

THE ROLE OF GOOD FAITH IN PRE-CONTRACTUAL LIABILITY*

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Abstract

The breaking off of the negotiation phase, which is contrary to the good faith principle and cause the damages to the party, is unfair to the aggrieved party if the law cannot be enforced against the party who acts in bad faith during the pre-contractual stage, particularly when the parties expect to reach the final agreement and preliminarily commence the work without having the formal execution of written agreement due to the mutual trust, strict due date, or any demonstrate commitment. Such breaking off contrary to the good faith principle causes the damage to the aggrieved party especially with the project which has significant and large-scale investment value who may not be able to claim the pre-contractual liability from the other party.

Under the Thai Civil and Commercial Code (“CCC”) the issue remainings unclear and there is no practical guideline of Thai court that interprets the pre-contractual liability principle. Unlike Thai law, some European countries such as Germany and France have annexed the pre-contractual liability concept phase as their domestic contract law covering pre-contractual liability cases against the party who breaks off the negotiation with bad faith.

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According to the above problem of Thai law, this article will address the comparative study of pre-contractual liability concept with the analysis of the role of good faith principle in pre-contractual liability under the English law, which has never acknowledged the good faith principle under contract law.

The analysis demonstrates how the court could apply the good faith principle under CCC Section 3, 4 and 5 to the pre-contractual liability case as well as an alternative solution of amending the CCC to solve the said problems of pre-contractual liability case in Thailand.

Keywords: Pre-Contractual Liability, Duty to Negotiate in Good Faith, Role of Good Faith

1. Introduction

In the business context, whenever two or more parties, whether individual persons or juristic persons, decide to start the negotiation or bargain procedure, the parties have high expectations to reach the last stage of signing the final agreement or contract in order to commence the business engagement for their beneficial and mutual profits. Also, the negotiation process is considered as an important mechanism for business parties i.e. buyer/ seller, service provider/ service receiver to achieve their ultimate goal in exchanges within business markets especially in terms of business.

The parties normally make the pre-contractual agreement either in verbal form or written form e.g. e-mail correspondence or engagement as their evidence of agreeable terms and condition which contained with the scope of work, quotation fee, and action plan in order to avoid misunderstanding the details when commencing the scope of works and signing the final agreement especially when the parties who have the long business relationship together. For example, the construction company who has been working with the customer i.e. real estate developer for 20 years in many projects may verbally agree with its customer to build the housing project in Thailand during the pre-contractual phase without the final agreement since both parties have a strong business relationship due to some reasons such as the limitation time of schedule of work, or the internal process which takes time for approval by customer's committee. Later on, if the customers break off the contract with the construction company on the project which has started working in advance without the agreement. The construction company might not be able to claim the pre-contractual liability from the customer during the pre-contractual phase under the CCC. In addition, if the fact provides that the customer has no intention to reach the final agreement at the beginning and has bad faith to enter into a bargain procedure because just only to have access to some "Business Secrets". Such pre-contractual liability should be able to claim

with the party who contrary to the good faith principle under Thai contract law.

An example case from overseas regarding the pre-contractual liability during pre-contractual phase is *SIGA v. PharmAthene*¹. The fact was summarized as follows:

SIGA Technologies, Inc. (“SIGA”) entered into a bridge loan and merger agreement with Pharmathene, Inc. (“Pharmathene”), Inc. to solve its financial hardship which had been dropped out. Under the term and condition of such agreement, the parties agreed that the parties would negotiate in good faith in the License agreement (LATS) attached thereof. Later on, the financial status of SIGA became profitable and turned the good sign of business operation, SIGA decided to exercise its right to terminate the merger agreement with Pharmathene and refused to negotiate under the LATS accordingly. Such termination by SIGA’s bad faith caused the damage to Pharmathene from breaking off the duty to negotiate in good faith under such agreement and the LATS. For the judgement, the judge applied the Delaware law as agreed by both parties to solve this case and encompassed the activity that good faith principle was at the heart of the case, SIGA had breached its contractual obligation to negotiate in good faith, as an express contractual obligation to negotiate in good faith was binding on the contracting parties.

Overview of pre-contractual liability concept in Civil Law systems, the duty of negotiation in good faith have been stipulated the principle in its domestic code and used in practice for many countries such as Germany², Dutch³, Italy⁴ as their general principle to cover the case of breaking off the negotiation wrongfully by the act of bad faith, while Thai Law does not enact such principle in its domestic contract law.

¹ *SIGA Techs. Inc. v. PharmAthene, Inc.*, 67 A.3d 330, 347 (Del. 2013).

² German Civil Code, s 242.

³ Dutch Civil Code, art 248.

⁴ Italian Civil Code, art 1337.

On the other hand, in the Common law, English law does not recognize the general concept of good faith based on the traditional and historical and strongly denied to apply in business commercial⁵ cases. However, in the recent case of English law, the role of implied good faith principle has been recognized and implied throughout the Court Decision⁶ to justify the aggrieved party. It seems that the English court starts to recognize the good faith principle depending on the duty and the context of a contract or agreement which shall be expanded to imply by the court to the pre-contractual liability case, especially in the “relational” contract which requires and involves with the long-term relationship of the parties.

Therefore, this next chapter shall demonstrate the problem of pre-contractual liability in Thailand under the CCC and in practice since the party cannot claim the pre-contractual liability which has not yet occurred during the negotiation stage since the contractual obligation “rights” to exercise with each other.

2. Problem of pre-contractual liability in Thailand

Juristic acts under the CCC is stipulated in Section 149 stating that “juristic acts are voluntary lawful acts, the immediate purpose of which is to establish between persons juristic relations, to create, modify, transfer, preserve or extinguish rights.”

The juristic acts in Thailand may be divided into 2 types which are the bilateral juristic act and unilateral juristic acts such as promise, offer, invitation to treat,, etc. The legal status of formation of contract under Thai law to be created the obligation or “Contractual obligation” binding between the parties, the declaration of intention of both parties (offer and acceptance) must be met, whilst the legal status of pre-contractual liability during the negotiation stage, the contractual obligation or the declaration of

⁵ *Walford v Miles*. [1992] 2 AC 128.

⁶ *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111.

intention of both parties has not yet occurred which the party has no right to claim the liability which contrary to good faith⁷ principle.

On the other hand, the principle of good faith under the CCC is stipulated under Section 5 which was based on and influenced by Roman law. Although, the good faith principle is regarded as the general principle which is universally applicable (*Generalkauseln*), the interpretation and implementation of this principle are still confusing and there is no clear guidance for a judge when applying the principle. Some legal professionals and practitioners in Thailand have different viewpoints on this principle in contract law.

As such, the good faith principle under the CCC can be rarely seen according to Thailand's Court Decision using such principle by the judge to justify the parties in the situation where the contract terms of business commercial take advantage of the other especially in the case of negotiation in bad faith and sudden walk away with the damages and expenses.

Regarding the good faith principle, it can be seen that the Thai court admitted the general principle of good faith in many kinds of good faith throughout the court judgements in the past. For example the court applied the good faith principle to estoppel by conduct⁸ or to identify the bad conduct⁹ or even to prevent the bad faith¹⁰. However, it has never seen the principle of good faith applied in the case of breaking off the negotiation contrary to good faith in the pre-contractual stage.

7 Jampee Sotthibandhu, Rak Kham Rab Pid Korn Sanya [Pre-contractual liability] (3th edn, Winyuchon 2005) 45 (จำปี ไสตติพันธ์, หลักความรับผิดชอบก่อนสัญญา, (พิมพ์ครั้งที่ 3: วิญญูชน 2548)) 45.

⁸ Supreme Court case no. 1082/2533.

⁹ Supreme Court case no. 1538/2508.

¹⁰ Supreme Court case no. 371/2534.

3. The role of good faith principle in pre-contractual liability in foreign laws

3.1 The role of good faith principle in Civil Law

Most EU member countries have apparently recognized the notion of good faith principle as the general law and incorporated in their Civil codes as domestic law especially in the case of the pre-contractual stage which requires the party to negotiate in good faith and fair dealing. The following are the sample of Civil Code provisions of the Civil Law systems in the EU.

In the German civil law, section 242 provides that “everyone must perform his contract in the manner required by good faith and fair dealing (Treu und Glauben) taking into consideration the general practice in commerce”.

In the Dutch civil law, article 6:2 provides that “Good faith will not only supplement obligations arising from contract but may also modify and extinguish them”.

Under section 1337 of Italian civil law, it is required the contracting parties to act with good faith in any stages of the relationships i.e. negotiation stage, contracting stage, while France civil law, Napoleonic Code under article 2268 is stipulated that “Good faith is always presumed, and it is on the person who alleges bad faith to prove it.” as the general term and provision.

Therefore, in most Civil Law system countries, the concept of good faith is regarded as the general law and the highest norm to be respected in contractual and pre-contractual obligation.

4. The role of good faith principle in pre-contractual liability in English Law

Under English law, the Common Law system, the good faith principle has been strongly denied in the contract law unlike the Civil law system. English law is more focusing on the individualism which means that they

respect the freedom of contract of the parties to freely negotiate and pursue their own interest. Also, English law is based on the “judicial precedent” or “judge make law”¹¹. It means that English law is not based on the written code, but it solely depends on the case precedent. Therefore, the termination of negotiation does not breach English contract law since, in England contract law, the formation of a contract requires (1) offer and acceptance (2) consideration (3) an intention to be legally bound.

Although, the offer can be terminated as long as it does not have the consideration element in such offer or the offer has made of deed required by the law¹². English law does not provide the principle of pre-contractual liability during the negotiation process, but the English court prefers to develop the piecemeal solution instead of applying the good faith principle to override the fact of the case¹³. Therefore, based on the case precedents in the past, the good faith principle in contract law has been not recognized and used much in the Court Decision as an exceptional case.

However, in the recent case¹⁴ of the English court, the role of good faith has implied in the contract law where it is lack of good commercial business in respect of “relational contract” as the long-term contractual relationships and specific the special characteristics to scope such imply of the good faith principle in that case to justify the party.

This can be seen that the perception of good faith principle in English law has been changed and shown up to the spotlight to be considered and focused on by many legislators and law practitioners in

¹¹ Lloyd Duhaime, ‘The Common Law Legal Definition’ (*Duhaime’s Law Dictionary*) <<http://www.duhaime.org/LegalDictionary/C/CommonLaw.aspx>> accessed 12 December 2019.

¹² *Routledge v Grant* (1828) 4 Bing 653; 130 ER 920.

¹³ *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] QB 433.

¹⁴ *Bates & Ors v Post Office Limited* [2019] EWHC 606.

England. This will be a big impact in English contract law in terms of good faith principle and provide the guidance for the next case of pre-contractual liability and the role of good faith principle with the relational contract.

Therefore, the recent cases can imply that the English court applies the good faith principle more widely to the commercial contract. However, this case is also reminded the English court that, which applies the good faith principle to the case, should not overarch the real intention of mutual agreement by the parties. Nevertheless, it shall be a good sign of English law that it has acknowledged the good faith principle, besides the utmost good faith case, to justify the suffering party from breaking off the “relational’ contract.

In this regard, the Thai court may adapt the recent English court case to imply the good faith to justify the parties in case of pre-contractual liability in Thailand.

4. Recommendation

As mentioned earlier, the duty of good faith during the pre-contractual negotiation under Thai law has not yet been recognized since there has never been a case for the court to interpret the good faith principle to justify the party in this regard, even though the principle of good faith is considered as the general principle among the contract law.

Also, under the tort law of the CCC, the “rights” before the formation of a contract are not protected. As such, the pre-contractual liability in the negotiation phase cannot be claimed by the party and the pre-contractual obligation has not existed.

Therefore, in order to solve the issue of pre-contractual liability during the negotiation, the author would like to propose the following alternative solutions for applying it under Thai law.

4.1 To amend the CCC

In order to draw up the requirement of the parties and the validity of pre-contractual obligation during the negotiation phase, the CCC should add the pre-contractual principle to adjust and apply with the pre-contractual liability case like the other EU countries i.e. Germany, Italy, France.

Thus, please be advised to amend section 5 of the CCC according to the German Civil Law to extend the pre-contractual stage as follows:

Section 5 *“Every person must, in the exercise of his rights and in the performance of his obligations, act in good faith.*

“The rights in paragraph one shall be exercised and performed including but not limited to the period of the negotiation and formation of the legitimacy”

However, the process for amendment of the CCC might take long time to be considered and approved by the cabinet. Therefore, the following alternative option shall be considered to solve the current issue under Thai law.

4.2 To interpret the good faith principle under section 5 of the CCC with the analogy/ general principle under section 4 of the CCC

Of course, if the court or the legal practitioner can interpret and override the intention or fact of the contracting parties wherever they want, the interpretation of good faith principle in each case would be too subjective and vague according to the individual discretion. While section 5 of the CCC does not entail the duty of good faith during the pre-contractual stage, therefore section 4 of the CCC as the general principle is considered to analogy the principle of good faith and extend such rights covering to the pre-contractual stage.

Therefore, the author would like to purpose the criteria for the Thai court applying the good faith principle with analogy methods under Section

5 and Section 4 as the piecemeal solution by considering the level of the party's expectation of reaching the final contract/ agreement and the degree of significant investment or substantial financial impact of the project to justify the suffering party especially in the case of a big project with the high value of investment i.e. Joint venture company.

In summary, the author would like to highlight that the recommendation for the interpretation option to the Thai court by implying the general principle of good faith under section 5 and 4 to apply the case of pre-contractual liability considering with the clear criteria as provided above case-by-case basis and avoid the subjective discretion and bias of judge rather than considering to the amendment of CCC or stipulation of the specific law to be in accordance with other European countries.

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