Migration Letters
Volume: 20, No: S12(2023), pp. 651-657
ISSN: 1741-8984 (Print) ISSN: 1741-8992 (Online)
www.migrationletters.com

Analyzing the Influence of the Good Faith Principle on Commercial Contracts within the Saudi Legal Framework

Saleh Mohammed Al-Hammami[1], Ghaleb Mubarak Al-Hammami[2], Salem Talib Al-Hammami[3]

Abstract

Undoubtedly, the principle of good faith is crucial in both Islamic Sharia and contemporary laws, as well. It paves the way for stable contracts and transactions. Adhering the principle of good faith is obligatory and signifies a sincere pursuit of the contract's objectives. Despite not being explicitly stated, the Saudi legislator has shown interest in this principle, with its provisions scattered throughout various regulations, including the Company Law. This research aims to demonstrate the impact of applying this principle in the Saudi company law. This research adopted the inductive and analytical approaches to analyze the texts in which good faith was mentioned. The findings confirm its significance and elucidate some practical aspects of this impact, such as the company's pillars, its legal personality, the theory of the actual company, and more. The recommendation includes proposing explicit legal provisions that highlight the impact of this principle in related regulations, as well as establishing a clause for it in the commercial transactions section and other relevant regulations, each in its appropriate place.

Keywords: *Company, contract, corporate system, good faith.*

Introduction

Good faith is indeed a crucial principle for material transactions among people. As the Kingdom of Saudi Arabia operates according to the provisions of Islamic Sharia, it has rightfully given good faith its legal due. Therefore, the application of good faith is evident in various Saudi regulations, including those pertaining to companies and commercial transactions. This research seeks to demonstrate the impact of good faith principle on commercial company contracts.

Research significance

The importance of this research lies in revealing the extent of Saudi regulatory interest in the principle of good faith and its enforcement, identifying any deficiencies and proposing corrective measures. The study also demonstrates the impact of the principle of good faith on commercial company contracts and the potential extent of its influence. I did not find - from what I looked at - a previous study that focused on the effect of good faith on corporate contracts in the Saudi system.

[1] Assistant Professor of Civil System, Najran University, smalhamame@nu.edu.sa, https://orcid.org/0009-0005-3751-347X
[2] Assistant Professor of Administrative System, Najran University, gmalhammami@nu.edu.sa, https://orcid.org/0009-0001-8981-4603
[3] Instructor at Najran University, stalhammami@nu.edu.sa, https://orcid.org/0009-0001-8981-4603

Research objectives

The research objectives are as follows:

1. Uncovering the extent to which the principle of good faith is applied in commercial company contracts and its resulting impact.

2. Illustrating the contribution of the principle of good faith to achieving justice, safeguarding rights, and combating fraud and deception.

Research questions

The research problem lies in the factors that the effects of the principle of good faith have not been explicitly demonstrated in various legal texts. It has only been mentioned in a few provisions and requires further investigation beyond the text to adequately showcase its effects.

Methodology

This research was based on the inductive and analytical method. I collected a wide range of research sources and references. I started by defining terms in both language and within the legal system. I conveyed the information in my own style, focusing on meaning rather than adhering strictly to the original wording unless direct quotation was necessary.

The research comprised two main sections and a conclusion. Section 1 focused on defining terms related to the good faith, with three sub-sections covering the definition of "good faith" in the Saudi legal system, contracts in the Saudi legal system, and companies in the Saudi legal system. Section 2 delved into the impact of good faith in the Saudi legal system, with four sub-sections exploring the pillars of commercial companies and the impact of good faith, the beginning and end of legal personality and the impact of good faith, termination of commercial companies and the impact of good faith, and dissolution of commercial companies and the impact of good faith. The conclusion highlighted key findings and recommendations, and the research included a list of references.

Good faith

Good faith in the Saudi legal system

The Saudi legal system, along with other legal frameworks, does not offer an independent definition of "good faith." Despite the absence of a direct definition, it is regarded as an essential principle in all legal relationships and is presumed to be implicit in all circumstances. Legal scholars have presented various definitions for "good faith," each facing its share of criticism. One notable definition by Dr. Shirzad Sulaiman characterizes good faith as a "commitment to directing the will to achieve the direct purpose of concluding the contract in a manner that aligns with the legitimate justifiable interests of the other party." Scholars have shown considerable differences in defining "good faith," with each definition receiving criticism. To be concise, I have highlighted the most notable definition by Dr. Shirzad Sulaiman, who regards good faith to one's intentions which are aimed at fulfilling the contract's direct purpose in a way that respects the legitimate and justifiable interests of the other party.

Contracts in the Saudi legal system

The Saudi regulations address the aspect of contracts by specifying their provisions and various principles, as evident in the Commercial Companies Law. However, there is no specific definition of a contract as a source of obligations. Nevertheless, we can refer to legal scholars' opinions to clarify the definition of a contract. There are various definitions, but I will mention the prevailing one, which is: "The agreement of two or more wills, leading to a legal consequence, whether it be the establishment, transfer, modification, or termination of an obligation.".

Companies in the Saudi legal system

A company is an institution in which people carry out joint work; In order to make a profit. The term "company" procedurally refers to a legal entity that is established according to the provisions of the Saudi Companies Law (SCL) based on an incorporation contract or articles of association. It involves two or more individuals committing to contribute either money, work, or both, with the aim of making a profit and sharing the resulting profits or losses.

Good faith in the Saudi legal system

The Saudi legal system, like other legal systems, places significant emphasis on the principle of good faith, stemming from the importance of Islamic law. This is evident in the effects that impact the validity and invalidity of commercial contracts, including company contracts. Briefly, some of the effects are as follows:

The effect of the company pillars in the Saudi system on good faith

Firstly, legal scholars have categorized the essential elements of a company into general objective elements and specific objective elements, with additional formal conditions. Most of these objectives show the influence of applying good faith.

A) The general principles of a company include consent, subject matter, reasonableness. The application of good faith is evident in most of these elements.

Consent: in the element of consent, the principle of good faith is clearly influential. Complete consent cannot be achieved unless it stems from a party with good intentions. If consent is affected by defects such as mistake , fraud , coercion , or exploitation, the contract is not valid and is subject to being voided. These defects typically arise from a party with ill intentions, impacting the validity of the contract due to the absence of good faith.

Subject matter: it is subject to several conditions, including being within the scope of transactions, specific, limited, feasible, and achievable.

Reasonableness: The principle of good faith certainly has an impact on the capacity requirement. A person's intent cannot be described as good or bad unless they have full capacity, understand their intentions, and comprehend their best interests and potential harm. Furthermore, the detailed provisions regarding capacity, whether it is total incapacity (such as insanity, idiocy, or undiscerning minor) or partial incapacity (such as a discerning minor), effectively prevent individuals with ill intentions from engaging with such persons. This is because those with total incapacity do not comprehend what is suitable for them, making it easy to exploit or deceive them during transactions. Similarly, those with partial capacity may or may not understand what is suitable for them, and the required level of capacity to become a partner in a company varies based on the type of company and the legal status of the partner.

B) Specific principles of partnership include multiple partners, contribution of shares, intention to participate, and sharing of profits and losses.

Multiple partners are inherent in the concept of partnership, signifying collaboration and the union of interests among individuals. This element is related to the principle of good faith, as it embodies the spirit of the contract between the parties. A person who willingly engages in partnership and commits to fulfilling all the necessary elements and conditions of a valid contract is considered to have good intentions, unlike someone who violates certain provisions.

Contribution of shares is impacted by of the principle of good faith; It is evident in motivating the partner to fulfill their financial or in-kind contribution or to perform the required work within the specified time and quantity. This demonstrates good intentions, whereas a lack of proactive action without any valid impediments to performance indicates bad intentions, leading to liability for any harm caused to the partnership due to delay or procrastination.

Intention to participate: though it is not mentioned in the Saudi partnership, it is considered the fundamental pillar of a company, and its absence would result in the non-existence of the company. Therefore, it is essential for the formation of a partnership and signifies the confirmation of the principle of good faith in company contracts. Each partner must act within the agreed-upon terms and conditions of the contract, without intentionally violating them, demonstrating good intentions.

Sharing of profits and losses: the principle of good faith play substantial role in clarifying the regulations surrounding it, such as determining the ratio of profits and losses. The requirement is that each partner should have a share of profits or losses without specifying the amount, provided that the share is not insignificant to the extent that it deprives the partner of their rightful share of profits or shields them from losses. These regulations are only applied by a partner described as having good intentions. If the contract includes conditions that give one party an unfair advantage, it signifies bad intentions on the part of the partners or some of them, not good intentions.

The impact of good faith on commercial partnership

The legal personality in law refers to the capacity to acquire rights and assume obligations. A legal entity, such as a company, generally acquires legal personality upon its formation, as expressly provided for in company law.

Therefore, the legal personality of a commercial company begins with its registration in the commercial register and is not solely dependent on fulfilling the procedural requirements specified by the law. Even if the company is not registered, a third party acting in good faith can still benefit from the legal personality of the company. The company acquires its legal personality as a general rule upon its formation, and this legal personality is not contingent upon registration. Therefore, the impact of good faith is manifested in allowing third parties to rely on the legal personality of the company for their benefit, irrespective of its registration status. This signifies the importance of good faith in upholding the legal rights and obligations of the company.

The impact of good faith on the partnership's termination

The expiration of a partnership refers to the dissolution of the legal relationship between the partners and the settlement of the company's relations with third parties. This expiration may be due to general, personal, or financial reasons, or due to reasons specific to companies with legal personality, or for special reasons. I will focus on the general reasons provided for in the regulations. As for the general reasons, Article 243 of the SCL specifies the general reasons for the expiration of partnership - regardless of their type - as follows: "Taking into account the specific reasons for the expiration of each type of company, a company expires for one of the following reasons:

1. The end of the partnerships' specified period - if it is for a specified period - unless extended in accordance with the provisions of the law.

2. An agreement by the partners or shareholders to dissolve the partnership.

3. Issuance of a final court judgment to dissolve it or declare it void.

When examining the first reason, we notice the impact of the principle of good faith. If the partners agree to extend the company explicitly or implicitly, it is permissible for the creditors of one of the partners to object to this extension. This objection results in suspending the effect of the extension on their rights. If the partner's creditors cannot execute against their debtor's share during the existence of the company, they should at least be allowed to object to the extension of the company so that they can execute against their debtor's share in it. Although there is no specific provision in the SCL that grants such a right to the creditors of the partner in this case, it is in the interest of justice to adopt such a rule.. This judgment and exception preserve the right of the creditor - who is not acting in good faith - from being lost in favor of the debtor.

As for the judicial dissolution, it can only be sought after one of the partners files a request for dissolution. Therefore, it is not permissible to agree to deprive the partners, or any of them, of the right to resort to the court to request dissolution. This judgment is considered a source of reassurance for those with ill intentions who want to participate in a contract of partnership.

The actual partnership and the effect of good faith on it

The actual partnership is defined as the legal personality of the company during the period between its establishment and the judgment of its nullity. The application of the theory of the actual company occurs during the liquidation phase. Liquidation procedures must be carried out in accordance with the provisions stated in the company's contract. If there are no specific liquidation provisions in the company's contract, then the provisions stated in the Companies Law must be followed.

The theory of the actual company is founded on the principle of good faith, as nullity typically renders a contract as if it never existed. When a company ceases to exist or is declared null and void, it can create significant harm for those involved in the company contract, such as partners and shareholders, especially if they have acted in good faith. It becomes challenging for them to assert their rights from a company that has been declared null and void and no longer exists. To address this, the judiciary has established the theory of the actual company, which limits the effects of nullity to the future only, without impacting the past. This is aimed at safeguarding the reliance of the other party, ensuring legal stability, and providing an opportunity for those who have acted in good faith to claim their rights.

Conclusion

The study found that the principle of good faith in dealings between people - in general - and in the conclusion of contracts - in particular - is of great importance. Through it, transactions are carried out with peace of mind, and the need for judicial intervention in resolving disputes is reduced. Furthermore, the study concluded that the impact of the principle of good faith is evident in the provisions of commercial company contracts, in their general and specific elements, and in their formal conditions. It also affects provisions related to the legal personality of the company from its inception to its end, including issues related to the theory of the actual company and similar matters. This principle directly or indirectly intervenes in all these issues, and its impact is clearly evident in their related applications.

Recommendations

Based on the results we reached in this modest research, we have some recommendations that were arrived at by my limited effort, while accepting them for criticism, and they are as follows:

1. Given that the principle of good faith is of utmost importance - as stated in this research -,we suggest that the Saudi regulator refer to it separately in an article, or several articles, whether in the Commercial Companies Law, or in other relevant regulations.

2. It has been mentioned that the Saudi system did not refer to a good faith control, and therefore we propose that the Saudi regulator establish a control for this principle, and the control that we see is what we referred to in the first section, that the principle of good faith in commercial law is a statement of: “an obligation by directing the will to achieve the direct purpose of concluding the contract, so that it is consistent with the legitimate justified interests of the opposing party.

Acknowledgement

The authors are thankful to the Deanship of Scientific Research at Najran University for funding this work, under the Research Groups Funding program grant code NU\RG\SEHRC\12\7.

References

1. abin fars, 'abu alhusayn 'ahmadu. muejam maqayis allugha ('iisdar bidun tabeatin). tahqiq eabdalsalam bin muhamad harun. bidun tabeatin. 6 mu. dimashqa: dar alfikr liltibaeat walnashr waltawziei, 1399.
2. abin manzurin, jamal aldiyn bin makram. lisan alearab ('iisdar bidun tabeatin). bidun tabeati. alsueudiati: dar ealam alkutub, 1424.
3. aljabara, muhamad hasan. alqanun altijariu alsueudiu. ta: alraabieati. jidat: maktabat alshaqri, 1996.
4. alkhwli, 'aktham 'amin. durus fi alqanun altijarii alsaeudii. bidun tabeati. alriyad: matbueat maehad al'iidarat aleamati, 1393.
5. alsinhuri, eabdalrazaqi. alwajiz fi alnazariaat aleamat lilailtizamu. tahqiq 'ahmad midhat almaraghi. bidun tabeati. alaskandariati: munsha'at almaearifi, 2004.
6. alsinhuri, eabdalrazaaqi. alwasit fi sharh alqanun almadani. bidun tabeati. bayrut: dar 'iihya' alturath alearabii, bidun tarikhi.
7. alsharif, nayif, w ziad alqarashi. alqanun altijari. ta: althaalithati. jidat: dar hafiz lilnashr waltawziei, 1430.
8. alsiduhi, eabdalmuneam. 'usul alqanuni. bidun tabeati. alqahirata: dar alnahdat alearabiat lilnashr waltawziei, 1998.
9. alsaraaf wahizbun, eabaas, wajurj. almadkhal 'iilaa eilm alqanuni. ta: alhadiat eashra. eaman, al'urdunu: dar lithaqafat lilnashr waltawziei, 1432.
10. alghamdi walhusayni, eabdalhadi, wabin yunis muhamadu. alqanun altijari. ta: althaalithati. alrayadi: maktabat alshaqray, 1430.
11. alfiruzbadi, majd aldiyn muhamad bin yaequba. alqamus almuhayta. ta: althaalithati. 4 mi. masiri: almatbaeat al'amiriati, bidun tarikhi.
12. alfiumi, 'ahmad bin muhamad. almisbah almunir fi ghurayb alsharh alkabiri. tahqiq eabdialeazim alshanawi. ta: althaaniatu. alqahirata: dar almaearifi, 1922.
13. alqadi, muhamad. hasan alniyat fi qanun aleuqubat dirasat tahliliat lifikrat hasan alniyat fi alqanun almisrii walqanun almuqarini. ta: al'uwlaa. alqahirata: dar alnahdat alearabiat lilnashr waltawzie, bidun tarikhi.
14. alqilyubi, samiha. alsharikat altijariati. ta: alkhamisati. alqahirata: dar alnahdat alearabiat lilnashr waltawziei, 2011.
15. alnizam al'asasiu lilhukm bialmamlakat alearabiat alsueudiat alsaadir bial'amr almalakii raqm 'a/90 bitarikh 27/8/1412h.
16. sliman, shir zad eaziza. hasan alniyat fi 'iibram aleuqud fi daw' alqawanin aldaakhiliat walaitifaqat alduwaliati. ta: al'uwlaa. al'urdunn: dar dijlat, 2008.
17. fraj waleadwi, twfyq hasan, wajalal ealay. alnazariat aleamat lilailtizam (masadir alailtizam wa'ahkam alailtizami). bidun tabeati. bayrut: manshurat alhalabi alhuquqiati, 2002.

18. fraj, twfyq hasan, w muhamad yahyaa mutari. al'usul aleamat lilqanuni. bayrut: aldaar aljamieiat liltibaeat walnashri, bidun tarikhi.

19. majmae allughat alearabiati. almuejam alwasiti. ta: al'uwlaa. bayrut: dar 'iihya' alturath alearabii, 1429.

20. musaa, muhamad yusif. al'amwal wanazariat aleaqd fi alfiqh al'iislamii mae madkhal lidirasat alfiqh wafalsafatih (dirasat muqaranatin. bidun tabeati. masra: dar alfikr alearabii, 1987.

21. nizam alsharikat alsueudiu alsaadir bialmarsum almalakii raqm ma/132 watarikh 1/12/1443h.