits. If the buyer has bartered original goods for cheaper goods, the seller will be worse

<sup>29</sup> For a recent detailed analysis of regulation of issues related to digital content, see M. Loos *et al.* Digital content contracts for consumers: Analysis of the applicable legal framework and suggestions for the contours of a model system of consumer protection in relation to digital content contracts. Available at [http://ec.europa.eu/justice/consumer-marketing/files/legal\\_report\\_final\\_30\\_august\\_2011.pdf](http://ec.europa.eu/justice/consumer-marketing/files/legal_report_final_30_august_2011.pdf) (most recently accessed on 8.4.2013).

<sup>30</sup> T. Tampuu. *Lepinguväliste võlasuhete õigus* ['Law of Non-contractual Obligations']. Tallinn: Juura 2012, p. 119 (in Estonian).

<sup>31</sup> P. Sirena (see Note 16), p. 993.

<sup>32</sup> P. Schlechtriem (see Note 17), pp. 355 *ff.* This principle is also adopted in the DCFR's Article VII.-5:101 (4).

<sup>33</sup> C. Wendehorst (see Note 28), p. 19.

off regardless of his right to choose between a substitute and the value of the substitute. Estonian law does not contain a rule on disgorgement of profits in relation to restitution of contracts<sup>\*34</sup>, which means that the buyer's liability is measured by the value of the original goods even if he is in bad faith.<sup>\*35</sup> Therefore, it may be concluded that a buyer in bad faith may be in a better position under Estonian law if he has made profits by disposing of the original goods; if, on the other hand, no profits are made, the buyer's liability is stricter under Estonian law than under the CESL.

Regarding compensation for the value of the goods, the LOA's §1032 (2) states that if it is impossible to deliver that which is received, whether on account of the nature thereof or for any other reason, the recipient shall compensate for the usual value obtaining when the right to reclaim was created. This corresponds to the idea that unjustified enrichment regulation is applied to contracts that are ineffective *ex tunc*. This means that when the contract was void *ab initio*, the value is to be calculated as of the time at which the performance was made.<sup>\*36</sup> However, the legal literature shows differing views on the starting point of the value calculation in cases of avoidance: some authors find that it is the moment when the notice of avoidance enters into force (e.g., when it reaches the other party<sup>\*37</sup>), others say that it is the time of performance.<sup>\*38</sup> Estonian law provides for objective assessment of value: the LOA's §1032 refers to the usual value, and according to §65 of the GPCCA, the usual value of an object is deemed to be the value of that object unless the law or a transaction determines otherwise. The usual value of an object is taken to be its average local selling price (market price).

Pursuant to Article 173 (2) of the CESL, the monetary value of goods is the value that they would have had on the date when payment of the monetary value would have been made if they had been kept by the recipient without destruction or damage until that date. It remains unclear what is meant by 'the date when payment of the monetary value would be made'—does it refer to the date of avoidance or to some later date? In any event, starting the calculation of value later than the avoidance of contract would contradict the idea that the parties should be put in such a position as if the contract had not existed.

It may be concluded that, with respect to the question of how to calculate the value of the goods in the case of avoidance of a contract, neither Estonian law nor the CESL provides a clear answer.

When deciding on the extent of enrichment claims in the case of nullity of a mutual contract, the Estonian Supreme Court has stated that the reciprocal claims of the parties may be considered set off (balanced) and the court shall require the party in whose disadvantage the balance (*saldo*) remains to pay the other party the difference of the claims.<sup>\*39</sup> It also follows from the provisions of the CESL that, as an outcome of reversal of performances, the parties may end up having reciprocal monetary claims. Therefore, it seems rather surprising that the CESL does not include regulation of such a practical matter as set-off.<sup>\*40</sup>

### 3.2.4. Fruits and use

Article 172 (2) of the CESL states that the obligation to return what was received includes any natural and legal fruits derived from what was received. This is in line with the principles of Estonian unjustified enrichment law, which provides that the transferor may demand that the recipient return that which is received and any gains derived therefrom (LOA, §1032 (1)). 'Gains' are to be understood as the fruits of the object and the advantages receivable from the use of the object (i.e., advantages of use) (GPCCA, §62 (1)).

The CESL does not define 'natural or legal fruits'. It is explained in the legal literature that natural fruits are products derived naturally from that received and legal fruits are benefits that are derived from that received through the operation of the law.<sup>\*41</sup> In Estonian law, 'fruits' are defined as 'fruits of a thing' or 'fruits received from a right' (GPCCA, §62 (2) and (3)). This reveals that the understanding of the notion of

<sup>34</sup> But disgorgement of profits is explicitly provided for in cases wherein the enrichment is a result of infringement of another's rights and the infringer is in bad faith (LOA, §1039).

<sup>35</sup> T. Tampuu (see Note 30), p. 133.

<sup>36</sup> CCSCd 2.5.2007, 3-2-1-33-07, para. 10.

<sup>37</sup> P. Varul *et al.* (see Note 27), p. 595.

<sup>38</sup> T. Tampuu (see Note 30), pp. 121–122.

<sup>39</sup> CCSCd 20.12.2005, 3-2-1-136-05, para. 27.

<sup>40</sup> The CESL's Recital 27 lists set-off among the issues to be resolved under national law; see also R. Zimmermann (see Note 9), p. 9.

<sup>41</sup> R. Schulze (see Note 23), p. 688.

‘fruits’ differs somewhat between the CESL and Estonian law: while it is suggested that the type of fruit in the CESL is distinguished on the basis of the object (a thing or a right), in Estonian law the classification of fruits is based on the manner of production of the fruit. Therefore, for example, renting out a flat involves ‘legal fruit’ under the CESL but ‘natural fruit’ under Estonian law.

Article 174 (1) of the CESL contains rules on payment for use. One’s first impression is that only the recipient in bad faith (e.g., one who has caused or was aware of the grounds for avoidance or termination)<sup>\*42</sup> is liable for compensation of use. This deviates from Estonian law (LOA, §1032 (1)), which orders the recipient to pay for the use irrespective of his state of mind. This explains why the Supreme Court of Estonia has found that ‘in using another person’s property, presumably one always receives advantages of use, which, among other things, means saving on one’s costs’<sup>\*43</sup>. It is worth mentioning that this view was expressed in a case related to a house that was (allegedly) so dilapidated that it was not fit for habitation. The Supreme Court tried to mitigate the above-mentioned rule by stressing that the other party must first establish the value of the use.<sup>\*44</sup> Also, in another dispute, the Supreme Court has stated that, pursuant to the principle of good faith, the transferor may demand reversal of gain only in the extent that amounts to the gain that he could have received upon adherence to the requirements for regular management if the unjustified enrichment had not occurred.<sup>\*45</sup>

Having said that, one might conclude that the recipient in good faith is in a better position under CESL rules, as he is not liable for compensation for use of the goods. Yet it appears that the CESL’s Article 174 (1) (c) provides for compensation if it would be inequitable to allow the recipient the free use of the goods for that time. The criteria that could be taken into account are the nature of the goods, the nature and amount of the use, and the availability of remedies other than termination. Therefore, one may say that the answer to the question of compensation for use under the CESL might not turn out to be that different from the Estonian solution.

If we now turn to the seller who has received the money in exchange for goods, the issue of the extent of his liability arises. First and foremost, the question that must be answered is whether the seller must pay interest. Under Estonian law, a recipient acting in bad faith must pay interest to the extent provided by law for any money received (LOA, §1035 (3)). A party threatening, exploiting, or defrauding the other party is definitely acting in bad faith so is expected to pay interest. The outcome would be the same under the CESL’s Article 174 (2) (b), which states that the recipient must pay interest if he gave cause for avoidance, on grounds of fraud, threats, and/or unfair exploitation. The wording of the LOA’s §1035 (3) has led to the conclusion in Estonian legal literature that the recipient in good faith need not pay interest, because the use of money does not have any value in itself.<sup>\*46</sup> This statement is questionable, especially when the recipient of the money is a business. To say that the trader must pay interest only if he was in bad faith would ignore the economic reality: it would be rather exceptional if the trader (whatever his state of mind) were **not** to use the money. When the buyer of a dilapidated house is obliged to pay for use because it is **presumed** that he has saved on costs, why is it not presumed that, by receiving the money from the buyer, the seller has saved on costs that he would normally incur if he were to borrow this money? This is a question that in the author’s view has not yet been answered in Estonian law. In comparison, the CESL’s Article 174 (2) (a) stipulates that a party must pay interest when the other party is obliged to pay for use. This means that the trader may be ordered to pay interest even when he is in good faith. This solution is not as unjust as it might appear, because, irrespective of the reasons for avoidance, the trader has had the opportunity to use the money.

Alongside fraud, threats, and unfair exploitation caused by the trader, other scenarios are possible when the trader is in bad faith. Accordingly, it is unclear in the author’s view why the buyer’s obligation to pay for use depends on his awareness of the grounds for avoidance or termination (CESL, Art. 174 (1) (c)) yet the seller’s liability for interest is tied not to such **awareness** but to the fact of him having defrauded, threatened, or exploited the other party (CESL, Art. 174 (2) (b)). Therefore, Pietro Sirena quite rightly observes that under Article 174 the undesirable result is possible that, because the consumer does not have

<sup>42</sup> In fact, it is not clear what is meant under ‘caused the grounds’ – e.g., whether this covers also those situations in which the consumer has made a mistake.

<sup>43</sup> CCSCd 20.12.2005, 3-2-1-136-05, para. 26.

<sup>44</sup> *Ibid.*

<sup>45</sup> CCSCd 15.6.2005, 3-2-1-67-05, para. 11.

<sup>46</sup> P. Varul *et al.* (see Note 27), p. 594.

to pay for the use, even the trader in bad faith may be exempted from the obligation to pay interest.<sup>\*47</sup> It may be concluded in view of this that, in respect of fruits and use, neither the Estonian law nor the CESL can be praised for presenting a clear and understandable solution, especially where the obligation of a trader to pay interest is concerned. Therefore, it is not possible to say which rules would be generally more advantageous for the consumer. Instead, the answer depends on the details of each particular case.

### 3.2.5. Disenrichment and expenditure

The defence of disenrichment has been introduced in Estonian legislation by the LOA (which came into force on 1 July 2002), except with respect to matters related to performances, for which it is regulated in §1033 of the LOA. The underlying idea of disenrichment is that a recipient in good faith is not required to return that which is received or compensate for the value thereof to the extent to which the recipient is not enriched thereby in consequence of the destruction or consumption thereof, damage thereto, or seizure thereof or for any other reasons.<sup>\*48</sup> 'Not enriched' means, for example, the defendant not having saved any costs because he himself would not have incurred the respective expenses.<sup>\*49</sup> If the enriched person disposed of the enrichment gratuitously and thus saved costs (for example, avoided costs that he otherwise would have incurred in buying a birthday present), he is still regarded as having been enriched. Also, the recipient's transfer of the money to a third party as a gift should not be considered to be disenrichment on the basis of the principle of good faith.<sup>\*50</sup> If a mutual contract (such as a sales contract) is void, the recipient may rely on the disenrichment only if the contract is void on account of the incapacity of the recipient or because of threats or violence on the part of the transferor (§1034 (1) of the LOA).<sup>\*51</sup>

The CESL does not appear to include the defence of disenrichment. Instead, Article 176 includes a general 'equity clause', stipulating that any obligation to return or to pay under that article may be modified to the extent that its performance would be grossly inequitable, in into consideration of, in particular, whether the party did not cause, or lacked knowledge of, the grounds for avoidance or termination. This solution is not to be applauded, because it is hard to imagine how this kind of regulation could facilitate cross-border trade and enable traders to avoid additional costs; it might instead discourage traders from applying the CESL. In Estonian law, it is possible to fill the gaps and even overrule the statutory provisions with the aid of the principle of good faith (LOA, §6). But, as the Estonian regulation on unjustified enrichment demonstrates, before one resorts to general principles it is more practicable to lay down the rules as to liability of the recipient in good faith and in bad faith. The author finds that the presence of rules on disenrichment in the LOA provides for greater clarity in comparison to the CESL's Article 176, and this clarity is advantageous for both the seller and the buyer.

Besides destruction or consumption of the goods, the recipient's disenrichment may occur in the form of expenditures he has made. This conclusion may be drawn from §1033 (2) of the LOA, which states that if the recipient indeed believed that the ownership of that which was received is permanent, he must return or compensate for the value of that received only if he is compensated for the expenditure.

This provision does not require that the expenditure be **for goods received**, or that the other party be enriched as a result of that expenditure.<sup>\*52</sup> Therefore, it is suggested in the literature that §1033 (2) of the LOA does not give rise to an active claim and only allows the recipient to refuse the return of what was received; instead, legal scholars are willing to grant the recipient an active claim for expenditures on grounds of the LOA's §1042.<sup>\*53</sup> The first sentence of §1042 (1) stipulates that 'a person who incurs expenditures with regard to an object of another person without a legal basis therefor may demand compensation

<sup>47</sup> P. Sirena (see Note 16), p. 998.

<sup>48</sup> German law is similar in this respect (with *Wegfall der Bereicherung*). See P. Schlechtriem (see Note 17), pp. 359 ff.

<sup>49</sup> ALCSCd 17.6.2004, 3-3-1-17-04, para. 22.

<sup>50</sup> T. Tampuu (see Note 30), p. 125.

<sup>51</sup> Whether this principle is to be extended to cases involving fraud or exploitation is subject to debate; the general view seems to be that it should not. See T. Tampuu (see Note 30), p. 124; P. Varul *et al.* (see Note 27), p. 600.

<sup>52</sup> This may be explained by reference to the requirement of the recipient's belief in the irrevocability of his ownership. One can conclude from this that said provision serves as a means of protection of the interests of a recipient in good faith; it is designed for providing grounds for evaluating the recipient's disenrichment, not the other party's enrichment (which may occur if the other party gets back an object that is improved in consequence of the recipient's expenditures).

<sup>53</sup> P. Varul *et al.* (see Note 27), p. 598; T. Tampuu (see Note 30), p. 125.

for the expenditures to the extent to which the person on whose object the expenditures are incurred has been enriched thereby, in consideration of, inter alia, the fact of whether said expenditures are useful to the person and the intent of the person with regard to the object'. Pursuant to §1042 (2) of the LOA, the claimant does not gain the right to state a claim if the other party requires the improvements to be removed; if, because of circumstances arising from him, the claimant failed to notify the other party in time of the intent to make expenditures; if the other party has contested the expenditures; or if making such expenditures was prohibited by law or by contract. In comparison, Article 175 of the CESL provides that 1) in the case of a party who did not know and could not be expected to have known of the grounds for avoidance or termination, the recipient is entitled to compensation to the extent that the expenditure benefited the other party and 2) a recipient who knew or could be expected to have known of the grounds for avoidance or termination is entitled to compensation only for expenditure that was necessary to protect the goods or digital content involved from being lost or diminishing in value, provided that the recipient had no opportunity to ask the other party for advice.

Thus it is that, in general, under both the LOA's §1042 and the CESL's Article 175 a person who had the opportunity to ask the other person's consent but did not do so is barred from making a claim for compensation at all, whereas a person in good faith may claim compensation only if the expenditure is useful (beneficial) for the other party. Commentators find that, in deciding whether the expenditures are beneficial (CESL, Art. 175 (1)), one must take into account the personal situation of the person in question: the mere fact that the goods are improved does not necessarily constitute a benefit.<sup>54</sup> This is, in fact, also the result that is sought with the LOA's §1042 (1). A certain difference can be observed between the CESL and LOA in situations wherein the recipient knew or could be expected to have known of the grounds for avoidance but could not ask the other party's consent for the expenditures: in such cases, the CESL provides compensation for necessary expenditure, whereas compensation under the LOA depends on the utility of the expenditures for the other party. The CESL's distinguishing between necessary and beneficial expenditures speaks for the conclusion that necessary expenditures shall be subject to compensation without regard for their actual result; for example, attempting to protect the goods will suffice and compensation will be granted even if the goods were destroyed. This outcome is not justified because, as is stated above, the compensation given to the recipient in good faith is contingent on the benefit for the other party.<sup>55</sup> Therefore, in comparison to the LOA, the CESL as it stands today, appears to be friendlier toward a recipient in bad faith.

## 4. Conclusions

The aim of this article has been to compare the rules of the CESL and Estonian law regarding the avoidance of contracts and restitution of performances made under such contracts. It was asked which of the two regimes offers a higher level of protection for the consumer. The results may be summarised thus: a consumer who has opted for the CESL is in a more advantageous position if it turns out that he has been defrauded. In that case, the period for giving notice of avoidance is longer than it would be under Estonian law. On the other hand, Estonian law offers somewhat better protection to the consumer who has concluded a contract under conditions of unfair exploitation: such a contract is considered to be null and void, whereas the CESL in such a situation grants the right to avoidance.

When it comes to restitution of performances, the CESL seems to provide more favourable treatment to a buyer who has made expenditures on goods while being aware of the grounds for avoidance. If the buyer has disposed of the goods through some form of transfer to a third party against money or some other object as a substitute, the buyer's position is better if the CESL is applied, because it allows the buyer to choose between giving up the substitute and compensating for its value (which may be lower than the value of the original goods). On the other hand, the CESL deprives the recipient (even a defrauded, exploited, or threatened consumer) of the right to return the digital content even if this is stored on a tangible medium and in its sealed package. This solution differs from that seen with the LOA and is clearly not preferable from the consumer's point of view. The CESL does not include a defence of disenrichment, which is less advantageous for the consumer than are the provisions of the LOA.

<sup>54</sup> R. Schulze (see Note 23), p. 713.

<sup>55</sup> C. Wendehorst (see Note 28), p. 22.

That said, it must be concluded that, with regard to restitution of avoided contracts, it is not possible to say which of the two regimes in general is more advantageous for the Estonian consumer as a buyer: as was demonstrated above, the level of protection of the buyer (as a recipient) under the CESL and LOA may vary with the situation. However, there are also some important issues that the CESL does not address at all (in particular, who should bear the costs of restitution, or the rules for set-off) or that the CESL does not regulate with sufficient clarity (such as the recipient's obligation to pay for use of goods). Therefore, it can be said that parties opting for the CESL as it stands today must in cases of restitution of avoided contracts be ready to face greater unpredictability than they would experience if the rules of the LOA were to be applied.