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# Pre-contractual Obligations in France and the United States

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PRE-CONTRACTUAL OBLIGATIONS IN FRANCE AND THE UNITED STATES:  
A COMPARATIVE ANALYSIS

by

FLORENCE CATERINI

(Under the Direction of Professor James NEHF)

This thesis compares the pre-contractual obligations in France and the United States. The focus of this study is to analyze how both legal systems deal with these pre-contractual obligations. It focuses on the possibilities given to the parties to protect themselves during the negotiation process. In event of breach of negotiations, the law gives legal remedies to the parties. French and American laws have a different analysis of the problem but they reach similar result: liability under contract law when a contract has been formed or a tentative agreement, or under tort law when no agreement whatsoever has been reached.

INDEX WORDS: pre-contractual obligations, preliminary negotiations, caveat emptor, duty to disclose, misrepresentation, duty of care, parol evidence rule, merger clause, letter of intent, good faith, fair dealing, reliance, promissory estoppel, unjust enrichment.

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## **DEDICATION**

*I dedicate this thesis to my parents*

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## TABLE OF CONTENTS

	Page
ACKNOWLEDGEMENTS.....	v
INTRODUCTION .....	1
CHAPTER I - LIABILITY FOR MISREPRESENTATION OR FAILURE TO DISCLOSE INFORMATION.....	6
I- Formation of contract and preliminary negotiations.....	6
II- Ways of incurring liability before there is mutual assent .....	13
III- Some procedural problems that can arise when trying to prove misrepresentation or duty to disclose: parol evidence rule and merger clause.....	26
CHAPTER II - LIABILITY WHEN A PRELIMINARY OR TENTATIVE AGREEMENT IS MADE, BUT A FORMAL AGREEMENT IS CONTEMPLATED (BUT NEVER EXECUTED) .....	35
I- Preliminary negotiations in general—introduction to problems that can arise during negotiations and things that can go wrong.....	35
II- Letters of Intent.....	46



CHAPITRE III – OTHER BASES FOR LIABILITY: RELIANCE, UNJUST ENRICHMENT, AND TORT .....	59
I- Promissory estoppel .....	59
II- Unjust enrichment (quasi contract or restitution) .....	68
CONCLUSION.....	78
BIBLIOGRAPHY.....	82
LIST OF CASES.....	86

## INTRODUCTION

In the business world context today, more and more contracts are formed without the traditional “bargaining” to reach an agreement. Instead, business negotiation is surrounded by rules, principles, and mostly trade usages. This is called the *lex mercatoria* (or law merchant), which was originally a body of principles and rules relating to merchants and mercantile transactions in both legal systems. These customs date back many years, but still exist today in the form of usages applied in commercial transactions. In fact, in almost every kind of business, merchants themselves established these rules to regulate their dealings.

Furthermore, the parties have the responsibility during the negotiation period to abide by the applicable the usages no matter the context. The bargaining period involves potential pre-contractual liability for the parties in both American law and French law. Even if these two systems are different by their basic structure -common law system and civil law- they reach similar results at the end. In both legal systems, there is no strict rule, but there are some principles that the parties have to follow and respect. Even if a final agreement is not reached, sometimes the parties may still be liable even in absence of a written contract or agreement.

This period of negotiation involves risk for the respective parties until an agreement is signed. Indeed, the term negotiation or “to negotiate” can be defined as:

[T]o transact business, to bargain with another respecting a transaction; to conduct communications or conferences with a view to reaching a settlement or agreement. It is that which passes between the parties or their agents in the course of or incident to the making of a contract and is also conversation in arranging terms of contract.<sup>1</sup>

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<sup>1</sup> BLACK’S DICTIONARY 1036 (7<sup>TH</sup> ED. 1999)

In addition, according to the court in Al Herd, Inc. v. Isaac<sup>2</sup>, the term “to negotiate” is “to communicate or confer with another so as to arrive at the settlement of some matter.”<sup>3</sup> It is also “to meet with another so as to arrive through discussion at some kind of agreement or compromise about something.”<sup>4</sup> It is important to bear in mind that the ultimate aim of negotiation is to reach an agreement between the parties, creating a binding contract which generates obligations for both of them, and sometimes for third parties. During this period, the parties are free to negotiate but also to withdraw at will. Nevertheless, if the parties can terminate at will, they have to do so in good faith. Although obligations between parties are recognized by the legal community when a contract is signed, the obligations during the period of negotiations are difficult to determine. The issue of whether preliminary negotiations are binding between the parties depends upon different factors such as the type of documents and the surrounding circumstances.

The aim of this comparative study is to examine how both American law and French law systems are dealing with pre-contractual obligations between the parties at the negotiation stage. This paper will also define and identify the obligations between the parties during this negotiation period. Pre-contractual obligations will be analyzed mostly among commercial contracts and consumer contracts.

In part one, this study will analyze how liability may be incurred before there is mutual assent. It will focus on the situation where one party is held liable for misrepresentation or failure to disclose some important and relevant information to the other party. It will define the term “contract” and what should be understood by “binding agreement.” The most important

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<sup>2</sup> 76 Cal. Rptr. 697 (Cal. App. 2d Dist. 1969)

<sup>3</sup> *Id.* at 700

<sup>4</sup> *Id.* at 700

remaining issues are whether the intent to contract exists between the parties and whether there is manifestation of assent.

Furthermore, this study will explain the different and important elements required to constitute a valid and binding contract. American law and French law do not require the same elements. Whereas French law focuses on the cause of the contract and the subject matter, American law concentrates on whether the agreement is supported by valid consideration.

Part one will also focus on the notion of caveat emptor and its exceptions: duty to disclose, duty of care, misrepresentation and misrepresentation by silence. Under this doctrine of caveat emptor, one party cannot recover damages because of his or her lack of awareness at the time of the negotiation or even later on when the contract was formed. However, despite the parties may have some legal duties such as the duty to disclose and the duty of care. Misrepresentation, whether by fraud or by silence, can happen during this negotiation period. Some procedural problems may arise when trying to prove misrepresentation or the duty to disclose. These are also discussed in part one. Indeed, the negotiation period can be protected by the effect of the parol evidence rule. It seeks to preserve the integrity of written contracts by refusing to contradict the oral declarations of contracting parties. To protect themselves, the parties may want to include a merger clause in their final agreement to enclose the previous dealings. A merger clause is a provision where the parties indicate their intention that their writing was intended to be final and complete.<sup>5</sup>

In the second part, this study will focus on the liability when a preliminary or tentative agreement is made, but a formal agreement is only contemplated (but never executed). Indeed, whether an agreement is reached at the end of the negotiation process, preliminary negotiations

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<sup>5</sup> MURRAY, MURRAY ON CONTRACTS, Fourth Edition, 2001: THE PAROL EVIDENCE RULE – “INCONSISTENT” AND “CONTRADICTORY” – FORM OF WRITING – THE MEANING OF “INTEGRATION” § 83, 432.

in themselves do not constitute a contract. The parties may draft a contract early in the stage of negotiation with a condition precedent called “*condition suspensive*” in French law, in which at realization of a condition, the contract will be formed. Moreover, the parties can include some essential terms in their contract on which the parties agreed. In order to hold a contract enforceable, the essential terms of agreement have to be certain enough to provide a substantial basis for providing an appropriate remedy.<sup>6</sup> The parties also may want to have an agreement to reduce the contract to writing or to make it more formal. Here again, by using legal tools, the parties try to protect their interests during the delicate period of negotiations. It is important to note that French law, especially French Civil Code, does not have provisions which directly deal with the negotiation period.

The second part of this paper will also compare the system of letters of intent in both American law and French law. The parties may want to use this type of document to memorialize a basic agreement and to identify any potential deal breaking issues early in the negotiating process.<sup>7</sup> This is a possibility for the parties to regulate this period of risks - the negotiation period. The main legal issue arising from letters of intent is whether there is a binding agreement. This second part will analyze the legal nature of this pre-contractual writing and distinguish it from other legal documents. Here again, the parties may be bound by the duty to negotiate in good faith and fair dealing. In addition, the acts and words of the parties have a direct effect on their legal situation.

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<sup>6</sup> *Linnet v. Hitchcock*, 471 A.2d 537 (1984) at 214, the court indicates that “ an agreement is an enforceable contract wherein the parties intended to conclude a binding agreement and the essential terms of that agreement are certain enough to provide the basis for providing an appropriate remedy.” The court refers to *Lombrado v. Gasparini Excavating Co.*, 123 A.2d 663 (1956); *Yellow Coal Co. v. Alma Elly-YV Mines*, 426 A.2d 1152 (1981); RESTATEMENT (SECOND) OF CONTRACTS § 33 (1981) comment a, b.

<sup>7</sup> KATHRYN COCHRANE MURPHY, LETTER OF INTENT, AMERICAN LAW INSTITUTE – AMERICAN BAR ASSOCIATION CONTINUING LEGAL EDUCATION ALI-ABA COURSE OF STURY, 2003 (SH008 ALI-ABA 387).

The third and final part will analyze two legal doctrines in American law: the theory of promissory estoppel and the doctrine of unjust enrichment. It will determine their respective relations with pre-contractual obligations and their effects on the negotiation process. Promissory estoppel provides one party a remedy when the other changes his mind to the injury of the former. Even if no contract has been signed between the parties, one party can still make a claim for promissory estoppel if some elements are met: a clear and unambiguous promise, a reliance by the party to whom the promise is made, and an injury to the party as a result of this reliance. In French law, such a theory does not exist. However, a similar doctrine might have the same effects the “*théorie de l’apparence*.”<sup>8</sup> In addition, the injured party can make a claim under the unjust enrichment theory or “*enrichissement sans cause*.” This doctrine prohibits one party to from keeping benefits through the other party’s loss. It is a non-contractual liability based on the theory of restitution. In French law, this involves tort law or “*responsabilité délictuelle*” rather than contract law.

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<sup>8</sup> It can be translated as “theory of appearance.”

## CHAPTER I

### LIABILITY FOR MISREPRESENTATION OR FAILURE TO DISCLOSE INFORMATION

#### I- Formation of contract and preliminary negotiations

Before analyzing the notion of preliminary negotiations, it is important to define the term “contract” and how a valid contract is formed. A contract can be defined as “an agreement between two or more persons which creates an obligation to do or not to do a particular thing.”<sup>9</sup> Moreover, the Restatement Second of Contracts defines a contract as “a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognized as a duty.”<sup>10</sup> The court in Lamoureux v. Burrillville Racing Ass’n<sup>11</sup> indicates that this is “a legal relationship consisting of the rights and duties of the contracting parties; a promise or set of promises constituting an agreement between the parties that gives each a legal duty to the other and also the right to seek a remedy for the breach of those duties. Its essentials are competent parties, subject matter, a legal consideration, mutuality of agreement, and mutuality of obligation.”<sup>12</sup> Under the U.C.C., the term “contract” refers to a legal obligation

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<sup>9</sup> BLACK’S DICTIONARY 322 (7<sup>th</sup> ed. 1999)

<sup>10</sup> RESTATEMENT (SECOND) OF CONTRACTS § 1

<sup>11</sup> 161 A.2d 213 (1960).

<sup>12</sup> *Id.* at 6

which results from an agreement between the parties as affected by the Code Section 1-201(12).<sup>13</sup>

In addition, as to sales of goods, under U.C.C. Section 2-106(1) the terms “contract for sale” includes “both a present sale of goods and a contract to sell goods at a future time”<sup>14</sup> as well, whereas the terms “agreement” and “contract” are only limited to those relating to present or future sales of goods.<sup>15</sup> Plus, this is “the writing which contains the agreement of parties, with the terms and conditions, and which serves as a proof of the obligation.”<sup>16</sup>

Accordingly, pre-contractual documents and therefore preliminary negotiations differ from final contracts in their nature and elements. Indeed, to have a legally binding agreement in both American and French law, several requirements and elements have to be fulfilled.

First of all, in American law, a contract must be supported by valid consideration. According to the court in an early case, Hardesty v. Smith,<sup>17</sup> consideration is described as follows:

The doing of an act by one at the request of another, which may be a detriment or inconvenience, however slight, to the party doing it, or may be a benefit, however slight, to the party at whose request it is performed, is a legal consideration for a promise by such requesting party. So the parting with a right, which one possesses, to another, at his request, may constitute a good consideration.<sup>18</sup>

The doctrine of consideration and its importance has been affirmed and still is recognized by the courts.<sup>19</sup> Restatement First of Contracts §75 (1932) defines consideration as “an act other

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<sup>13</sup> U.C.C. §1-201(12) “‘contracts’, as distinguished from ‘agreement’, means the total legal obligation that results from the parties’ agreement as determined by [the Uniform Commercial Code] as supplemented by any other applicable laws.”

<sup>14</sup> U.C.C. §2-106(1)

<sup>15</sup> U.C.C. §2-106(1). See the Vienna Convention on International sale of goods (CISG), 1980 which includes the contract to sell goods at a future time.

<sup>16</sup> 191 A.2d 213 at 215 (1960).

<sup>17</sup> 3 N.E.2d 39 (1851).

<sup>18</sup> *Id.* See for a definition of consideration: *Curry v. Estate of Thompson*, 481 A.2d 658 at 661 (1984) Consideration “confers a benefit upon the promisor or causes a detriment to the promise and must be an act, forbearance of return promise bargained for and given in exchange for the original promise.”

<sup>19</sup> *Dougherty v. Salt*, 125 N.E. 94. (1919).



than a promise, or (b) a forbearance, or (c) the creation, modification or destruction of a legal relation, or (d) a return promise, bargained for and given in exchange for the promise...” Under the Restatement Second of Contracts §71 (1978) “(1) To constitute consideration, a performance or a return promise must be bargained for; (2) A performance or return promise is bargained for if it sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise; (3) The performance may consist of (a) an act other than a promise, or (b) a forbearance, or (c) the creation, modification, or destruction of a legal relation; (4) The performance or return promise may be given to the promisor or to some other person. It may be given by the promisee or by some other person.”

The second element is the intent to enter into a contract. A contract will be formed and enforceable only if the parties intended to enter into one. It is the manifestation of a party’s intention which counts, not the inner intention. The manifestation of mutual assent is therefore important and necessary to constitute a valid contract.<sup>20</sup> In fact, the intent of one party to enter into an agreement must be known by the other party (or at least reasonably apparent) in order for the agreement to be valid and enforceable at law.<sup>21</sup>

Moreover, the nature of assent is very important in the formation of contracts. The court in Embry v. Hargadin, McKittrick Dry Goods Co.<sup>22</sup> specifies that a contract is formed when there is the manifestation of intention of the parties. Accordingly, there is an agreement between the parties when they agreed on the same terms of their contract.<sup>23</sup> Further, in Hotchkiss v.

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<sup>20</sup> Lucy v. Zehmer, 84 S.E.2d 516 (1954).

<sup>21</sup> Butler v. Moses, 1 N.E. 316 (1885).

<sup>22</sup> 105 S.W. 777 (1907).

<sup>23</sup> *Id.* at 778 in this case only an oral contract was involved. The court asserts that to constitute a contract “there must be a meeting of the minds of the parties, and both must agree to the same thing in the same sense... the inner intention of parties to a conversation subsequently alleged to create a contract cannot either make a contract of what transpired, or prevent one from arising, if the words used were sufficient to constitute a contract... it is only such intention as the words or acts of the parties indicate; not one secretly cherished which is inconsistent with those words or acts.”

National City Bank of New York<sup>24</sup> the court indicates that the inner intent does not count but only express intent does.<sup>25</sup> In Lucy v. Zehmer,<sup>26</sup> the court cites the importance of taking into account the outward expression of the intent.<sup>27</sup>

However, in some situations, the parties do not seem to agree about some elements of the contract (present or future) but they misunderstand each other. If there is a basic misunderstanding, no contract or agreement can be reached by the parties because there is no manifestation of mutual assent. The Restatement Second of Contracts regulates the situation of misunderstanding.<sup>28</sup> A particular decision, Cargill Commission Co. v. Mowery,<sup>29</sup> illustrates this situation and therefore emphasizes the importance of words in contracts.<sup>30</sup>

The third element of a contract is the offer. A contract is constituted by an offer and an acceptance. An offer is defined as “an expression by one party of his assent to certain definite terms, provided that the other party involved in the bargaining transaction will likewise express his assent to the identically same terms.”<sup>31</sup> The court in Lefkowitz v. Great Minneapolis Surplus Store, Inc.<sup>32</sup> indicates that an offer has to be definite, clear, and explicit. It has to leave nothing

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<sup>24</sup> 200 Fed. 287 (S.D.N.Y. 1911).

<sup>25</sup> *Id.* at 293

<sup>26</sup> 84 S.E. 2d 516 (1954).

<sup>27</sup> *Id.* at 521 the court indicates that “we must look to the outward expression of a person as manifesting his intention rather than to his secret and unexpressed intention.” According to First Nat. Exchange Bank of Roanoke v. Roanoke Oil Co., 192 S.E. 794 at 770 (1937) the court states that “the law imputes to a person an intention corresponding to the reasonable meaning of his words and acts.”

<sup>28</sup> RESTATEMENT (SECOND) OF CONTRACTS: EFFECT OF MISUNDERSTANDING §20 “(1) There is no manifestation of mutual assent to an exchange if the parties attach materially different meanings to their manifestations and (a) neither party knows or has reason to know the meaning attached by the other; or (b) each party knows or each party has reason to know the meaning attached by the other. (2) The manifestations of the parties are operative in accordance with the meaning attached to them by one of the parties if (a) that party does not know of any different meaning attached by the other, and the other knows the meaning attached by the first party, or (b) that party has no reason to know of any different meaning attached by the other, and the other has reason to know the meaning attached by the first party.”

<sup>29</sup> 161 P. 634 (1916)

<sup>30</sup> *Id.* In this case a mistake was made regarding the amount of goods. *See also Raffles v. Wichelhaus*, 2 Hurlstone & Coltman 906 (Court of Exchequer, 1864).

<sup>31</sup> CORBIN ON CONTRACTS §11 at 22 (1963), 403, in ROBERT S. SUMMERS & ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATIONS: THEORY, DOCTRINE, AND PRACTICE, Fourth Edition 2001.

<sup>32</sup> 86 N.W. 2d 689 (1957).

open for negotiation.<sup>33</sup> Thus, it constitutes an offer, acceptance of which will complete the contract.<sup>34</sup>

Accordingly, an offer must be followed by an acceptance. Acceptance is the fourth element of a valid agreement. The acceptance is a voluntary act of the offeree whereby he exercises the power conferred upon him by the offer, and thereby creates the set of legal relations called a contract.<sup>35</sup> The court in Ardente v. Horan<sup>36</sup> indicates that “to be effective, an acceptance must be definite and unequivocal.”<sup>37</sup> Further, acceptance should not add some conditions or limitation on the offer. If that is the case, it will not be an acceptance but a counter-offer.<sup>38</sup> Moreover, an acceptance has to be in the form required by the offer.<sup>39</sup> It is important to emphasize that silence does not usually constitute an acceptance.<sup>40</sup> Therefore, in some cases, it is difficult to determine whether there is a binding contract between the parties.<sup>41</sup> Nevertheless, a

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<sup>33</sup> *Id.* at 691 the court refers also to *Johnson v. Capital City Ford Co.*, 85 So. 2d 75 (1955) at 192.

<sup>34</sup> *See* *Courteen Seed Co. v. Abraham*, 275 P. 684 (1929) (which emphasized the importance of the words in an offer. The court held that “the language... did not constitute an offer of sale; that the language was general, and such, might be used in an advertisement or circular addressed generally to those engaged in the seed business; and that such language was not an offer by which the defendant was bound, if accepted by any or all of the persons addressed.”)

<sup>35</sup> COBIN, OFFER AND ACCEPTANCE, AND SOME OF THE RESULTING LEGAL RELATIONS, 26 Yale L.J. 169, 199-200 (1917) citing in ROBERT S. SUMMERS & ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATIONS: THEORY, DOCTRINE AND PRACTICE, Fourth Edition, 417.

<sup>36</sup> 366 A.2d 162 (1976)

<sup>37</sup> *Id.* at 260. *See* RESTATEMENT (FIRST) CONTRACTS §58, (1932) comment a “An offeror is entitled to know in clear terms whether the offeree accepts his proposal. It is not enough that the words of a reply justify a probable inference of assent.”

<sup>38</sup> In *Ardente*, 366 A.2d 162 (1976), the court found that was the case of a counteroffer and not an acceptance. The court asserts that “an acceptance which is equivocal or upon condition or with a limitation is a counteroffer and requires acceptance by the original offeror before a contractual relationship can exist. However, an acceptance may be valid despite conditional language if the acceptance is clearly independent of the condition.” *Id.* at 165.

<sup>39</sup> *See* *Eliason v. Henshaw*, 17 U.S. 225 (1819), (this explains that an acceptance has to be made in the manner required and stipulated by the offer. The court states that “an acceptance communicated at a place different from that pointed out by the buyers, and forming a part of their proposal, imposed no obligation binding upon them, unless they had acquiesced in it, which they declined doing.”)

*See* UNIFORM COMMERCIAL CODE §2-206(1)(a) “(1) Unless otherwise unambiguously indicated by the language or circumstances (a) an offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in the circumstances.”

<sup>40</sup> *Ducommun v. Johnson*, 110 N.W. 2d 271 at 274 (1961). RESTATEMENT (SECOND) CONTRACTS: ACCEPTANCE BY SILENCE OR EXERCISE OF DOMINION §69 cites the cases in which the silence or inaction means acceptance.

<sup>41</sup> *Southworth v. Oliver*, 581 P.2d 994 (1978) in which the question was whether there is a binding contract. The court refers to the intention of the parties, the manifestation of this intention, the facts and the circumstances existing

contract can be recognized as binding even if some terms are left open.<sup>42</sup> Here again, it is the intention of the parties which will determine whether the contract is binding.

French law has approximately the same concept of contract and the same elements toward contract formation as American law. However, the concept of consideration does not exist in the French law system. Article 1101 of the French Civil Code defines a contract as an agreement by which one or more parties obligate themselves to one or more other parties to give, or to do or not to do, something.<sup>43</sup> Besides an offer and acceptance, a contract needs four elements according to article 1108 of the French Civil Code: the consent of the party who has the duty to perform, his or her capacity of contracting, a subject-matter or object upon which the contract is based (a sale of goods or services), and a cause (the reason why the contract is made).<sup>44</sup>

In addition, a contract needs to have a price.<sup>45</sup> This element remains very important in French law. It does not matter if the price is defined or not but at least it has to have some elements towards its determination. The price has to be designed by the parties and included in

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at the time of the document (the letter) was received and to what a reasonable person would have done (and whether the intention was obvious to a reasonable person).

<sup>42</sup> See UNIFORM COMMERCIAL CODE §2-204(3) which explicitly provides that “Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.”

<sup>43</sup> See PAULA GILIKER, *PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW*, 3 (Kluwer Law International, 2002) “le contrat est une convention par laquelle une ou plusieurs personnes s’obligent, envers une ou plusieurs autres, à donner, à faire ou à ne pas faire quelque chose.”

See also Article of JOHANNA SCHMIDT, *LES LETTRES D’INTENTION*, [LETTERS OF INTENT] RDAI/IBLJ, Number 3/4, 2002.

<sup>44</sup> Article 1108 C.CIV states that “Quatre conditions sont essentielles pour la validité d’une convention : le consentement de la partie qui s’oblige; sa capacité de contracter; un objet certain qui forme la matière de l’engagement; une cause licite dans l’obligation.”

<sup>45</sup> Article 1591 C.CIV states that “le prix de la vente doit être déterminé et désigné par les parties” and article 1129 C.CIV cites “il faut que l’obligation ait pour objet une chose au moins déterminée quant à son espèce. La quotité de la chose peut être incertaine, pourvu qu’elle puisse être déterminée.” which means that an obligation must have for its object something determinate at least as to its nature.

the contract.<sup>46</sup> This requirement is essential in contracts of sale. Article 1583 of the French Civil Code requires that there must be agreement on the price and the object of the contract.<sup>47</sup>

French law requires the subjective will of the parties or “*l'accord de volontés.*”<sup>48</sup> Moreover, according to article 1108 of the French Civil Code<sup>49</sup> the consent of both parties is required and necessary. Accordingly, the formation of a contract will depend on the subjective will of the parties.<sup>50</sup> Thus, in case of a suit, the courts will seek terms which both parties objectively and subjectively agree are essential to the contract. Thus, it is more difficult to know whether or not the agreement of the parties constitutes a valid and binding contract during the stage of negotiation.

Because the negotiation period involves risks for both of the parties, it is important to know what exactly their legal obligations and duties are during this pre-contractual stage.

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<sup>46</sup> Article 1591 C.CIV and Article 1129 C.CIV. See Cass. Civ, Jul. 16, 1974, D. 1974. 681 note P. Malaurie, which indicates that the price has to be clear and adequate. Since 1978, by three important cases, the Cour de Cassation intervenes on the grounds of article 1129 C.CIV and not on article 1591 C.CIV in order to determine whether the price is determined or can be determined by some methods (which shall be cited in the agreement). See Cass. Com. Oct. 11, 1978, D. 1979. 135 note R Houin; JCP 1979 II 19034 note Y Loussouarn; RTDC 1979. 129 obs Y Loussouarn; RTDC 1980.364 obs G Cornu.

<sup>47</sup> Article 1583 C.CIV provides that “elle est parfaite entre les parties, et la propriété est acquise de droit à l'acheteur à l'égard du vendeur, dès qu'on est convenu de la chose et du prix, quoique la chose n'ait pas encore été livrée ni le prix payé” which can be translated in “the sale is perfect between the parties, the ownership is transferred from the seller to the buyer, when there is an agreement upon the thing and the price, even if the thing has not been delivered yet and the price has not been paid.”

<sup>48</sup> Article 1134 C.CIV indicates that “les conventions légalement formées tiennent lieu de loi à ceux qui les ont faites. Elles ne peuvent être révoquées que de leur consentement mutuel, ou pour les causes que la loi autorise. Elles doivent être exécutées de bonne foi.”

<sup>49</sup> Article 1108 C.CIV stipulates “le consentement de la partie qui s'oblige.”

<sup>50</sup> See the leading case of 1978, Cass. Civ., May 2, 1978, D. 1979. 317 note J Schmidt; JCP 1980 II 19435. The “Cour de Cassation” (superior French jurisdiction) found that a disagreement about some modalities of the payment (dates for payment of the balance of the sale price and for possession) which were very important to the seller, obstructed formation of the contract. It has to be concluded that the will of one party is thereby capable of rendering an ordinary minor term vital in the context of the present agreement, although this must be stated expressly before acceptance by the other party. See also Rep 20.1.1941 DA 1941. 179.

## II- Ways of incurring liability before there is mutual assent

### A- Caveat emptor: the general approach in the U.S.

Because the parties are free to contract or not,<sup>51</sup> they should be liable for their acts or forbearances. Moreover, they have to pay attention to the contract they sign, the terms cited in this contract, and their respective obligations. In addition to the theory of freedom of contract,<sup>52</sup> the common law brought the theory of *caveat emptor*. This legal maxim means “let the buyer beware.” In sum, it implies that the buyer takes the risk regarding quality or condition of the item purchased unless protected by warranty, or if the buyer is a victim of misrepresentation.<sup>53</sup> As an illustration, in Colton v. Stanford,<sup>54</sup> the court emphasizes that “the greatest liberty of making contracts is essential to the business interests of the country. In general, the parties must look out for themselves.”<sup>55</sup> In Obde v. Schlemeyer,<sup>56</sup> a case involving a purchase of a house in which damages occurred because of a termite infestation, the sellers argued that the purchasers asked no questions respecting the possibility of termites. They relied on Swinton v. Whitinsville Sav. Bank<sup>57</sup> in which the doctrine of *caveat emptor* was strictly applied. The court stated that “as between parties dealing at arms length (as vendor and purchaser) there is no duty to speak, in the absence of a request for information... A vendor of real property has no duty to disclose to a

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<sup>51</sup> They are also free to cancel a contract. *See Colton v. Stanford*, 82 Cal. 351 at 398 (1890) “the power to cancel a contract is a most extraordinary power. It is one which should be exercised with great caution... A too free use of this power would render all business uncertain; ... make the length of a chancellor’s foot the measure of individual rights.”

<sup>52</sup> This principle which also exists in French law, refers to the fact that the parties can contract whenever they want and they are free to do so. Therefore the contract requires the meeting of minds or “*accord de volontés*” of both parties.

<sup>53</sup> See infra 2) Duties of the parties: exceptions to caveat emptor b) Misrepresentation.

<sup>54</sup> 82 Cal. 351 (1890).

<sup>55</sup> *Id.* at 398

<sup>56</sup> 353 P.2d 672 (1960). In this case the doctrine of *caveat emptor* was not applied and the court cites “we are convinced that the defendant had a duty to inform the plaintiff of the termite condition.”

<sup>57</sup> 42 N.E. 2d 808 (1942).

prospective purchaser the fact of a latent termite condition in the premises.”<sup>58</sup> In some decisions, courts have recognized the buyer liable under the doctrine of caveat emptor.<sup>59</sup>

However, despite its apparent force, the caveat emptor doctrine has been limited since its origin.<sup>60</sup> It is shown by several decisions that courts often try to protect the consumer from the acts or words of the seller.<sup>61</sup> In fact, sellers usually are in a stronger position than the buyer is. Indeed, most of the time, they do not have the same bargaining power. Legislation regarding consumer contracts aims to give strong protection to the consumer. Of course, buyers still have to beware when purchasing a good (or a service), but sellers are confronted with more obligations than they were in the past. Sellers sometimes have a duty to disclose and a duty of care. Indeed, in Reed v. King,<sup>62</sup> the court emphasized that in real estate transactions, the seller has a duty to disclose known defects and therefore the doctrine of caveat emptor has little or no application.<sup>63</sup>

When contracts do not involve a consumer and a seller but rather two professionals (in a sense that they are both doing the same type of business), the doctrine of caveat emptor can be applied and the seller has no duty to disclose. This notion of duty to disclose is discussed in the

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<sup>58</sup> *Id.* at 452

<sup>59</sup> See e.g., Kuczanski v. Gill, 302 S.E.2d 48 (1983); Layman v. Binns, 35 Ohio St. 3d 176 (1988); Williams v. Neff, 43 Va. Cir. 464 (1997), Van Horn v. Peoples Banking Co., 64 Ohio App. 3d 745 (1990); Landers v. Scroggy, 294 Ky. 848 (1943); Lee v. Bowers, 31 Va. Cir. 147 (1993); Gibson v. Lambeth, 86 N.C. App. 264 (1987).

<sup>60</sup> See article KEETON, FRAUD - CONCEALMENT AND NON-DISCLOSURE, 15 Tex. Law Review (December 1936) 1, 14-16. Professor Keeton cites “when Lord Cairns stated in Peek v. Gurney that there was no duty to disclose facts, however morally censurable their non-disclosure may be, he was stating the law as shaped by an individualistic philosophy based upon freedom of contract. It was not concerned with morals. In the present stage of the law, the decisions show a drawing away from this idea, and there can be seen an attempt by many courts to reach a just result in so far as possible, but yet maintaining the degree of certainty which the law must have. The statement may often be found that if either party to a contract of sale conceals or suppresses a material fact which he is in good faith bound to disclose then his silence is fraudulent.”

<sup>61</sup> See e.g. Obde v. Schlemeyer, 353 P.2d 672 at 674-675; Bowdring v. McKee, 57 Va. Cir. 9 at 9-10 (2001)

<sup>62</sup> 193 Cal. Rptr. 130 (1983).

<sup>63</sup> *Id.* at 131-132 “a seller of real property has a duty to disclose: where the seller knows of facts materially affecting the value or desirability of the property which are known or accessible only to him and also knows that such facts are not known to, or within the reach of the diligent attention and observation of the buyer, the seller is under a duty to disclose them to the buyer. The ancient maxim caveat emptor, let the buyer beware, has little or no application to California real estate transactions.” *E.g.* some States like Georgia have legislation regarding duty to disclose in real estate contracts.

following section. However, a seller cannot be afforded protection under the doctrine of caveat emptor if he or she makes false representations of material fact.<sup>64</sup>

## B- Duties of parties: exceptions to caveat emptor

### 1) Duty to disclose

One party, usually the seller, has a duty not to mislead the other. This is called the duty to disclose. The questions are what is the extent of this legal duty and how does a seller know when he has fulfilled his obligation.

In American law, duty to disclose is part of the notion of misrepresentation. According to Professor Murray, “the notion that one party has a duty to disclose relevant information to the other party who has equal access to such information appeared antithetical to courts holding traditional views of individuality and bargaining.”<sup>65</sup> This legal duty is therefore more important in pre-contractual relations between the parties. In order to contract, a party has to know all (or almost) the information and relevant material facts about the agreement the parties will reach. For example, in Bates v. Cashman,<sup>66</sup> a case regarding the purchase of stocks and bonds of a company, the buyer would not have signed the contract if he had known that the seller’s statement during the negotiations preceding the contract did not correspond to reality. The buyer has the possibility to rescind a contract if the seller failed to disclose important and relevant material facts or if the seller misrepresented the facts.<sup>67</sup>

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<sup>64</sup> *E.g.* Bowdring v. McKee, 57 Va. Cir. 9. (2001); Jacobs v. Racevskis, 663 N.E.2d 653 (1995); Lepera v. Fuson, 613 N.E.2d 1060 (1992); Grigsby v. Stapleton, 7 S.W. 421 (1887).

<sup>65</sup> MURRAY, MURRAY ON CONTRACTS, Fourth Edition, 2001: MISREPRESENTATION §95, 536.

<sup>66</sup> 119 N.E. 663 (1918).

<sup>67</sup> *Id.* 119 N.E. 663 at 663 (1918) “the defendant relied upon it and would not have signed the contract if he had known that it was false. A person seasonably rescind a contract to which he has been induced to become a party in reliance upon false though innocent misrepresentations respecting a cognizable material fact made as of his own knowledge by the other party to the contract.”



Nowadays, courts analyze non-disclosure as misrepresentation regarding its legal effects. For example, in a case dealing with the purchase of a house infested with termites, and the seller knew this fact and failed to disclose it to the buyer, even though the contract contained a disclaimer clause, the court stated that “a provision in such a contract, to the effect that the agent cannot bind the company by any representations, statements or agreements, will not relieve the principal from responsibility for the fraudulent representations, made by its agents, concerning the subject-matter of the contract . . . for a sales agent has ostensible authority to make representations as to the subject-matter of the sale, and his fraud, committed within the limits of such authority, will fix responsibility upon his principal.”<sup>68</sup> Here again, this is an important material fact that the buyer of a house should know, especially during the negotiation process. A situation of non-disclosure is legally similar to disclosing a fraudulent fact. Indeed, misrepresentation can be either by fraud or by silence. Silence fraud occurs when the defendant fails to disclose some information to the plaintiff. In order to establish this, the plaintiff has to prove five elements. First, the plaintiff must prove that the defendant failed to disclose some material fact about the subject matter of the claim; second, that the defendant knew these material facts; third, that there was a causal link between the defendant’s failure to disclose the facts and the plaintiff having a false impression (and moreover that the defendant knew the failure would create a false impression); fourth, that the defendant intended that the plaintiff rely on the resulting false impression and he effectively relied on this false impression; and finally, a damage occurred as a result of the reliance on the false impression.<sup>69</sup> For example, in Swinton v. Whitinsville Savings Bank,<sup>70</sup> a case dealing with concealment of a termite infestation in the

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<sup>68</sup> *Gibb v. Citicorp Mortgage, Inc*, 518 N.W.2d 910 (1994) at 364.

<sup>69</sup> See article AARON LARSON “FRAUD, SILENT FRAUD AND INNOCENT MISREPRESENTATION”, Oct, 2003, available at [http://www.expertlaw.com/library/pubarticles/Business\\_Law/fraud.html](http://www.expertlaw.com/library/pubarticles/Business_Law/fraud.html).

<sup>70</sup> 42 N.E.2d 808 (1942).

house the buyer purchased, the seller knew that the house was infested and the buyer could not readily observe this condition upon inspection.<sup>71</sup> The seller fraudulently and falsely concealed from the buyer the house's true condition. In Weintraub v. Kroatsh,<sup>72</sup> a house was purchased and the buyer discovered that it was infested by cockroaches when he moved in.<sup>73</sup> The seller had a duty to speak and failed to do so.<sup>74</sup> In addition, the seller conducted the visit of the house during the day although the buyer could have seen the cockroaches only during the night.<sup>75</sup> The buyer sued for rescission of the contract. The *Weintraub* court refers to Keen v. James,<sup>76</sup> where the court pointed out that "silence may be fraudulent and the relief may be granted to one contractual party where the other suppresses facts which he, under the circumstances, is bound in conscience and duty to disclose to the other party, and in respect to which he cannot, innocently, be silent."<sup>77</sup> Therefore, even if the buyer has to make reasonable investigations about the good he wants to purchase,<sup>78</sup> the seller still has a duty to speak.<sup>79</sup>

This duty to disclose imposed by the law to the seller constitutes an exception to the well-known doctrine of *caveat emptor*. This doctrine no longer prevails and courts do not apply it

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<sup>71</sup> *Id.* at 678

<sup>72</sup> 317 A.2d 68 (1974).

<sup>73</sup> *Id.* at 70

<sup>74</sup> *Id.* at 72 relying on *Obde v. Schlemeyer*, 353 P.2d 672 at 674 (1960).

<sup>75</sup> *Id.* at 70

<sup>76</sup> 39 N.J.Eq. 527 (E. & A. 1885).

<sup>77</sup> *Id.* at 541

<sup>78</sup> See *Simmons v. Evans*, 206 S.W.2d 295 (1947) in which the plaintiffs purchased a house in which the water was supplied only at the day time but not at night. The sellers failed to disclose this important fact and the plaintiffs filed an action to rescind their purchase. But the lower court dismissed it on the ground that "the defendants had not made any written or verbal representations and the plaintiffs had inspected the property, knew the source of the water supply, and could have made specific inquiry of these defendants or ascertained from other sources the true situation and, therefore, are estopped." 206 S.W.2d at 296. However, the dismissal was reversed on appeal. The court asserts that "one may be guilty of fraud by his silence, as here it is expressly incumbent upon him to speak concerning material matters that are entirely within his own knowledge" 206 S.W.2d at 296 and also that the plaintiffs were not required to "make a night inspection in order to ascertain whether the water situation with reference to this residence was different from what it was during the day." 206 S.W.2d at 297.

<sup>79</sup> See *Conover v. Wardell*, 22 N.J. Eq 492 at 498-99 (E. & A. 1871), "under the circumstances, is bound in conscience and duty to disclose to the other party, and in respect to which he cannot, innocently, be silent."

anymore (or in rare cases).<sup>80</sup> In Obde v. Schlemeyer,<sup>81</sup> a similar case about fraudulent silence, the seller had a duty to disclose that the apartment was infested by termites and failed to do so.<sup>82</sup> The court asserted that there is a duty to speak whenever justice, equity and fair dealing demand it. Indeed, because a termite infestation of an apartment is a serious and dangerous condition (major condition), the seller had a strong responsibility is to disclose this fact and thus not mislead the buyer by keeping silent about it.<sup>83</sup> Therefore, if a seller fails to disclose a material fact or to answer a question asked by the purchaser, he can be liable for fraudulent nondisclosure.<sup>84</sup> The court indicated the difference between minor conditions, which ordinary parties would reasonably disregard as of little or no materiality in the transaction which would clearly not call for judicial intervention, and major condition upon which sellers have a duty to disclose and a duty to speak. Moreover, the seller has the duty to disclose the material facts, and a half-truth will be considered as misrepresentation unless the party to whom such a revelation is made does not rely upon it.<sup>85</sup> Also, according to Restatement Second of Contracts<sup>86</sup> there are some limited cases when the non-disclosure is equivalent to an assertion.<sup>87</sup>

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<sup>80</sup> See e.g. about the doctrine of *caveat emptor* which is not applied anymore in New Jersey Berman v. Gurwicz, 458 A.2d 1311 at 455 (Ch. Div. 1981), Lingsch v. Savage, 29 Cal. Rptr. 201 at 209 (Dist. Ct. App. 1963), Easton v. Strassburger, 199 Cal. Rptr. 383 (Ct. App. 1984).

<sup>81</sup> 353 P.2d 672 (1960).

<sup>82</sup> *Id.* at 675

<sup>83</sup> Ensminger v. Terminix Int'l Co., 102 F. 3d 1571 (10<sup>th</sup> Cir. 1996); Johnson v. Davis, 480 So. 2d 625 (1985); Mercer v. Woodard, 303 S.E.2d 475 (1983); Lynn v. Taylor, 642 P.2d 131 (1982).

<sup>84</sup> In some decisions the court refers to the "duty to speak." See Marchand v. Presutti, 505 A.2d. 1092 (1986).

<sup>85</sup> Nader v. Allegheny Airlines, Inc., 626 F.2d 1031 (1980).

More explanations will be made on the notion of misrepresentation in part 2) Misrepresentation.

<sup>86</sup> RESTATEMENT (SECOND) OF CONTRACT §161 provides "a person's non-disclosure of a fact known to him is equivalent to an assertion that the fact does not exist in the following cases only: (a) where he knows that disclosure of the fact is necessary to prevent some previous assertion from being a misrepresentation or from being fraudulent or material. (b) Where he knows that disclosure of the fact would correct a mistake of the other party as to a basic assumption on which that party is making the contract and if non-disclosure of the fact amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing. (c) Where he knows that disclosure of the fact would correct a mistake of the other party as to the contents or effect of a writing, evidencing or embodying an agreement in whole or in part. (d) Where the other person is entitled to know the fact because of a relation of trust and confidence between them."

<sup>87</sup> See Skagit State Bank v. Rasmussen, 716 P.2d 314 (1986); 745 P.2d 37 (1987).

Because dealings are often long and complicated, it is important for both of the parties to disclose any relevant information. Moreover, sometimes it is not only important to disclose information about what is being sold but also any information about the legal effect of the contract terms.<sup>88</sup> The seller has a duty to inform the buyer about the contract when it contains either fine print or hidden terms. This duty especially exists when one party is in a superior position or has superior knowledge.<sup>89</sup> If the information is not disclosed, such a contract will be an unconscionable one regarding the bargaining power of the stronger party.<sup>90</sup>

In French law, the principle and legal effects of this duty to disclose or “*obligation précontractuelle de renseignement*” is the same as in American law. French law imposes a pre-contractual obligation to disclose information.<sup>91</sup> It is based on a mixture of statutory (consumer protection by French Civil Code) and case-law intervention, but the courts have been prepared to award damages on the basis of tort responsibility (or “*responsabilité délictuelle*”) for non-disclosure of certain essential and material facts provided by article 1382.<sup>92</sup> As it is for misrepresentation, misrepresentation by silence or “*omission*” in French law makes the contract voidable.<sup>93</sup> Thus the party can ask for rescission of the contract in a situation of “*omission*.”<sup>94</sup> French law provides that silence is considered as a “*dol*” and more precisely a “*dol négatif*” if

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<sup>88</sup> Weintraub v. Krobatsch, 317 A.2d 68 (1974).

<sup>89</sup> E.g. Weaver v. American Oil Co., 276 N.E.2d 144 (1971) in which one party could not read the lease because of its lack of education. In such a case the other party has a duty to inform him about the terms and conditions of the said lease.

<sup>90</sup> *Id.* at 148 (1971) “when a party can show that the contract, which is sought to be enforced, was in fact an unconscionable one, due to a prodigious amount of bargaining power on behalf of the stronger party, which is used to the stronger party’s advantage and is unknown to the lesser party, causing a great hardship and risk on the lesser party, the contract provision, or the contract as a whole, if the provision is not separable, should not be enforceable on the grounds that the provision is contrary to public policy.”

<sup>91</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 128 (Kluwer Law International, 2002).

<sup>92</sup> Article 1382 C.CIV. provides “tout fait quelconque de l’homme, qui cause à autrui un dommage, oblige celui par la faute duquel il est arrivé, à le réparer.” The idea of this provisions is that every act of someone, which cause to someone’ else an injury, has the duty to repair it.

<sup>93</sup> VALERIE TOULET, DROIT CIVIL, OBLIGATIONS RESPONSABILITE CIVILE, [CIVIL LAW, OBLIGATIONS CIVIL RESPONSABILITY], 64 (édition centre de publications universitaire 1999).

<sup>94</sup> Held v. Trafford Realty Co., 414 So. 2d 631 at 632 (Fla. Dist. Ct. App. 1982).

this silence is fraudulent and the party which has the duty to reveal some elements failed to do so.<sup>95</sup> For example, a “*dol négatif*” or “*réticence dolosive*” was recognized in a case where an automobile mechanic kept silent about the fact that an engine was very old.<sup>96</sup> The buyer purchased the automobile with a strong believe that the engine was a new one regarding its mileage. The automobile mechanic modified the mileage of the engine and kept silent about this change. Thus, in cases like this one, courts consider that voluntary silence is in reality lack of good faith.<sup>97</sup>

Furthermore, French law makes a distinction between persons who are not in the same type of business (considered non-professionals or consumers) and others who are in the same type of business. Similar to American law, French law gives more protection to consumers than to parties who are engaged in the same type of business. It is important to note that usually the duty to disclose is related to formation of a contract: a party signed a contract without being informed or advised of certain facts which would have influenced his decision.

Although French law has no regulations in its civil code about preliminary contracts or preliminary negotiations, it recognizes that at least at the beginning of the dealings no responsibility could arise. This can be explained by the French law principle of “*liberté contractuelle*” (freedom to contract). According to this concept, courts do not usually interfere in private contractual relations except when a law suit is brought. Then, there are some risks which are endured by both of the parties during negotiations. However, one party, usually the seller,

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<sup>95</sup> VALERIE TOULET, DROIT CIVIL, OBLIGATIONS RESPONSABILITE CIVILE, [CIVIL LAW, OBLIGATIONS CIVIL RESPONSABILITY], 64 (édition centre de publications universitaire 1999).

<sup>96</sup> Cour de Cassation, Civ. 1<sup>re</sup>, 19.06.1985, Bull. civ. I, Numero 201, the court indicates that “en s’abstenant d’indiquer [à l’acheteur non spécialiste] que le moteur, remonté sur un modèle de 1975 annoncé comme en parfait état, datait de 1968.”

<sup>97</sup> VALERIE TOULET, DROIT CIVIL, OBLIGATIONS RESPONSABILITE CIVILE, [CIVIL LAW, OBLIGATIONS CIVIL RESPONSABILITY], 65 (édition centre de publications universitaire 1999).

still has the duty to disclose and this party can be liable when he fails his obligation. In French law, this responsibility will be based on lack of good faith.<sup>98</sup>

## 2) Misrepresentation

Sometimes at the time of negotiations a party wants to convince the other to contract and will mislead with regard to some relevant material facts. Misrepresentation can be defined as the act of making a false or misleading statement with the intent to deceive or mislead someone.<sup>99</sup> According to Restatement Second of Contracts, misrepresentation is defined as “an assertion that is not in accord with the facts.”<sup>100</sup> However, sometimes it is difficult to differentiate the “seller’s talk”<sup>101</sup> (or “puffing”) from misrepresentation. Furthermore, in accordance with Restatement Second of Torts §552C, the party who made the misrepresentation of a material fact “for the purpose of inducing the other to act or to refrain from acting in reliance upon it” shall be liable “to the other for pecuniary loss caused to him by his justifiable reliance upon the misrepresentation, even though it is not made fraudulently or negligently.”<sup>102</sup>

Therefore, in preliminary negotiations very often a party wants to mislead (or does mislead) the other party with regard to some relevant facts of the subject matter of the contract. However, to recover damages, the party who is misled has to prove some elements.<sup>103</sup> To have a successful claim the party must prove that there was a “false representation or concealment of a

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<sup>98</sup> Liability based on article 1134 C.CIV. about good faith in contracts which provides: “les conventions légalement formées tiennent lieu de loi à ceux qui les ont faites. Elles ne peuvent être révoquées que de leur consentement mutuel, ou pour les causes que la loi autorise. Elles doivent être exécutées de bonne foi.”

<sup>99</sup> BLACK’S DICTIONARY 1016 (7<sup>TH</sup> ed. 1999)

<sup>100</sup> RESTATEMENT (SECOND) OF CONTRACTS §159.

<sup>101</sup> ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, 550, (Fourth Edition 2001).

<sup>102</sup> RESTATEMENT (SECOND) OF TORTS §552C (1); and also (2) which provides “damages recoverable under the rule stated in this section are limited to the difference between the value of what the other has parted with and the value of what he has received in the transaction.”

<sup>103</sup> See e.g. *Dorris Joni Reed v. Robert J. King*, 193 Cal. Rptr. 130 (1983).

material fact susceptible of knowledge, made with knowledge of its falsity or without sufficient knowledge on the subject to warrant a representation, with the intent to induce the person to whom it is made to act upon it; and such person must act in reliance upon the representation to his damage.”<sup>104</sup> Once all the elements of misrepresentation are met, the contract which has been signed by the parties is voidable according to Restatement Second of Contracts §164(1).<sup>105</sup> Indeed, the court asserts in Carpenter v. Vreeman<sup>106</sup> that “a contract is voidable if a party’s assent is induced by either a fraudulent or a material misrepresentation by the other party, and is an assertion on which the recipient is justified in relying.”<sup>107</sup> The agreement may also be an unconscionable contract as provided by section 2-302 of the Uniform Commercial Code.<sup>108</sup> The situation may be more difficult when no contract has been signed between the parties and they are still in the process of negotiations. Restatement Second of Contracts §163 deals with this particular matter.<sup>109</sup>

The misrepresentation may be fraudulent or “innocent.”<sup>110</sup> A misrepresentation is fraudulent “where the maker knows or believes the assertion to be false and intends to mislead

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<sup>104</sup> *Id.* at 131

<sup>105</sup> RESTATEMENT (SECOND) OF CONTRACTS §164 (1) provides: “if a party’s manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is justified in relying, the contract is voidable by the recipient.” *See also* RESTATEMENT (SECOND) OF CONTRACTS §164 (2).

<sup>106</sup> 409 N.W.2d 258 (Minn. Ct. App. 1987).

<sup>107</sup> *Id.* at 261

<sup>108</sup> UNIFORM COMMERCIAL CODE §2-302 provides that “(1) if the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.” *See Waters v. Min Ltd*, 587 N.E.2d 231 (1992) citing *Industralease Automated & Scientific Equip. Corp. v. R.M.E. Enters., Inc.*, 58 A.D.2d 482 at 488-490 (1977) (in which the court asserts that “high pressure tactics and misrepresentation have been recognized as factors rendering a contract unconscionable.”)

<sup>109</sup> RESTATEMENT (SECOND) OF CONTRACTS §163 “if a misrepresentation as to the character or essential terms of a proposed contract induces conduct that appears to be a manifestation of assent by one who neither knows nor has reasonable opportunity to know of the character or essential terms of the proposed contract, his conduct is not effective as a manifestation of assent.”

<sup>110</sup> MURRAY, MURRAY ON CONTRACTS: MISREPRESENTATION §95, B. FRAUDULENT OR MATERIAL, 538 (Fourth Edition 2001)

the other party.”<sup>111</sup> A misrepresentation is innocent if the party does not know it is false, but he is wrong. In that case, the contract might still be avoided if the innocent misrepresentation was very important, or material. It is material if it would induce the manifest assent by a party.<sup>112</sup> Moreover, a misrepresentation is material if “the maker knows that, because of special reasons, it would be likely to induce a particular party to assent, though it would not induce such assent by a reasonable party.”<sup>113</sup> If the misrepresentation is not fraudulent, therefore to be actionable it must be material.<sup>114</sup> For example, in Gibb v. Citicorp Mortgage, Inc.,<sup>115</sup> deals with misrepresentation by an agent acting for the seller for the purchase of a house that had a termite infestation.<sup>116</sup> In this case, the agent knew about the termites’ infestation and misled the buyer.<sup>117</sup> This is fraudulent misrepresentation.

In French law, the notion of misrepresentation includes both the notion of “*dol*” and “*erreur*.” The first notion, the “*dol*,”<sup>118</sup> is when there is fraudulent misrepresentation. “*L’erreur*” is when a mistake is made by one party but was not intentional.<sup>119</sup> In French law, when there is “*dol*” the plaintiff has to prove that the defendant used some “*manoeuvres*

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<sup>111</sup> *Id.*

<sup>112</sup> See Hampton v. Sabin, 621 P.2d 1202 at 1207 (1980) (citing that “a representation is material if ‘it would be likely to affect the conduct of a reasonable man with reference to a transaction with another person’”) quoting Millikin v. Green, 283 Or. 283 at 285 (1978).

<sup>113</sup> RESTATEMENT (SECOND) OF CONTRACTS §162(2) comment c “a misrepresentation is material if it would be likely to induce a reasonable person to manifest his assent, or if the maker knows that it would be likely to induce the recipient to do so.” “A maker may know of particular idiosyncrasies of the recipient and, while the assertion may not induce a reasonable person to assent, the maker may know that the assertion is likely to induce this person. See also RESTATEMENT (SECOND) OF TORTS §526 (2) (b).

<sup>114</sup> MURRAY, MURRAY ON CONTRACTS: MISREPRESENTATION § 95, B. FRAUDULENT OR MATERIAL, 538 (Fourth Edition 2001)

<sup>115</sup> 518 N.W.2d 910 (1994).

<sup>116</sup> *Id.* at 914

<sup>117</sup> *Id.* at 915

<sup>118</sup> Article 1116 C.CIV “le dol est une cause de nullité de la convention lorsque les manoeuvres pratiquées par l'une des parties sont telles, qu'il est évident que, sans ces manoeuvres, l'autre partie n'aurait pas contracté. Il ne se présume pas, et doit être prouvé.”

<sup>119</sup> Article 1110 C.CIV “l'erreur n'est une cause de nullité de la convention que lorsqu'elle tombe sur la substance même de la chose qui en est l'objet. Elle n'est point une cause de nullité, lorsqu'elle ne tombe que sur la personne avec laquelle on a intention de contracter, à moins que la considération de cette personne ne soit la cause principale de la convention.”



*frauduleuses*<sup>120</sup> with the real and manifest intent to mislead him.<sup>121</sup> The “*dol*” has to be decisive enough to lead the plaintiff to contract with the defendant.<sup>122</sup> Moreover, the seriousness of the “*dol*” shall be appreciated *in concreto*.<sup>123</sup>

Accordingly, a contract affected by either fraudulent misrepresentation or by mistake is void.<sup>124</sup> The parties will be put in the legal situation before the contract was made.<sup>125</sup> However, the victim of fraudulent misrepresentation or mistake may lose his power of avoidance by affirming the contract.

### 3) Duty of care

Duty of care is defined as a duty owed by one to another to take reasonable care not to cause physical, psychiatric or economic loss or harm.<sup>126</sup> This notion is also involved at the negotiation stage. Parties must deal in good faith and fairness. French law imposes some duties of good conduct called “*obligation de loyauté et de bonne foi*” on both of parties, in addition to the duty of care, called “*obligation de vigilance*.”<sup>127</sup> When a party fails its duty of care under French law, its responsibility will be analyzed under tort law.<sup>128</sup> This duty of care can be analyzed as an “*obligation de moyens*,” that is to say, to do everything that is possible to

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<sup>120</sup> Fraudulent skills

<sup>121</sup> See e.g., Cass. req., Feb. 6, 1934; Somm. 1935, I, 296 (when the court asserts that a simple lie is a “*dol*.”)

<sup>122</sup> VALERIE TOULET, DROIT CIVIL, OBLIGATIONS RESPONSABILITE CIVILE, [CIVIL LAW, OBLIGATIONS CIVIL RESPONSABILITY] édition centre de publications universitaire, 1999, 65.

<sup>123</sup> That is to say in the concrete and real situation of the victim that is to say for example his age, his experience and his degree of education.

<sup>124</sup> Article 1117 of C.CIV provides that “la convention contractée par erreur, violence ou dol, n'est point nulle de plein droit ; elle donne seulement lieu à une action en nullité ou en rescision, dans les cas et de la manière expliqués à la section VII du chapitre V du présent titre.”

<sup>125</sup> “Remise des parties en l'état.”

<sup>126</sup> BLACK'S DICTIONARY 523 (7<sup>TH</sup> ED. 1999)

<sup>127</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 105 (Kluwer Law International, 2002).

<sup>128</sup> Article 1382 C.CIV. provides “tout fait quelconque de l'homme, qui cause à autrui un dommage, oblige celui par la faute duquel il est arrivé, à le réparer.” The idea of this provisions is that every act of someone, which cause to someone' else an injury, has the duty to repair it.

perform the contract correctly. Therefore, even if liability in negligence involves the lack and failure to take reasonable care not to cause a foreseeable damage, it is not because one party fails its duty of care (which failure results in damage) that this party will automatically be liable. This party may inflict loss on another by his or her unreasonable conduct, and yet will not be responsible.

In order to prove that one party has failed his duty of care, several requirements have to be met. First, the party's conduct must have been wrongful. This is the element of negligence. The plaintiff has to prove that the defendant has been negligent.<sup>129</sup> Second, he has to prove that the defendant owes him a duty of care and the defendant's conduct fell below the standard of a reasonable person. Third, the damage has to be foreseeable. If not, the defendant has no duty of care. However, in the early stages of preliminary negotiations it is sometimes very difficult to determine whether the damage was foreseeable. Not all damages can be recovered under the duty of care. The consequences are different depending on the type of damage. Damages resulting from negligence during preliminary negotiations between the parties are frequently of economic loss. These kinds of damages are difficult to recover,<sup>130</sup> especially in the scope of economic activity when much risk is involved. Therefore, the existence of the duty of care depends on the nature of the damage resulting from a failure of care.<sup>131</sup> In order to determine the liability of one party to another, courts refer to the reasonable person standard.

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<sup>129</sup> In fact, proving negligence is easier than proving fraud.

<sup>130</sup> See A. J. E. JAFFEY, THE DUTY OF CARE: CHAP. 1 "TESTS AND CONCEPTS", 4 (Edition Dartmouth 1992), when the author cites as an example damages resulting to a failure to confer a benefit. This kind of damage is not actionable in tort "although it may be in contract when the defendant has promised for consideration to provide the benefit."

<sup>131</sup> *Id.* "whether a duty of care exists may depend on the kind of damage which the conduct in question causes. Generally damage is not suffered for the purposes of the law of tort unless as the result of the defendant's conduct the plaintiff's position is made worse than it would otherwise have been."

III- Some procedural problems that can arise when trying to prove misrepresentation or duty to disclose: parol evidence rule and merger clause

A- Effect of Parol Evidence Rule

There are different ways for the parties to a contract to express their assent and intent. They may express their assent in oral or written language or by their acts and conduct.<sup>132</sup> One way to avoid dishonest behavior in the resolution of business disputes is to encourage the parties to put their agreement in writing.<sup>133</sup> This will limit the dispute resolution process to what the written agreement says. This is exactly what the parol evidence rule provides.<sup>134</sup> The parol evidence rule seeks to preserve integrity of written agreements by forbidding contracting parties from attempting to alter their contract through use of contemporaneous oral declarations.<sup>135</sup> Under this rule, when the parties have made an agreement expressed in writing to which both parties intend to be the final, complete and accurate integration of that contract, the agreement cannot be varied or contradicted by evidence, whether parol or otherwise, of any prior written or oral agreement, in the absence of fraud, duress, or mutual mistake.<sup>136</sup> Restatement Second of Contracts §213 dealing with the parol evidence rule<sup>137</sup> indicates the differences between

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<sup>132</sup> MURRAY, MURRAY ON CONTRACTS, THE PAROL EVIDENCE RULE – “INCONSISTENT” AND “CONTRADICTION” – FORM OF WRITING – THE MEANING OF “INTEGRATION” §83 A. THE POSSIBLE INTENTION OF THE PARTIES, 431 (Fourth Edition 2001).

<sup>133</sup> LAWRENCE M. SOLAN, SYMPOSIUM: THEORY INFORMS BUSINESS PRACTICE: THE WRITTEN CONTRACT AS SAFE HARBOR FOR DISHONEST CONDUCT, 77 Chi.-Kent. L. Rev. 87, 2001.

<sup>134</sup> *Id.*

<sup>135</sup> See BLACK’S DICTIONARY 1117 (7<sup>th</sup> ed. 1999); See HELEN HADJIYANNAKIS, THE PAROL EVIDENCE RULE AND IMPLIED TERMS: THE SOUNDS OF SILENCE, 54 Fordham L. Rev. 35, 36 (1985) and UNIFORM COMMERCIAL CODE § 2-202, 2A-202 for some current revisions of the rule, which provides that “if the parties assent to a writing as the final and complete expression of the terms of their agreement, evidence of prior or contemporaneous agreements may not be admitted to contradict, vary, or add to the terms of the writing.”

<sup>136</sup> See Harrison v. Fred S. James, P.A., Inc., 558 F. Supp. 438 (1983) (citing Scott v. Bryn Mawr Arms, 312 A.2d 592 at 594 (1973) “unless fraud, accident or mistake is averred, the writing constitutes the agreement between the parties, and its terms cannot be added to nor subtracted from by parol evidence.”) See also 3 CORBIN ON CONTRACTS §573 (1960).

<sup>137</sup> RESTATEMENT (SECOND) OF CONTRACTS §213 comment a “it is not a rule of evidence but a rule of substantive law. Nor is it a rule of interpretation; it defines the subject matter of interpretation. It renders inoperative prior written agreements as well as prior oral agreements...”

integrated agreements and completely integrated agreements.<sup>138</sup> The question before a court remains the same, that is to say, whether the parties intended their writing to be their final and complete expression.<sup>139</sup> When the parties agree that their sole writing will generate obligations and be the only one which contains a complete statement of their undertakings, they show their intention to not be bound by any other contemporaneous oral agreements.<sup>140</sup> Moreover, any antecedent understandings and negotiations will not be admitted if they contradict or vary the written agreement,<sup>141</sup> but it is always possible to admit evidence of prior negotiations in case of mistake.<sup>142</sup>

According to section 2-202 of the U.C.C., although it is not possible to contradict a complete and final writing between the parties, it can be supplemented by some evidence of course of performance, course of dealings and by any additional terms unless the court finds that the writing had been intended as an exclusive statement of the terms of the agreement.<sup>143</sup> In some

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<sup>138</sup> RESTATEMENT (SECOND) OF CONTRACTS §213 which provides that “(1) a binding integrated agreement discharges prior agreements to the extent that it is inconsistent with them, (2) A binding completely integrated agreement discharges prior agreements to the extent that they are within its scope, (3) An integrated agreement that is not binding or that is voidable and avoided does not discharge a prior agreement. But an integrated agreement, even though not binding, may be effective to render inoperative a term which would have been part of the agreement if it had not been integrated.”

<sup>139</sup> See e.g. *Masterson v. Sine*, 68 Cal. 2d 222, 65 Cal. Rptr. 545, 436 P.2d 561 (1968).

<sup>140</sup> See e.g. *Mitchill v. Lath*, 247 N.Y. 377 (1928) in which the question before the court is whether an oral agreement shall be enforced when there is a complete written contract between the parties. See *O’Malley v. Grady*, 109 N.E. 829 (1915) in which the court asserted that the parol evidence rule “is more than a rule of evidence, and oral testimony, even if admitted, will not control the written contract; *Brady v. Nally*, 45 N.E. 547 (1896).

<sup>141</sup> *Id.* at 381

<sup>142</sup> *Phillips Gas and Oil Co. v. Kline*, 84 A.2d 301 (1951) at 302-303 “where no fraud, accident or mistake is averred and proved, and the alleged prior or contemporaneous oral representation or agreement concerns a subject which is specifically dealt with in the written contract, the law is clearly and well settled that the alleged oral representation or agreement is merged in or superseded by the subsequent written contract and cannot vary, modify or supersede the written contract;” “and hence parol evidence thereof is inadmissible in evidence” citing *Grubb v. Rockey*, 79 A.2d 255 (1951); *Walker v. Saricks*, 63 A.2d 9 (1949); *Gianni v. Russell & Co., Inc.*, 126 A. 791 (1924); *Speier v. Michelson*, 154 A. 127 (1931); *O’Brien v. O’Brien*, 66 A.2d 309 (1949); *Russell v. Sickles*, 160 A. 610 (1932).

<sup>143</sup> UNIFORM COMMERCIAL CODE §2-202 “(1) Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement by may be explained or supplemented (a) by course of performance, course of dealing, usage of trade (section 1-303); and (b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.”

cases, the contract written by the parties is not clear enough and needs more details to determine the real intention of the parties. This is the reason why the Uniform Commercial Code permits the parties to bring in any evidence of their course of dealing, course of performance, and trade usage.<sup>144</sup> The real intention and understanding of the parties has to be known.<sup>145</sup> In fact, a court will have to look first to the contract and whether it is the complete and final expression of the parties.<sup>146</sup> Indeed, the question of whether further evidences will be allowed in the future will depend upon the terms of the agreement.

Three possibilities can be distinguished.<sup>147</sup> The first possibility is when the parties do not intend their written agreement to preclude evidence of any documents or expression related to their agreement. This possibility is unlikely because it does not prevent a party from resurrecting evidence contrary to their agreement.<sup>148</sup> However, when prior evidence contradicts the terms of the writing, this evidence would not be operative if it is the apparent intention of the parties.

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<sup>144</sup> *Id.* UNIFORM COMMERCIAL CODE §2-202 official comment 2 which explain that “paragraph (a) makes admissible evidence of course of dealing, usage of trade and course of performance to explain or supplement the terms of any writing stating the agreement of the parties in order that the true understanding of the parties as to the agreement may be reached. Such writings are to be read on the assumption that the course of prior dealings between the parties and the usages of trade were taken for granted when the document was phrased. Unless carefully negated they have become an element of the meaning of the words used. Similarly, the course of actual performance by the parties is considered the best indication of what they intended the writing to mean.”

<sup>145</sup> In order to do so, courts will analyze the intention of the parties by applying the “appearance” test. By such a test, courts will ask the question of whether the parties intend their writing to be a final (partially integrated) or a complete and exclusive (fully integrated) agreement.

<sup>146</sup> *See* MURRAY, MURRAY ON CONTRACTS: §84. 3. THE NATURAL INCLUSION TEST – WILLISTON/CORBIN – GIANNI V. RUSSEL – MITCHILL V. LATH – MASTERSON V. SINE, 442, (Fourth Edition 2001) citing 3 CORBIN § 582 at 457 (1963 ed.) “the Corbin position is simple: either the parties assented to the writing as an integrated agreement or they did not, and all ‘respectable’ evidence should be considered to determine this critical question. This position is completely consistent with the basic Corbin view that courts must determine whether the parties have agreed today to nullify their agreement of yesterday and that there is no need to call upon some ‘parol evidence rule’ to prove that intention.”

<sup>147</sup> MURRAY, MURRAY ON CONTRACTS: §83 THE PAROL EVIDENCE RULE – “INCONSISTENT” AND “CONTRADICTORY” – FORM OF WRITING – THE MEANING OF “INTEGRATION” A. THE POSSIBLE INTENTION OF THE PARTIES, 431, (Fourth Edition 2001).

<sup>148</sup> *Id.* MURRAY wrote that “if the parties have taken the time and trouble to express themselves in writing, certainly evidence of prior contradictory agreements appear less credible than the subsequent written agreement. Assuming prior agreement was made, if the parties later executed a written agreement containing contradictory terms, the later expression of agreement should prevail on the rudimentary principle of contract law that the parties may always agree today to rescind or modify their agreement of yesterday.”

Such contradictory terms are characterized as “inconsistent” with the terms of the final writing.<sup>149</sup>

The second scenario is when the parties understand that their written contract is final as to any matters included in the writing, but the parties do not exclude any other manifestations of agreement not contained in the document by which they declare to be bound. This case occurs in the preliminary negotiations when the parties sign a final written contract but also agree to admit any kind of writings (related to their negotiation and to their written agreement) which occurred during the negotiation process. However, such a case does not protect a party from any documents that he did not expressly agree on or did not know about.

In the third and final category, the parties protect themselves by preventing any written or oral declarations to reappear, and to do so they make clear that their writing is to be the final, complete and exclusive manifestation of their agreement.<sup>150</sup> In such a case, they express their intention to be bound only by this agreement. Then, evidence of any anterior agreements (whether consistent or not) would be automatically excluded whereas in the second category only inconsistent terms will be inoperative. In addition, parties can express their intent by including a merger clause in their agreement. This clause will provide that the parties intended their writing to be their final and complete intention. This is discussed in the next section.

The second and third categories, the parties intended their writing to be final (second possibility) or complete (third possibility) as to any particular matters including in their writing. By such an expression a court will know the intent of the parties and will give an appropriate

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<sup>149</sup> See *Hunt Foods & Industries, Inc. v. Doliner*, 270 N.Y.S.2d 937 at 940 (1966) which give the definition of the term “inconsistent”: “to be inconsistent, the term must contradict or negate a term of the writing.”

<sup>150</sup> In *Masterson*, 65 Cal. Rptr. 545 at 547 (1968) the court indicates that because the issue is whether there has been an integration and whether the parties intended their writing to serve as the exclusive embodiment of their agreement, therefore the first thing to look at is the writing. It can states that “there are no previous understandings or agreements not contained in the writing, and thus express the parties’ intention to nullify antecedent understandings or agreements.” the court cites 3 CORBIN, CONTRACTS (1960) §578, 411.

interpretation. Here again, the intention of the parties remains crucial. Courts will scrutinize whether the parties intended their writing to be both complete and final.<sup>151</sup> In such a case, according to Restatement Second of Contracts §228<sup>152</sup> the writing is “fully integrated”<sup>153</sup> and cannot support any evidence of prior understandings.<sup>154</sup> If the writing is only final, but not complete, it is said to be “partially integrated.” Then, it supports evidence of prior or contemporaneous agreements if these do not contradict the terms of the final writing.<sup>155</sup>

Courts will sometimes focus on whether the writing contains a merger clause by which the parties express their agreement as unique and fully integrated.<sup>156</sup> Although it shows the intention of the parties to have their writing as fully integrated, such a clause does not always prevent one party to show evidence to the contrary.<sup>157</sup>

## B- Effect of Merger Clause

The parties may want to include a merger clause, sometimes called an “integration” or “zipper” clause, in their contract. This is a good way to be sure that every single element of their

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<sup>151</sup> See MURRAY, MURRAY ON CONTRACTS: §83 THE PAROL EVIDENCE RULE – “INCONSISTENT” AND “CONTRADICTION” – FORM OF WRITING – THE MEANING OF “INTEGRATION”. D. THE MEANING OF “INTEGRATED” – “FULLY” OR “PARTIALLY” INTEGRATED, 433 (Fourth Edition 2001), in which the author explains that the courts have to “focus on the threshold question in the application of the parol evidence rule: Did the parties intend their writing to be final at least as to the matters expressed therein, or did they intend their writing to be both final and complete so that no prior expression of agreement of any kind will be operative?”

<sup>152</sup> See RESTATEMENT (SECOND) OF CONTRACTS §228 which provides that “an agreement is integrated where the parties thereto adopt a writing or writings as the final and complete expression of the agreement.” See also 3 CORBIN ON CONTRACTS §581 at 441-42 (1960) “the parol evidence rule does not itself purport to establish the fact of “integration”; and until that fact is established the “rule” does not purport to have any legal operation.”

<sup>153</sup> See RESTATEMENT (FIRST) §237 comment b. “an integration by definition contains what the parties agreed upon as a complete statement of their promises.”

<sup>154</sup> See *South Side Plumbing Co. v. Tigges*, 525 S.W.2d 583 at 588 (Mo. Ct. App. 1975) (the court indicates that “evidence of prior or contemporaneous agreements that varies or contradicts the terms of a written instrument is not admissible absent fraud, accident, or mistake. But the rule is applicable only where the instrument is a complete integration of the parties' agreement and is unambiguous. Where the agreement provides that the document plus any additional documents identified thereunder shall comprise the entire agreement among the parties thereto, it is the intention of the parties on the face of the agreement to create a complete and integrated contract.”)

<sup>155</sup> *Merk v. Jewel Food Stores Div. of Jewel Cos.*, 945 F.2d 889 at 893 (7<sup>th</sup> Cir. 1991), cert. denied, 504 U.S. 914, 112 S. Ct., 1951, 118 L. Ed. 2d 555 (1992); *Intercorp., Inc. v. Pennzoil Co.*, 877 F.2d 1524 at 1528 (11<sup>th</sup> Cir. 1989).

<sup>156</sup> *Union Bank v. Swenson*, 707 P.2d 663 (Utah 1985).

<sup>157</sup> *Id.* at 665

negotiations will be included in their written agreement. A merger clause provides that in the absence of mistake or fraud, a written contract merges all prior and contemporaneous negotiations in reference to the same subject, and the whole engagement of the parties and the extent and manner of their undertaking are embraced in the writing.<sup>158</sup> According to the court in Gerdlund v. Electronic Dispensers Int'l,<sup>159</sup> a merger clause has to reflect the parties' intention that their written agreement was intended to be final and complete.<sup>160</sup> By such a clause the parties state that their writing is the unique and exclusive agreement. They will be bound only by this unique contract, and all agreements which are not cited in their contract (such as preliminary documents written during the period of negotiations) are not taken into account. For example, in Betz Labs v. Hines,<sup>161</sup> the parties included a merger clause in their contract stating that the writing constituted the unique agreement between the parties, and they did not intend to be bound by any other agreement, understanding, representation, obligation or negotiation either oral or written of whatsoever kind or nature.<sup>162</sup>

Such a merger clause should have legal effect because it reflects the intention of the parties. The court in ARB, Inc. v. E-Systems, Inc.<sup>163</sup> asserts that "integration clauses, although not 'absolutely conclusive,' are indicative of the intention of the parties to finalize their complete understanding in the written contract that there was no other prior or contemporaneous agreement not included in the written contract."<sup>164</sup> By such a clause the parties are making "the

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<sup>158</sup> MURRAY, MURRAY ON CONTRACTS: §83 THE PAROL EVIDENCE RULE – "INCONSISTENT" AND "CONTRADICTORY" – FORM OF WRITING – THE MEANING OF "INTEGRATION". A. THE POSSIBLE INTENTION OF THE PARTIES, 431-432 (Fourth Edition 2001).

<sup>159</sup> 235 Cal. Rptr. 279 (6<sup>th</sup> Dist. 1987)

<sup>160</sup> *Id.* at 282 referring to *Masterson*, 65 Cal. Rptr. 545, "that such a clause while it certainly helps to resolve the issue, does not itself establish an integration; the collateral agreement itself must be examined in order to determine whether the parties intended it to be a part of their bargain."

<sup>161</sup> *Betz Labs v. Hines*, 647 F.2d 402 (3d Cir. 1981).

<sup>162</sup> *Id.* at 403

<sup>163</sup> 663 F.2d 189 (1980)

<sup>164</sup> *Id.* citing also *Pumphrey v. Kehoe*, 276 A.2d 194 at 199 (1971).



document a complete integration.”<sup>165</sup> However, the merger clause will not be given effect if the writing is too incomplete or there is either fraud or mistake.<sup>166</sup> Indeed, merger clauses create a strong presumption that the writing represents the final agreement between the parties. To rebut this presumption and invalidate the merger clause as a result, the injured party must establish the existence of fraud, bad faith, unconscionability, negligent omission or mistake in fact.<sup>167</sup> Further, to determine the intention of the parties a court can refer to the circumstances surrounding the making of the agreement.<sup>168</sup>

Further, it seems that courts tend to enforce merger clauses when they are the result of negotiations between the parties, whereas they do not tend to enforce printed merger clauses in standardized agreements. The reason is obvious: printed clauses in standardized agreements are given to not only one person but several. Thus, such a clause is not the ultimate result of negotiation between the parties. Then there is no reason to give an enforceable effect to a merger clause which was not the subject of dealings between the parties. For example, in Eberhardt v. Comerica Bank,<sup>169</sup> a case where a standardized agreement included a printed merger clause, the court indicated that merger clauses are not given conclusive effects in cases when the parties’

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<sup>165</sup> A. CORBIN, CORBIN IN CONTRACTS §578 (1960).

<sup>166</sup> See MURRAY, MURRAY ON CONTRACTS, §84 THE PAROL EVIDENCE PROCESS – TESTS, 2. MERGER CLAUSE TEST, 439, (Fourth Edition 2001) citing “Professors Cobin and Williston suggest that such a merger clause should have conclusive effect in determining an integration unless the writing was obviously incomplete, the clause was inserted as a result of fraud or mistake, or there are grounds to set aside the contract.”

<sup>167</sup> See *Smith v. Central Soya of Athens, Inc.*, 604 F. Supp. 518 (1985); *Neal v. Marrone*, 79 S.E.2d 239 at 242 (1953); *A & A Discount Center v. Sawyer*, 219 S.E. 2d at 534-535 (1975).

<sup>168</sup> *Shoreham Developers, Inc. v. Randolph Hills, Inc.*, 235 A.2d 735 at 739 (1967) “Maryland law further requires... that the circumstances surrounding the making of the contract be considered to discover whether the integration clause in question does, in fact, express the genuine intention of the parties to make the written contract the complete and exclusive statement of their agreement.” See *Rinaudo v. Bloom*, 120 A.2d 184 at 190 (1956); See RESTATEMENT (SECOND) OF CONTRACTS §212 about interpretation of integrated agreement and comment c which suggests that in a case of ambiguity, interpretation should be made in the light of the “relevant evidence of the situation and relations of the parties, the subject matter of the transaction, preliminary negotiations and statements made therein, usages of trade, and the course of dealing between the parties.”

<sup>169</sup> 171 B.R. 239 (E.D. Mich. 1994). The court asserts that “the presence of an integration clause, while often taken as strong evidence of the parties’ intent, is not conclusive in all cases, particularly when the contract is a pre-printed form drawn by a sophisticated seller.”

intent cannot be shown.<sup>170</sup> Moreover, in Zinn v. Walker,<sup>171</sup> the court stated that “when the parties’ conduct indicates their intention to include collateral agreements despite the existence of the merger clause... from the written contract, the parties’ intention should prevail.”<sup>172</sup>

Merger clauses aim to protect against the risk that one party will, honestly or dishonestly, seek to resurrect some proposal that did not show up in the final writing. According to Restatement Second of Contracts §215,<sup>173</sup> if there is any evidence of previous dealings between the parties which contradict a term of the writing, it is not admissible whereas evidence of a consistent additional term is admissible.<sup>174</sup> In contrast, Restatement Second of Contracts §214<sup>175</sup> recommends that any evidence of negotiations and existing agreements should be shown before the final writing. If there is collateral evidence a court may decide not to ignore it because the writing contains a merger clause.<sup>176</sup> In Masterson v. Sine,<sup>177</sup> the court explains that the existence of a merger clause does not of itself establish an integration and that a court should examine the collateral agreement itself to determine whether the parties wanted it to be part of their

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<sup>170</sup> *Id.* at 243. *See also* Sierra Diesel Injection Serv. v. Burroughs Corp., 874 F.2d 653 at 656 (9<sup>th</sup> Cir. 1989).

<sup>171</sup> 361 S.E.2d 314 (1987).

<sup>172</sup> *Id.* at 334. *See also* T. A. Loving Co. v. Latham, 201 S.E.2d 516 (1974).

<sup>173</sup> RESTATEMENT (SECOND) OF CONTRACTS §215 “except as stated in the preceding Section, where there is a binding agreement, either completely or partially integrated, evidence of prior or contemporaneous agreements or negotiations is not admissible in evidence to contradict a term of the writing.” *See* comment a. “a binding integrated agreement discharges inconsistent prior agreements, and evidence of a prior agreement is therefore irrelevant to the rights of the parties when offered to contradict a term of the writing... the earlier agreement, no matter how clear, cannot override a later agreement which supersedes or amends it.”

<sup>174</sup> RESTATEMENT (SECOND) OF CONTRACTS §216 “(1) Evidence of a consistent additional term is admissible to supplement an integrated agreement unless the court finds that the agreement was completely integrated. (2) An agreement is not completely integrated if the writing omits a consistent additional agreed term which is (a) agreed to for separate consideration, or (b) such a term as in the circumstances might naturally be omitted from the writing.”

<sup>175</sup> RESTATEMENT (SECOND) OF CONTRACTS §214 “agreements and negotiations prior to or contemporaneous with the adoption of a writing are admissible in evidence to establish (a) that the writing is or is not an integrated agreement; (b) that the integrated agreement, if any, is completely or partially integrated; (c) the meaning of the writing, whether or not integrated; (d) illegality, fraud, duress, mistake, lack of consideration or other invalidating cause; (e) ground for granting or denying rescission, reformation, specific performance, or other remedy.”

<sup>176</sup> *See e.g.* Gerdlund v. Electronic Dispensers Int’l, 235 Cal. Rptr. 279 at 282 (6<sup>th</sup> Dist. 1987).

<sup>177</sup> 436 P.2d 561 (1968).

bargain.<sup>178</sup> However, some courts give merger clauses conclusive effect absent fraud, mistake, or another reason to set aside the contract.<sup>179</sup> In addition, according to some courts such a clause creates a “rebuttable presumption that the writing is a complete and exclusive statement of the contract terms.”<sup>180</sup> It is important to emphasize that if the contract is void because of fraud, mistake or other reasons invalidating the writing, a merger clause has no legal effect.<sup>181</sup> Restatement Second of Contracts §214(d)<sup>182</sup> provides that evidence of illegality, fraud, duress, mistake, lack of consideration, or other invalidating causes is always admissible and is not barred by the application of the parol evidence rule. Accordingly a party can either prove that there was fraudulent misrepresentation, mistake,<sup>183</sup> or a lack of consideration<sup>184</sup> when the contract was made.<sup>185</sup> In some cases courts will look for extrinsic evidences of a prior agreement even if there is no fraud, mistake or lack of consideration. An example would be when the writing contains a merger clause which states that the writing contained the entire agreement and the court interprets this as meaning that the contract between the parties contains the entire agreement as to “its limited subject matter alone.”<sup>186</sup> Courts usually hold parties to the contract terms when they sign an agreement. But in order to give the strongest protection to them it remains crucial to draft the merger clause carefully.

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<sup>178</sup> *Id.* at 563. See also *Matthews v. Drew Chem. Corp.*, 475 F.2d 146 (5<sup>th</sup> Cir. 1973); *Anderson & Nafziger v. G.T. Newcomb, Inc.*, 595 P.2d 709 (1979).

<sup>179</sup> See *Smith v. Central Soya of Athens, Inc.*, 604 F. Supp. 518 at 526 (E.D.N.C. 1985); *Colafrancesco v. Crown Pontiac-GMC, Inc.*, 485 So. 2d 1131 (Ala. 1986).

<sup>180</sup> *Smith v. Central Soya of Athens, Inc.*, 604 F. Supp. 518 at 526 (E.D.N.C. 1985), “in order to rebut the presumption and, in effect, invalidate the merger clause, a party must offer evidence to establish the existence of fraud, bad faith, unconscionability, negligent omission or mistake in fact.”

<sup>181</sup> See *Betz Labs v. Hines*, 647 F.2d 402 (3d Cir. 1981) (in which the court explains that if the integration (merger) clause is included in the contract and this contract is void because of fraud, mistake, or other invalidated causes, the merger clause is itself struck down.)

<sup>182</sup> RESTATEMENT (SECOND) OF CONTRACTS §214 “agreements and negotiations prior to or contemporaneous with the adoption of a writing are admissible in evidence to establish...illegality, fraud, duress, mistake, lack of consideration, or other invalidating cause.”

<sup>183</sup> *Franklin v. White*, 493 N.E.2d 161 (Ind. 1986).

<sup>184</sup> *City of Warwick v. Boeng Corp.*, 472 A.2d 1214 (R.I. 1984).

<sup>185</sup> *GTE Automatic Elec., Inc. v. Martin’s Inc.*, 512 N.Y.S.2d 107 (1987).

<sup>186</sup> *Gem Corrugated Box Corp. v. National Kraft Container Corp.*, 427 F.2d 499 at 503 (2d Cir. 1970).

## CHAPTER II

### LIABILITY WHEN A PRELIMINARY OR TENTATIVE AGREEMENT IS MADE, BUT A FORMAL AGREEMENT IS CONTEMPLATED (BUT NEVER EXECUTED)

The liability is clear when a party fails to disclose some information or misrepresents some facts. However, the liability when a tentative agreement is made but a formal agreement is never executed is more difficult to establish. Some problems may arise during negotiations. The parties may want to draft a letter of intent to memorize their dealings.

#### I- Preliminary negotiations in general—introduction to problems that can arise during negotiations and things that can go wrong

In both legal systems, the parties have the duty to negotiate in good faith and with fair dealing. In American law, Restatement Second of Contract §205 which deals with the duty of good faith and fair dealing, provides that “every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.”<sup>187</sup> This notion is also defined by the Vienna Convention<sup>188</sup> and by the UNIDROIT Principles which both impose a duty to act in good faith and with fair dealing in international trade.<sup>189</sup> Good faith is a standard connoting

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<sup>187</sup> RESTATEMENT (SECOND) OF CONTRACTS §205

<sup>188</sup> Article 7 (1) United Nations Convention on Contracts for the International Sale of Goods (1980).

<sup>189</sup> UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS, article 1.7(1), and article 2.15 (upon which a party can be held liable for bad faith in negotiations as misrepresenting facts or negotiating without an intention to reach an agreement.)

decency, fairness and reasonableness.<sup>190</sup> The principle of good faith is applied in various contractual contexts which point out the “faithfulness to an agreed common purpose and consistency with the justified expectation to the other party.”<sup>191</sup> The Uniform Commercial Code imposes an obligation of good faith in contracts during both the performance of the contract and its enforcement.

There are actually two definitions of this notion: one is generic<sup>192</sup> and the other one deals with merchants’ transactions.<sup>193</sup> In transactions between merchants the standard of conduct regarding good faith and fair dealing is higher than other transactions.<sup>194</sup>

Even there is no duress, misrepresentation, undue influence or unconscionability, the absence of good faith will permit a court to refuse to enforce all or part of a contract.<sup>195</sup> For example, a court may deem the agreement of the parties inoperative because one of the parties has not performed in good faith or did not conduct the negotiations in good faith.<sup>196</sup> Moreover, it is important to distinguish between the implied duty of good faith and fair dealing in the performance and enforcement of contracts,<sup>197</sup> and the duty to negotiate in good faith that arises from a preliminary letter of intent.<sup>198</sup>

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<sup>190</sup> RESTATEMENT (SECOND) OF CONTRACTS §205, comment a.

<sup>191</sup> *Black Horse Lane Ass., L.P. v. Dow Chem. Corp.*, 228 F.3d 275 at 288 (3d Cir. 2000) (quoting RESTATEMENT (SECOND) § 205, comment a).

<sup>192</sup> UNIFORM COMMERCIAL CODE §1-201(19) in which good faith “means honesty in fact in the conduct or transaction concerned.” UNIFORM COMMERCIAL CODE §1-203 “every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.”

<sup>193</sup> *See* UNIFORM COMMERCIAL CODE §2-103 (1) (b) and UNIFORM COMMERCIAL CODE §2-104 which define good faith as honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.

<sup>194</sup> *Zapatha v. Dairy Mart, Inc.*, 408 N.E.2d 1370 (1980) (in which the court states that “the article 2 definition applicable to merchants includes a higher standard of conduct through the addition of the observance of reasonable commercial standards of fair dealing in the trade.”)

<sup>195</sup> MURRAY, MURRAY ON CONTRACTS: §92 INTRODUCTION – RELATION AMONG CONCEPTS EVIDENCING AN ABUSE OF THE BARGAINING PROCESS, 523 (Fourth Edition 2001).

<sup>196</sup> *Id.*

<sup>197</sup> *Foster Enterprises v. Germania Federal Savings & Loan Asso.*, 421 N.E.2d 1375 at 1380 (1981)

<sup>198</sup> *See* *Channel Home Centers, Div. of Grace Retail Corp. v. Grossman*, 795 F.2d 291 at 299 (1986); *Teachers Insurance and Annuity Association of America v. Tribune Company*, 670 F. Supp. 491 at 498 (1987).

The duty to perform in good faith includes the obligation to use reasonable efforts, whereas the duty to negotiate in good faith is influenced by the terms of the letter of intent.<sup>199</sup> Thus, one duty is imposed by laws whereas the other by a private agreement between the parties. The obligation to negotiate in good faith can be described as preventing one party from “renouncing the deal, abandoning the negotiations, or insisting on conditions that do not conform to the preliminary agreement.”<sup>200</sup>

French statutes make no distinction between the implied duty of good faith and fair dealing in the performance and enforcement of contracts, and the duty to negotiate in good faith stated by a letter of intent. Article 1134 (3) of the French Civil Code provides that conventions have to be performed in good faith.<sup>201</sup> Therefore the parties must deal in good faith. Article 1135 of the French Civil Code adds that the convention leads to all legal suits that equity gives according to the nature of the obligation.<sup>202</sup> French law, like American law, has the requirement of fairness and equity in contracts. However, the French Civil Code does not contain other explicit references to the good faith principle. There are some situations when it is obvious that the duty of good faith applies.<sup>203</sup> French law distinguishes the formation of a contract from the performance of a contract. When the contract is still in the formation process, the parties must deal in good faith and fair dealing. Though the French civil code provides that the parties are free

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<sup>199</sup> A/S Apothekernes Laboratorium for Specialpraeparater v. I.M.C. Chemical Group, Inc. and Dr. M.B. Gills, 873 F.2d 155 (1989). In this case, an action was brought for breach of negotiations to purchase corporate assets. The question here is whether the defendant did breach the duty to negotiate in good faith as imposed by the letter of intent to negotiate sale of corporate assets. The court held that there is no breach of duty to negotiate in good faith because no contract was made between the parties.

<sup>200</sup> *Id.* at 158 citing Teachers Insurance and Annuity Association of America v. Tribune Company, 670 F.Supp. 491 at 498 (1987).

<sup>201</sup> Article 1134 alinéa 3 C.CIV. “les conventions doivent être exécutées de bonne foi.”

<sup>202</sup> Article 1135 C.CIV. “la convention oblige à toutes suites que l’équité donne à l’obligation d’après sa nature.”

<sup>203</sup> See ALBERTO M. MUSY, THE GOOD FAITH PRINCIPLE IN CONTRACT LAW AND THE PRECONTRACTUAL DUTY TO DISCLOSE: A COMPARATIVE ANALYSIS OF NEW DIFFERENCES IN LEGAL CULTURES, December 2000. citing TERRE F, SIMLER R., LAQUETTE Y., DROIT CIVIL – LES OBLIGATIONS, 347, (6e éd., Paris, 1996).

to enter into a contract, they still have to do so in good faith.<sup>204</sup> French courts analyze whether the principle of good faith has been respected by paying close attention to the assent of both parties. Then French courts focus on whether there is a situation of deceit.<sup>205</sup> When the contract is performed, it also has to be in good faith.<sup>206</sup> The parties have several duties, but two of them apply the good faith principle: the duty of loyalty (*devoir de loyauté*)<sup>207</sup> and the duty of cooperation (*devoir de coopération*).<sup>208</sup> The duty of loyalty includes two other duties: the obligation of result (*obligation de résultat*) and the obligation of making reasonable efforts to perform the obligations of the contract (*obligation de moyens*). By the former, one party has to perform a specific obligation. One party will be free of obligations under contract law only when the complete performance of the exact obligation or goal foreseen by the contract between the parties is done.<sup>209</sup> Therefore, a performance which does not reach the foreseen goal is not considered a performance at all. However, the “*obligation de moyens*” is different. In such a case, one party has to accomplish his obligation by acting with due care.<sup>210</sup> The notion of “*obligation de moyens*” is very close to the duty of care in American law. One party will have to act in a “*bon père de famille*,”<sup>211</sup> a notion very close to the reasonable person standard.

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<sup>204</sup> *Id.*

<sup>205</sup> The court will analyze whether there was a misrepresentation or a fraud by one party to the other that will show a lack of good faith. It could be “l’erreur sur la substance or sur la chose” or le “dol.”

<sup>206</sup> *See supra* article 1134 C. CIV.

<sup>207</sup> *See* article ALBERTO M. MUSY, THE GOOD FAITH PRINCIPLE IN CONTRACT LAW AND THE PRECONTRACTUAL DUTY TO DISCLOSE: A COMPARATIVE ANALYSIS OF NEW DIFFERENCES IN LEGAL CULTURES, December 2000, which cites some French cases rendered by the French Superior Court “cour de cassation”: Cass. Civ., April 8, 1987, Bull., III, numéro 88, 53, RTD civ. 1988, 122 note J. Mestre; Cass., juin 5, 1968, D., 1970, 543, note Ph. Jestaz; *See also* statutes about consumer protection article 1244-1 of C. CIV. and article 331-1 CONSUMER CODE.

<sup>208</sup> This kind of duty is related only to certain contracts. *See* Y. PICOD, L’OBLIGATION DE COOPÉRATION DANS L’EXÉCUTION DU CONTRAT [OBLIGATION OF COOPERATION IN PERFORMANCE OF CONTRACT], JCP 1988, I, 3318; TERRÉ F., SIMLER R., LAQUETTE Y., DROIT CIVIL – LES OBLIGATIONS, §416, 350 (6<sup>e</sup> édition, Paris, 1996).

<sup>209</sup> *E.g.* a customer gives his car to a garage mechanic because it has a problem with the brakes. The garage mechanic will be free of obligations when the brakes of the car are completely fixed and are working again.

<sup>210</sup> *E.g.* doctors and lawyers have this “*obligation de moyens*” that is to say to take reasonable care and to do everything it is possible to perform the contract. When a doctor operates on a patient he has to perform the surgery with care and doing everything is currently possible to perform correctly the surgery and reach the foreseen result.

<sup>211</sup> Good father of family

Further, the duty of cooperation implies two different categories, the good faith in contracts and the duty to disclose.<sup>212</sup> Contrary to the American law notion of good faith, French law in both its statutes and case law does not make a clear the distinction between subjective and objective good faith. This is shown particularly in cases involving “*reticence dolosive*” (silent misrepresentation) and “*erreur sur la substance*” (“mistake on the substance”).<sup>213</sup>

Because the negotiation period is a time of risk, the parties may want to draft a preliminary writing that aims to protect them from an eventual unlawful breach by one party. They also may want to clarify their dealings in a document. Here again, it is important to know the intent of each party to determine whether they want to be bound by their preliminary writing. Therefore the law will determine whether these preliminary agreements should be enforced, and, if they are enforced, what the remedies should be in case of a breach by one party.<sup>214</sup>

In defining preliminary negotiations, Restatement Second of Contracts §26 provides that “a manifestation of willingness to enter into a bargain is not an offer if the person to whom it is addressed knows or has reason to know that the person making it does not intend to conclude a bargain until he has made a further manifestation of assent.” Moreover, according to Murray, “preliminary negotiations as to the terms of an agreement do not constitute a contract although this does not preclude the formation of a binding contract during negotiations.”<sup>215</sup> To determine whether the parties intended to be bound by their preliminary agreements, a court will have to seek their respective intentions. A court refers to the express, not the inner intention, of the parties. It seems that the closer the preliminary agreement is to a contract (because this

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<sup>212</sup> These contracts include the “*contrat de société*” (corporation contract), “*contrat de travail*” (employment contract) and “*contrat d’assurance*” (insurance contract).

<sup>213</sup> GHESTIN J., LA FORMATION [THE FORMATION (OF CONTRACTS)], n.593 ff., 576 (3e edition, Paris, 1993); FABRE-MAGNAN M., DE L’OBLIGATION D’INFORMATION DANS LES CONTRATS. ESSAI D’UNE THÉORIE, L.G.D.J., 1992.

<sup>214</sup> ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, 491 (Fourth Edition 2001).

<sup>215</sup> MURRAY, MURRAY ON CONTRACTS, 61 (Fourth Edition 2001).



preliminary agreement contains all the elements necessary to constitute a contract), the greater chance it has to be recognized as enforceable at law and therefore binding between the parties. Indeed, in a preliminary agreement which is supported by a valid consideration, an agreement of both parties on important elements of the agreement and their mutual intention to contract together shall be recognized as binding. It will be the same result in French law if the preliminary agreement reaches the elements of a valid contract which are defined in article 1101 of the French Civil Code.

The court in Citizens' Committee of North End v. Hampton<sup>216</sup> indicates the importance of acts and conduct of the parties to determine whether there was a contract. There the court had to resolve whether a contract was made between the parties during the negotiation period.<sup>217</sup> The court will also pay attention to the type of document on which the parties indicate that they are bound.<sup>218</sup> Documents as communications between the parties shall not be construed as an agreement.<sup>219</sup> These are only private communications between the parties regulating the scope of preliminary negotiations. The parties usually do not intend to have these types of documents enforceable at law, but, in some cases, courts recognize these documents as binding because they contain all the essential elements necessary to constitute a valid contract.<sup>220</sup> Indeed, in Parkview General Hospital, Inc. v. Eppes,<sup>221</sup> the parties were bound by their communications which constituted an offer and an acceptance.

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<sup>216</sup> 114 A2d 388 (1955)

<sup>217</sup> *Id* at 376. *See* also *Boston Iron Co v. United States*, 118 U.S. 37 (1886)

<sup>218</sup> *See* *Head & Amory v. Providence Ins. Co.*, 6 U.S. 127 at 165 (1884), (which refers to communications "which have been cited [in the case], do not import a contract. They were negotiations preparatory to an agreement, but not an agreement itself.")

<sup>219</sup> *Id.* at 164

<sup>220</sup> *See* *Wussler v. Peterson*, 270 S.W.2d 12 at 15 (1954); *Jackson v. Stearns*, 113 P 30 at 31 (1911) in which the court indicates that letters passing between the parties cannot be read together to constitute a contract for the sale of real estate, if they do not indicate precisely the land which is intended to be the subject matter of the contract, so that parol evidence would be required to substantiate the truth of the matter.

<sup>221</sup> 447 S.W.2d 487 (1969).

On the other hand, in Onyx Oils & Resins, Inc. v. Moss,<sup>222</sup> the court indicated that a preliminary writing or agreement on only some elements of a proposed contract cannot be enforced at law.<sup>223</sup> Moreover, a proposal left open to further negotiation has to be accepted to be binding. However, in Lombardo v. Gasparini Excavating Co.,<sup>224</sup> the court observed that “the parties intended only to enter into a binding agreement sometime in the future. In such a case, the preliminary negotiations do not constitute a contract.”<sup>225</sup> Therefore, the requirement of certainty is important. A binding and enforceable contract has to be certain and clear regarding its elements as well as the nature and extent of its obligations. The parties must agree upon every important part of the dealing.

In an important case, Channel Home Centers v. Grossman,<sup>226</sup> the court states that “it is hornbook law that evidence of preliminary negotiations or an agreement to enter into a binding contract in the future does not alone constitute a contract.”<sup>227</sup> Thus, a contract has to be made to recognize preliminary negotiations as binding between the parties.<sup>228</sup> Moreover, the court asserted that the question of whether there is a contract formed between the parties is one for the trier of fact.<sup>229</sup> The court indicated that for an agreement to be enforceable, the parties should demonstrate that they intend to have their agreement binding. The terms of the agreement have to be definite and clear enough (to avoid ambiguity) and there must be consideration on both

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<sup>222</sup> 80 A.2d 815 (1951).

<sup>223</sup> *Id.* at 817

<sup>224</sup> 123 A.2d 663 (1956).

<sup>225</sup> *Id.* at 666, referring to *Upsal Street Realty Company v. Rubin*, 192 A. 481 (1937); *Berkowitz v. Kass*, 40 A.2d 691 (1945).

<sup>226</sup> 795 F.2d. 291(1986).

<sup>227</sup> *Id.* at 298

<sup>228</sup> *Id.* at 301, the District Court for the Eastern District of Pennsylvania held that the letter of intent did not bind the parties to any obligation and therefore was enforceable because of its lack of consideration. Moreover, the letter of intent was insufficient to satisfy the Pennsylvania Statute of Frauds for leases. The District Court rejected the plaintiff argument that the said letter of intent should be enforced under the promissory estoppel doctrine. However, in the present case, the district court “erroneously concluded that the letter of intent was unenforceable as a matter of law, it makes no factual findings with regard to this critical term.”

<sup>229</sup> *Id.* at 300

sides.<sup>230</sup> To determinate the nature of a preliminary document, the court may refer to some evidence of preliminary negotiations which occurred between the parties.<sup>231</sup> Therefore, a preliminary agreement drafted by the parties has to be scrutinized by the courts to determine its legal nature.

The parties may want to include a condition precedent or “*condition suspensive*”<sup>232</sup> in their contract, by which at its realization the contract will be formed and consequently binding. Both American and French legal systems allow parties to include such a provision in their contracts.<sup>233</sup> By including a condition precedent, the parties protect themselves from a wrongful interpretation of their preliminary writing by a court. It will be a condition precedent to the existence of a contract.<sup>234</sup> Consequently, the parties have agreed that the contract will be enforceable at law and effective when the condition precedent occurs or is performed. Whatever this condition precedent is, the contract will not be operative until the happening of the event (or the performance of something stated in the contract) by one of the parties, both of them, or even

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<sup>230</sup> *Id.* at 298 (this is a test under Pennsylvania law). *See Lombardo v. Gasparini Excavating Co.*, 123 A.2d 663 at 666 (1956); *Linnet v. Hitchcock*, 471 A.2d 537 at 540 (1984). *See* about the requirement of consideration: *Stelmack v. Glen Alden Coal Co.*, 14 A.2d 127 (1940); *Cardamone v. University of Pittsburgh*, 384 A.2d 1228 (1978).

<sup>231</sup> *See Goldman v. McShain*, 247 A.2d 455 (1968) (which raised the issue of whether there is a binding contract between the parties. In this case there are evidences of preliminary negotiations. The intent of the parties has been discussed as well. The statute of Frauds requires a written contract. )

<sup>232</sup> Condition precedent or “*condition suspensive*” is completely different from condition subsequent or “*condition résolutoire*” because in this case the contract is valid and enforceable at its beginning (at the conclusion of the said contract) but when the condition is happening the contract is therefore void and null. This is article 1183 C. CIV provides that “la condition résolutoire est celle qui, lorsqu'elle s'accomplit, opère la révocation de l'obligation, et qui remet les choses au même état que si l'obligation n'avait pas existé. Elle ne suspend point l'exécution de l'obligation; elle oblige seulement le créancier à restituer ce qu'il reçu, dans le cas où l'événement prévu par la condition arrive.”

<sup>233</sup> Article 1181 C. CIV indicates that the obligation under which the condition precedent has been made is the one which depends on the realization of a future event. Article 1181 C. CIV provides that “l'obligation contractée sous une condition suspensive est celle qui dépend ou d'un événement futur et incertain, ou d'un événement actuellement arrivé, mais encore inconnu des parties. Dans le premier cas, l'obligation ne peut être exécutée qu'après l'événement. Dans le second cas, l'obligation a son effet du jour où elle a été contractée.”

<sup>234</sup> *See Atlantic Pacific Oil Co. v. Gas Development Co.*, 69 P.2d 750 (1937); *O' Brien v. Fricke*, 27 N.W.2d 403 (1947); *Toland v. Kaliff* 435 S.W.2d 260 (1968); *Quinn Distributing Co. v. North Hill Bowl, Inc.*, 139 N.W.2d 860 (1966); *Federal Reserve Bank v. Neuse Mfg. Co.*, 196 S.E. 848 (1938).

by a third person.<sup>235</sup> As an example, the parties may wish to reduce their agreement into a certain form of writing. The parties include a condition precedent which states that they will be bound when their agreement will be reduced in writing.

In addition to the condition precedent, the parties may want to include some essential terms in their preliminary agreement or their final contract. Whether the preliminary writing between the parties will be binding depends on the terms included in their contract and the importance given by both of the parties to these terms. Some terms are essential (as the subject matter of the contract, quantity of goods, place of delivery of goods, etc) and others are unessential (where matters will be discussed later on by the parties and are not essential to the agreement). The parties must agree on essential terms of their agreement. They must agree upon the material and necessary details of the bargain.<sup>236</sup> If any essential term is left open for future consideration there is no binding contract. But when the parties agree on the essential terms of their agreement, that is to say, upon the material and necessary details of the bargain, their agreement can constitute an enforceable contract according to the court in several cases even if a later written agreement was contemplated.<sup>237</sup> The court asks to whether the elements (terms) of the contract are certain enough to provide a basis for an appropriate remedy. In Linnet v. Hitchcock,<sup>238</sup> the court assets that “the essential terms of the agreement are too uncertain to permit enforcement of the agreement in favor of either party.”<sup>239</sup> The court held that if “the essential terms of the agreement were so uncertain that there was no basis for determining

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<sup>235</sup> See Federal Reserve Bank v. Neuse Mfg. Co., 196 S.E. 848 (1938); See also Miners’ & Merchants’ Bank v. Gidley, 144 S.E.2d 711 at 715 (1965) (about the making of the promise which can “be conditioned on the act or will of a third person.”)

<sup>236</sup> 123 A.2d 663 (1956).

<sup>237</sup> See Edgcomb v. Clough, 118 A. 610 (1922); Beachler v. Mellon-Stuart Company, 47 A.2d. 147 (1946); and Potter v. Leitenberger Machine Company, 70 A.2d 390 (1950).

<sup>238</sup> 471 A.2d 537 (1984).

<sup>239</sup> *Id.* at 540

whether the agreement was kept or broken, there was no enforceable contract.”<sup>240</sup> The court applies the same rule in Lombardo v. Gasparini Excavating Co.<sup>241</sup> by emphasizing that since the parties intended to conclude an enforceable contract and the essential terms of that agreement were certain enough in the sense that they provided a basis for an appropriate remedy, the agreement was an enforceable contract. However, where a preliminary agreement leaves some important terms to be agreed upon later, it is not an enforceable contract.<sup>242</sup>

In order to determine the scope and extent of their dealings the parties may want to draft an agreement or intent which will reduce the contract to writing or make it more formal. Here again it is a question of intent<sup>243</sup> whether the parties will be bound by their previous dealing, especially by an oral or informal agreement prior to the contemplated contract. The court in United States for the Use and Benefit of Cortolano & Barone, Inc. v. Morano Construction Corp.,<sup>244</sup> indicates that “it is recognized that if the parties intend not to be bound until they have executed a formal document embodying their agreement, they will not be bound until then.”<sup>245</sup> Sometimes the parties may want to include a condition precedent in their preliminary writing which indicates that they will not be bound until they sign a final contract.<sup>246</sup> However, the parties have to be aware of the fact that some obligations may arise from their oral or informal agreement even if they express their intent to be bound only upon the performance of the full and

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<sup>240</sup> *Id.* at 540-541 (the court found that the terms of the agreement between the parties were too uncertain to permit enforcement and accordingly the court allows restitution for benefit conferred under an agreement that was void for indefiniteness.)

<sup>241</sup> 123 A.2d 663 (1956).

<sup>242</sup> *Joseph v. Donover Co.* 261 F2d 812, (1958). For a more concrete example: *see e.g. Gray v. Hager*, 317 S.E.2d 59 (1984), in which a contract of sale was involved. This contract did not state the modality of payment and leaved it for future agreement. Thus it cannot be a valid and enforceable agreement between the parties because of its lacked of essential terms (even if the sale price was fixed).

<sup>243</sup> *Warrior Constitutors, Inc. v. International Union of Operating Engineers*, 383 F2d 700 (1967).

<sup>244</sup> 724 F Supp 88 (1989).

<sup>245</sup> *Id.* at 99

<sup>246</sup> *Culter v. Anderson*, 357 P.2d 76 (1960).

final contract.<sup>247</sup> Thus, it really depends on the intention of the parties whether provisions of informal agreements which are to be incorporated into a written contract constitute a binding contract in themselves.<sup>248</sup>

According to Restatement Second of Contracts §27,<sup>249</sup> besides the intent of the parties, the circumstances surrounding the dealings may show that the agreements and writings are preliminary negotiations. In fact, according to the Restatement, manifestations of assent are necessary to constitute a contract. Indeed, in Kazanjian v. New England Petroleum Corp.,<sup>250</sup> the court indicated that preliminary dealings do not constitute a binding contract.<sup>251</sup> Nevertheless, if the parties orally agree to all the terms and provisions of their contract, and they want to draft their final agreement as soon as possible (which will reflect their previous dealings and therefore include all the terms and provisions stated in the first draft upon which they orally agreed), the oral contract may be enforceable.<sup>252</sup> In addition, the courts in several cases have recognized that when the parties act under their preliminary agreement, it will be considered as binding between them notwithstanding that a formal contract had never been executed.<sup>253</sup>

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<sup>247</sup> *Id.* at 80, the court emphasizes that “Many cases support the general rule that the mere fact that parties to an oral or informal agreement intend that the same shall be reduced to a written or more formal contract will not necessarily prevent present, binding obligations from arising, even though the contemplated written or formal contract is never drawn up and executed. If the agreement is finally assented to by the parties and covers fully and definitely the terms of the contract; or, as some of the cases, in effect, state the rule, the mere intention to reduce an oral or informal agreement to writing, or to a more formal writing, is not of itself sufficient to show that the parties intended that until such formal writing was executed the oral or informal contract should be without binding force.”

<sup>248</sup> See *Bjornson v. Fire Star Mfg. Co.*, 61 N.W.2d 913 at 915 (1953) (in which the court indicates that the circumstances surrounding the preliminary negotiations and dealings of the parties are important in order to not whether there was an intent of the parties to be bound.)

<sup>249</sup> RESTATEMENT (SECOND) OF CONTRACTS: EXISTENCE OF CONTRACT WHEN WRITTEN MEMORIAL IS CONTEMPLATED §27 “Manifestations of assent that are in themselves sufficient to conclude a contract will not be prevented from so operating by the fact that the parties also manifest an intention to prepare and adopt a written memorial thereof; but the circumstances may show that the agreements are preliminary negotiations.”

<sup>250</sup> 480 A.2d 1153 (1984).

<sup>251</sup> *Id.* at 1157

<sup>252</sup> *Id.* at 1157 citing *Skrock v. Caltabiano*, 505 F. Supp. 916 (1981); *Ketchum v. Conneaut Lake Co.*, 163 A. 534 (1933); See also *Springer v. Springer*, 386 A.2d 122 at 124 (1978), *Schermer v. Wilmart*, 127 A. 315 (1925) and *Taylor v. Stanley Co. of America*, 158 A. 157 (1932) (where parties have reached an oral agreement, the fact that they intend to reduce the agreement to writing does not prevent enforcement of the oral agreement.)

<sup>253</sup> *Empson Packing Co. v. Lamb-Davis Lumber Co.*, 191 P 833 (1920).

## II - Letters of Intent

### A- Definition of Letters of Intent

#### 1) Definition and notion

In order to protect themselves during the period of negotiations, the parties can draft a letter of intent which may be recognized as enforceable at law. A letter of intent is used to memorialize a basic agreement and to flush out any potential deal breaking issues early in the negotiating process.<sup>254</sup> This type of document is often used in business transactions in order to focus the parties on open issues, increase efficiency and indicate willingness to negotiate diligently and in good faith.<sup>255</sup>

The difficult question raised by this type of document is whether it constitutes a contract enforceable at law. Indeed, even if the first aim of a letter of intent is to memorialize a basic agreement, it does not indicate that it is binding. The parties can finalize their contractual relation faster than they would have done without drafting a letter of intent. But the question still stands whether or not such pre-contractual writing is a contract.

In international negotiations, the parties should ask themselves which country's law they wish to apply to the transaction. The judge has to resolve the difficult question of choice of law in accordance with his or her own legal system of conflict of laws.<sup>256</sup> In the French legal system, the judge will determine the law applicable to the contract (to resolve the question of whether a contract exists) in accordance with the provisions of the Rome Convention on the Law Applicable to Contractual Obligations of June 19, 1980. The same convention applies to all the members of the European Community. If nothing is stated in the document regarding the

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<sup>254</sup> KATHRYN COCHRANE MURPHY, LETTERS OF INTENT, American Law Bar Association Continuing Legal Education, 2003 (SH008 ALI-ABA 387).

<sup>255</sup> *Id.*

<sup>256</sup> JOHANNA SCHMIDT, LES LETTERS D'INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002.

applicable law,<sup>257</sup> the judge will apply the law of the country where the contract has the most connection.<sup>258</sup> Article 4 of the Rome Convention refers to the principle of proper law in American law.<sup>259</sup> Therefore, in international negotiations, when the parties are dealing within the European borders, the judge will go through all these steps to determine the law of the contract and then, in accordance with this law, decide whether a contract was drafted between the parties.

In the American system, the judge will decide if the letter of intent is binding as a contract in accordance with the definition of the term contract itself, the intent of the parties, and some other relevant elements.

## 2) Distinction from other documents

The question at issue is whether a letter of intent constitutes a valid and enforceable contract at law. In fact, the enforceability of a contract really depends on a lot of factors,<sup>260</sup> and it is interesting to look closer at the definition itself of a contract.

In American law a contract is “an agreement between two or more persons which creates an obligation to do or not to do a particular thing.”<sup>261</sup> A valid contract has to be made by a clear, definite and express offer upon which is made an acceptance to the exact same terms. A contract is supported by a valid consideration.

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<sup>257</sup> *Id.* In the first time the judge will look to the document wrote by the parties and whether there is a provision regarding the applicable law. If it is the case, he will apply the Rome Convention, June 19, 1980, art. 8 of which provides “the existence and validity of a contract, or any term of a contract, shall be determined by the law which would govern it under this Convention if the contract or term were valid.” (“l’existence et la validité du contrat ou d’une disposition de celui-ci sont soumises à la loi qui serait applicable en vertu de la présente convention si le contrat ou la disposition était valable.”)

<sup>258</sup> *Id.* Rome Convention, June 19, 1980, art. 4 provides “the contract shall be governed by the law of the country with which it is the most closely connected.” (“le contrat est régi par la loi du pays avec lequel il présente les liens les plus étroits.”) It can be the nationality of the parties, the place where some goods are (as houses, apartments, etc.), the language of the contract, etc.

<sup>259</sup> *Id.*

<sup>260</sup> See supra Part 2) Legal nature of letter of intent.

<sup>261</sup> BLACK’S DICTIONARY 322 (7<sup>th</sup> ed. 1999)



A letter of intent is by itself not a contract at all. In fact, a letter of intent is not supported by any consideration except maybe to negotiate or to conclude the contract in a short period of time. It would be a hard task to prove that the letter of intent is supported by a valid consideration. In addition, according to Restatement Second of Contracts §71, a consideration can be an act “other than a promise.”<sup>262</sup> A letter of intent also may include an offer and an acceptance. But because the parties are still negotiating, any agreement is not yet final. The terms upon which they agree can be discussed again further.

French law defines a contract as a promise to do or not to do something.<sup>263</sup> It also says that a promise will be enforced or at least recognized in some way.<sup>264</sup> Therefore, a contract is an enforceable document. It reveals the intention of both parties to be bound by such an agreement. French law is a system where the subjective will of the parties is very important and comes first in deciding whether there is a contract.<sup>265</sup> Thus, a letter of intent may be considered as a contract in the sense that the parties are bound by it if the parties intended to be. The parties have the liberty to contract but they also have the choice not to contract. The intent of the parties has to be shown. Otherwise, the parties could be considered as bound by their writing (formalized into a letter of intent) even if they did not intend to be. In both legal systems, because of this thin line between contract and letter of intent, the courts have the difficult task to determine whether there is an enforceable contract between the parties.

There is another kind of document that is distinguishable from a letter of intent (and contract also), a memorandum of understanding. A memorandum is not a binding contract, so it

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<sup>262</sup> RESTATEMENT (SECOND) OF CONTRACTS § 71 “(3) the performance may consist of (a) an act other than a promise.” It can be understood that a consideration can be either a performance or a promise.

<sup>263</sup> Article 1101 C.CIV “Le contrat est une convention par laquelle une ou plusieurs personnes s'obligent, envers une ou plusieurs autres, à donner, à faire ou à ne pas faire quelque chose.”

<sup>264</sup> JOHANNA SCHMIDT, LES LETTERS D'INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002.

<sup>265</sup> *Id.* “In the “Romano-Germanic” systems the “consensual” point of view prevails: the parties’ intention to be bound is the necessary but also the sufficient condition of existence of a contract.”

differs from a letter of intent which can be recognized as binding. A memorandum is a less formal document which shows that the minds of the parties have not met. This writing does not express a completed agreement, but states terms which, if accepted, would be the foundation of a contract. It is a document used to summarize the legal situation of the parties when they are still negotiating.

The question is how the parties can be sure that their letter of intent will not be considered as binding by a jurisdiction when they do not want it to have legal force. Thus the legal nature of letter of intent has to be analyzed.

#### A- Legal nature of Letter of Intent

##### 1) *Duty to negotiate in good faith and with fair dealing*

Before analyzing in depth the behavior of the parties in order to recognize whether the letter of intent is binding, it is necessary to point out that the parties have a duty to negotiate in good faith and conduct the negotiations with fairness.

The letter of intent can include some condition such as the parties having to make a reasonable effort to negotiate in good faith in order to finalize the transaction. Moreover, the parties can indicate in their writing that they have a duty to negotiate with each other. For example, in Feldman v. Allegheny International, Inc.,<sup>266</sup> the seller was bound to negotiate exclusively with the buyer until they disagreed.<sup>267</sup> However it is important to bear in mind that in such a case “the letter of intent is merely an agreement to negotiate, not a promise that those

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<sup>266</sup> 850 F.2d 1217 (1988).

<sup>267</sup> *Id.* at 1219-1221, the provision in the letter of intent provided that the seller would not “hold discussions or negotiate with any person other than Fedman Associate [the potential buyer]...while the proposed acquisition was being pursued”.

negotiations would be fruitful.”<sup>268</sup> The parties have to determine the scope of their obligations in their letter of intent. In addition, in A/S Apothekernes Laboratorium v. I.M.C. Chem.,<sup>269</sup> the court asserted that the extent of any obligation to deal in good faith and fair dealing can only be analyzed and determined from the structure of the letter of intent written by the parties.<sup>270</sup>

Under the duty to negotiate in good faith, the parties cannot vary from the content of the letter of intent.<sup>271</sup> In Channel Home Centers, Grace Retail v. Grossman,<sup>272</sup> an action was brought for breach of contract to negotiate in good faith. The United States District Court for the Eastern District of Pennsylvania held that the letter of intent was not an enforceable contract because it did not bind the parties to any obligations, it was unenforceable for lack of consideration, and finally, because it was insufficient to satisfy the requirement of the Pennsylvania Statute of Frauds for leases.<sup>273</sup> The plaintiff appealed and won the case.<sup>274</sup> The Court of Appeals held that the letter of intent imposed a duty to negotiate in good faith for reasonable and certain periods of time.<sup>275</sup> The court referred to the intent of the parties.<sup>276</sup>

In several cases, courts held that there are two different kinds of agreements: agreements to agree, which do not constitute a closed proposition, and agreements to negotiate in good faith,

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<sup>268</sup> *Id.* at 1223.

<sup>269</sup> 678 F. Supp. 193 (1988)

<sup>270</sup> *Id.* at 195

<sup>271</sup> See THOMAS C. HOMBURGER AND JAMES R. SCHUELLER, LETTER OF INTENT – A TRAP FOR THE UNWARY 37 REAL PROP. PROB. & TR. J. 509, 511 (2002).

<sup>272</sup> 795 F.2d 291 (1986).

<sup>273</sup> *Id.* at 297

<sup>274</sup> *Id.* at 293-301

<sup>275</sup> *Id.* at 292

<sup>276</sup> *Id.* at 298, the court used the test for enforceability of an agreement under Pennsylvania law which is 1) whether “both parties have manifested an intention to be bound by its terms,” 2) whether the terms are “sufficiently definite to be specifically enforced,” 3) whether the letter of intent is supported by a consideration on both sides.” See also *Lombardo v. Gasparini Excavating Co.*, 123 A.2 663 at 666 (1956); *Linnet v. Hitchcock*, 471 A.2d 537 at 540 (1984); *Stelmack v. Glen Alden Coal Co.*, 14 A.2d 127 (1940); *Cardamone v. University of Pittsburgh*, 384 A.2d 1228 (1978).

which are closed propositions that are “discrete and actionable.”<sup>277</sup> These two agreements thus have to be distinguished because their effects are not the same.

Furthermore, Restatement Second of Contracts §205 provides that “every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.”<sup>278</sup> It implies that the parties have to negotiate in good faith and with fair dealing in order to reach a final contract. When the parties are bound to a letter of intent which indicates their duty to negotiate in good faith, there is always the possibility that one of them does not want to continue dealing with the other and then wants to terminate the contract.<sup>279</sup> It should be possible for one party to get out of the contract or pre-contract under the principle of freedom of contract. Nevertheless, a party bound by the obligation to continue negotiations in good faith cannot withdraw the contract at will. If he does so, the injured party will be able to sue him under breach of contract to negotiate in good faith and ask for damages. However, in such a case, only restitution or reliance damages can usually be awarded but not expectancy damages. Restitution damages will include the out-of-pocket expenses like lawyer’s fees and due diligence costs.<sup>280</sup>

Courts will scrutinize the letter of intent in question to determine whether it creates a duty to negotiate in good faith. If there is no express duty to negotiate in good faith, the document may impose implied obligations upon the parties, especially of course the duty to negotiate in good faith. If it is not the case, the document shall be considered as a memorandum which aims

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<sup>277</sup> See *Reprosystem, B.V. v. SCM Corp.*, 727 F.2d 257 at 264 (1984); *Chase v. Consolidated Foods Corp.*, 744 F.2d 566 at 571 (1984); *Arnold Palmer Golf Co. v. Fuqua Industries Inc.*, 541 F.2d 584 (1976); *Itek Corp. v. Chicago Aerial Industries, Inc.*, 248 A.2d 625 (1968).

<sup>278</sup> See *Baker v. Lafayette College*, 504 A.2d 247 at 255 (1986); *Germantown Manufacturing Co. v. Rawlinson*, 491 A.2d 138 at 148 (1985).

<sup>279</sup> KATHRYN COCHRANE MURPHY, *LETTERS OF INTENT*, American Law Bar Association Continuing Legal Education, 2003 (SH008 ALI-ABA 387).

<sup>280</sup> Y. DAVID SCHARF, “PRE-AGREEMENT LETTER OF INTENT; BEWARE, IT MAY BE ENFORCEABLE”, N.Y.L.J., at 53 (March 25, 2002).

to memorialize the state of ongoing negotiations.<sup>281</sup> Therefore, the parties have to pay close attention to the words in their letter of intent, to the circumstances surrounding the conclusion of this writing, and to the acts by the parties after the conclusion of the letter of intent.

## 2) Behavior of parties: words and acts

### a- Situations in which the Letter of Intent is recognized as binding

First of all, it is important to know the intent of the parties and whether they desired their letter of intent to be a binding writing. In American law, the most important remaining issue is whether the parties have manifested their intent to contract and to be bound by this agreement. Sometimes courts will recognize a letter of intent as a binding document if the parties have expressed their willingness to be bound, and the writing is sufficient to be binding (that is, if the parties agreed on all the essential terms of the contract and it is supported by a valid consideration). In Quake Construction, Inc. v. American Airlines,<sup>282</sup> the court specifies that a letter of intent will not be enforceable unless the parties really intend for it to be a legally binding writing.<sup>283</sup> Thus, courts have to know the express intent, that is to say, the outward expression, of the parties.<sup>284</sup> To do so, courts will refer to the terms of the letter of intent. For example, a letter of intent might include a provision such as, “[this letter of intent] is a legal document that creates binding obligations. If not understood, consult an attorney.” This is considered as a binding contract by the effects of this provision.<sup>285</sup> That is the reason why the parties have to pay close attention to the words stated in their document.

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<sup>281</sup> KATHRYN COCHRANE MURPHY, LETTERS OF INTENT, American Law Bar Association Continuing Legal Education, 2003 (SH008 ALI-ABA 387).

<sup>282</sup> 565 N.E. 2d 990 (1990).

<sup>283</sup> *Id.* at 994

<sup>284</sup> See *Cooper Realty Co. v. United States*, 36 Fed. Cl. 284 (1996) (stated that “when seeking to resolve a question of contract interpretation, the court's primary goal is to ascertain the intent of the contracting parties.”)

<sup>285</sup> *McCarthy v. Tobin*, 690 N.E. 2d 460 at 276 (Mass. App. Ct. 1998).

The parties should avoid any ambiguity in their document. Courts will analyze whether the language of a purported contract is ambiguous as to the parties' intent. If no ambiguity exists in the writing, the parties' intent must be derived solely from the writing itself. If the terms of an alleged contract are ambiguous or capable of more than one interpretation, however, parol evidence is admissible to ascertain the parties' intent. Furthermore, the interpretation of the language is not a question of law but a question of fact if the language of an alleged contract is ambiguous regarding the parties' intent.<sup>286</sup> Indeed, in McCarthy v. Tobin<sup>287</sup> the court asserted that the parties have to be careful that the preliminary agreement include language indicating whether or not it will be considered binding.<sup>288</sup> In *Quake*, on appeal, the court analyzed the intent of the parties and found that the letter of intent was ambiguous regarding the intent of the parties to be bound. The court reasoned that “although the letter of intent included detailed terms of the agreement, the letter also referred several times to the execution of a formal agreement, thus indicating that the intent was not to be bound by the letter.”<sup>289</sup> It seems that a letter of intent is a binding writing between the parties when there is a meeting of minds of the parties, that is to say they agreed upon the same terms of the letter of intent. In addition, a binding letter of intent must be supported by sufficient consideration and fully executed (signed, delivered and accepted by the parties).<sup>290</sup> Moreover, in *Quake*, the court asserted that a letter of intent is not a binding

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<sup>286</sup> See e.g. *W & F Bldg. Maint. Co. v. United States*, 56 Fed. Cl. 62 (2003); *Huna Totem Corp. v. United States*, 35 Fed. Cl. 603 (1996); *Nicholson v. United States*, 29 Fed. Cl. 180 (1993); *Jamsar, Inc. v. United States*, 194 Ct. Cl. 819 (1971); *GPA-I, L.P. v. United States*, 46 Fed. Cl. 762 (2000); *P.R. Burke Corp. v. United States*, 47 Fed. Cl. 340 (2000); *Monarch Painting Corp. v. United States*, 16 Cl. Ct. 280 (1989); *Cooper Realty Co. v. United States*, 36 Fed. Cl. 284 (1996).

<sup>287</sup> 690 N.E. 2d 460 (Mass. App. Ct. 1998).

<sup>288</sup> *Id.* at 278

<sup>289</sup> *Quake*, 565 N.E. 2d 990 (1990).

<sup>290</sup> Article KATHRYN COCHRANE MURPHY, LETTERS OF INTENT, American Law Bar Association Continuing Legal Education, 2003 (SH008 ALI-ABA 387) citing article THOMAS C. HOMBURGER AND JAMES R. SCHUELLER, LETTERS OF INTENT – A TRAP FOR THE UNWARY, 37 REAL PROP. Prob. & TR. J. 509, 511 (2002).

agreement if execution of a formal agreement is listed as a condition precedent to enforcement.<sup>291</sup>

In French law, it is quite similar to American law regarding the legal regime of letters of intent. French courts look at the intent of the parties. According to the rules of French contract law, a proposal may become the basis of a contractual obligation only if the clear, express and firm intention of the parties is shown.<sup>292</sup> Indeed, the parties must give willing assent. One cannot force another to contract. However some difficulties can arise when a party expresses just a vague intention to contract, especially the possibility to accept the agreement. Courts will refer to the outward intention of the parties. In some cases, this intention could be hard to find because there is a difference between the outward intention and the real intention of the parties. Therefore, when the express intent is ambiguous, courts will interpret it to find the real intent of the parties. Indeed, only the real intent of the parties generates contractual obligations. Nevertheless, courts will correct this “subjective approach” to contract by reference to the social value of trust, taking into account the outward expression of one party’s intent as manifested by their actions and understood by the other party.<sup>293</sup> French law tries to accommodate the objective and subjective approach regarding the intent to contract by emphasizing the importance of the real intent but by balancing it by considering the outward intention.<sup>294</sup> According to article 1156 of the French Civil Code the real intent of the parties must be sought.<sup>295</sup> The French legal system does not have the principle of reliance as it exists in the American legal system. However, courts

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<sup>291</sup> *Quake*, 565 N.E. 2d 990 at 993 (1990).

<sup>292</sup> JOHANNA SCHMIDT, LES LETTERS D’INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002.

<sup>293</sup> *Id.*

<sup>294</sup> *Id.* citing J. SCHMIDT, PRELIMINARY AGREEMENTS IN INTERNATIONAL CONTRACT NEGOTIATION, 6 Houston J. of Intn. L., 37 (1983).

<sup>295</sup> Article 1156 C.CIV. provides that “the parties’ common intention must be sought, rather than the literal meaning of the words.” (“on doit dans les conventions rechercher quelle a été la commune intention des parties contractantes, plutôt que de s’arrêter au sens littéral des termes.”).

have a tendency to decide that this declared intent is binding if it has been understood as such by the other party.<sup>296</sup>

Furthermore, if the parties agreed on the essential terms stated in their letter of intent, this writing will be binding between them (if they want it to). Indeed, according to article 1583 of the French Civil Code, “the sale is perfect when there is an agreement on the thing and the price.”<sup>297</sup> Moreover, sometimes the parties state in their letter of intent that even if they did agree on all the terms, an additional formality will have to be completed in the near future. It could be, for example, the drafting of a formal document or an authorization to be given by an authority. However, the question of whether this formality is a *sine qua non* condition to the formation of the contract is not relevant in French or American law. Indeed, the French civil code provides that the promise to sell is a sale when the parties mutually agreed on the thing and the price.<sup>298</sup>

#### b- Situations in which the Letter of Intent is not recognized as binding

In both legal systems, it seems that a letter of intent is declared to be a binding contract when all the constitutive elements of a valid contract are met. In the American law system, a letter of intent can be recognized as a non binding document either because the parties express their intention not to be bound or because not all the necessary elements of a valid contract are met. Moreover, courts can find that the parties did not intend to be bound even if it is not expressly said in their writing. Indeed, this was the case in Philmar Mid-Atlantic, Inc. v. New York Street Associates II,<sup>299</sup> where the court found that the parties did not express their intent to be bound. Here, as a result of the absence of manifestation of intention, the court indicated that

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<sup>296</sup> JOHANNA SCHMIDT, LES LETTERS D’INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002.

<sup>297</sup> Article 1583 C.CIV. provides that “la vente est parfaite dès qu’on est convenu de la chose et du prix.”

<sup>298</sup> Article 1589 C.CIV. provides that “la promesse de vente vaut vente lorsqu’il y a consentement réciproque des deux parties sur la chose et sur le prix.”

<sup>299</sup> 566 A.2d 1253 (1989)



no enforceable agreement existed regarding the negotiations concerning the terms of a possible future contract.<sup>300</sup> In addition, the intent of the parties has to be respected and the court went on by indicating that the letter of intent provided that “neither party would be bound until a mutually satisfactory lease had been negotiated and executed.”<sup>301</sup> Moreover, a letter of intent stating that the parties would be interested in working together is not a binding contract.<sup>302</sup> Indeed, this letter of intent did not aim to bind either party.<sup>303</sup> Furthermore, in Officemax, Inc. v. Sapp,<sup>304</sup> the court held unenforceable a clause in a letter of intent because it was not supported by valid consideration and was “not sufficiently definite [as] to all of its essential terms.”<sup>305</sup>

If the parties do not intend to be bound by their letter of intent, they have to be careful about the words they use. For example, the parties should not use terms like “contract” or “agreement” in their letter of intent. Preferable terms include “proposal,” “term sheet” or “list of proposed points.”<sup>306</sup> Moreover, the parties should stipulate that the letter of intent cannot generate binding obligations, even the obligation to negotiate in good faith.<sup>307</sup> They should also not include essential terms of an agreement since a court will not recognize it as binding (for example, they should not stipulate the price). Here again, the words in the letter of intent remain

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<sup>300</sup> *Id.* at 1255. See also *Goldman v. McShain*, 247 A.2d 455 at 458 (1968); *Kazanjian v. New England Petroleum Corp.*, 480 A.2d 1153 at 1157 (1984) (“Absent a manifestation of an intent to be bound... however, negotiations concerning the terms of a possible future contract do not result in an enforceable agreement.”)

<sup>301</sup> See *Philmar*, 566 A.2d 1253 (1989) at 1255

<sup>302</sup> *VHB Associates Inc. v. Orix Real Estate Equities*, Case No. CV 02-4710 JFW (RNBx), slip op. at 8, 2002 U.S. Dist. LEXIS 17569 (C.D. Cal. 2002).

<sup>303</sup> *Id.* at 8

<sup>304</sup> 132 F. Supp.2d. 1079 (M.D. Ga. 2001)

<sup>305</sup> *Id.* at 1084

<sup>306</sup> KATHRYN COCHRANE MURPHY, LETTERS OF INTENT, American Law Bar Association Continuing Legal Education, 2003 (SH008 ALI-ABA 387)

<sup>307</sup> *Id.* the author proposes a provision such as: “this document is only a list of proposed points that may or may not become part of an eventual contract. It is not based on any agreement between the parties. It is not intended to impose any obligation whatsoever on either party, including without limitation an obligation to bargain in good faith or in any way other than at arms’ length. The parties do not intend to be bound by any agreement until both agree to and sign a formal written contract, and neither party may reasonably rely on any promises inconsistent with this paragraph. This paragraph supercedes all other conflicting language.”

very important because courts will rely on them to decide whether the document is binding or not.

Furthermore, Restatement Second of Contracts §21 allows the parties to exclude the binding force of their agreement.<sup>308</sup> It provides that “neither real nor apparent intention that a promise be legally binding is essential to the formation of a contract, but a manifestation of intention that a promise shall not affect legal relations may prevent the formation of a contract.”<sup>309</sup> Moreover, such a clause negating contractual sanction may be held unenforceable as against public policy “because it unreasonably limits recourse to the courts or as ‘unconscionably’ limiting the remedies for breach of contract.”<sup>310</sup>

In French law, it is quite the same as American law: the parties may clearly express their intention not to be bound by any contractual obligations.<sup>311</sup> In order to do so, the parties expressly exclude the existence of a contract or they exclude the legal sanctions of an obligation they accepted to undertake.<sup>312</sup> However, commercial and business relations are usually not without legal obligations or duties. Therefore if the parties want their letter of intent not to be binding they have to expressly stipulate it in their letter of intent. As it is in American law, parties must pay close attention to the words in their document. They may wish to write on the top of their document “subject to contract” or “this document is not a contract” (“*document non contractuel*”).<sup>313</sup> French courts, respecting the intention of the parties, will declare such a letter of intent or writing as not binding and without any contractual force. Clearly, courts take a close look at the real intent of the parties and whether this intent has been indicated in their writing.

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<sup>308</sup> RESTATEMENT (SECOND) OF CONTRACTS §21. INTENTION TO BE LEGALLY BOUND.

<sup>309</sup> *Id.*

<sup>310</sup> See JOHANNA SCHMIDT, LES LETTERS D’INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002, citing RESTATEMENT (SECOND) OF CONTRACTS §21, comment b (1981).

<sup>311</sup> JOHANNA SCHMIDT, LES LETTERS D’INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002, 259

<sup>312</sup> *Id.*

<sup>313</sup> *Id.* p.259-260

Therefore the parties have to be very clear and express their intent not to be bound. In addition, courts will pay attention to the circumstances surrounding the conclusion of the writing and thus whatever is stated in the writing.<sup>314</sup>

In some cases, the parties express their intent to be bound by their letter of intent but not to be bound by any legal sanctions in a case of a breach.<sup>315</sup> The issue is whether such clauses are legal and enforceable. French courts refuse to admit these kinds of clauses when they relate to the non-performance of the main thrust of obligation of the contract. Since the contract is not valid and enforceable anymore, neither is the clause.<sup>316</sup>

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<sup>314</sup> *Id.* Courts will analyze the clause in question when bargaining power is unequal and one party is in a weaker position than the other one. It will be the same in labor contract (because employees are in a weaker position than employers).

<sup>315</sup> *See e.g.* Cass. Com. Oct. 22, 1996, Bull. Civ. IV, n. 261 “l’arrêt Chronopost” [Chronopost’s case]

<sup>316</sup> *Id.* citing in JOHANNA SCHMIDT, LES LETTERS D’INTENTION [LETTERS OF INTENT], RDAI/IBLJ, Number 3/4, 2002, 261, called the “famous Chronopost case law”, in which a clause was limiting the liability of a carrier in the even of delay. The court held this clause invalid and unenforceable because ‘such a clause contradicts the scope of the given promise.’”

## CHAPTER III

### OTHER BASES FOR LIABILITY: RELIANCE, UNJUST ENRICHMENT, AND TORT

In both systems the parties can express their intent not to be bound and courts will recognize it when it is clearly and expressly stipulated in their writing. Nevertheless, the situation is different when the parties did not draft any documents relating to their negotiation period.

Therefore, in case of a wrongful breach of negotiations when there is not a breach of the good faith duty, parties must use other legal remedies provided, such as promissory estoppel or unjust enrichment theory.

#### I- Promissory estoppel

Whereas few problems arise in relation to pre-contractual liability when a contract has been formed or at least a tentative agreement is made but never executed, real problems and difficulties exist where no contract has been reached. Indeed, in such a case neither the French Civil Code nor the traditional rules of French contract law contain any provisions.<sup>317</sup> Nevertheless, French law still has the concept of good faith and fair dealing as a prerequisite in contractual negotiations.<sup>318</sup> During this period of negotiations, both parties have some obligations like the duty to negotiate in good faith and with fair dealing, the duty to disclose, the

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<sup>317</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 137 (ed. Kluwer Law International, 2002).

<sup>318</sup> *Id.*

duty of care and some others.<sup>319</sup> However, it remains very difficult to hold a party liable when no contract is reached at the end.

In the United States, the law provides a remedy which is an obligation arising from justified reliance called promissory estoppel. By this theory, no one may change his mind to the injury of another.<sup>320</sup> Indeed, the idea behind this doctrine is the principle of fairness and equity. Where one party, the promisor, expects another party, the promisee, to rely on the promise and “the promisee does rely to its detriment, it would be unjust to refuse to enforce the promise.”<sup>321</sup> In addition, some courts define this doctrine as a promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee and which does induce action or forbearance which is binding if injustice can be avoided only by enforcement of the promise.<sup>322</sup> Restatement Second of Contracts §90 gives the definition of promissory estoppel as “a promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance [that] is binding if injustice can be avoided only by enforcement of the promise.”<sup>323</sup> Indeed, if someone has suffered any injury or damage from the non performance of a promise on which he did rely on and trust another person, consequently the promisor is bound to make good the matter and in sum to perform the promise.<sup>324</sup> Thus, the promise is binding if the promisee has suffered some detriment in reliance thereon even if this detriment was not

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<sup>319</sup> See supra Chap. I section B) 2) Duties of parties: exceptions to caveat emptor

<sup>320</sup> See ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE AND PRACTICE, 81, (fourth edition 2001), which cites PAPIAN (CIRCA 200 A.D.) IN JUSTINIAN, DIGEST, 50.17.75 (circa 534) “*nemo potest mutare consilium suum in alterius iniuriam.*”

<sup>321</sup> Miles Homes Div. of Insilco Corp. v. First State Bank of Joplin, 782 S.W.2d 798 (Mo. Ct. App. 1990).

<sup>322</sup> See Hinchey v. Nynex Corporation, 144 F.3d 134 (1<sup>st</sup> Cir. 1998); Lange v. TIG Ins. Co., 81 Cal. Rptr. 2d 39 (2d Dist. 1998), review denied, (Mar. 9, 1999); Gallagher, Langlas & Gallagher v. Burco, 587 N.W. 2d 615 (Iowa Ct. App. 1998); Decatur County Feed Yard, Inc. v. Fahey, 974 P.2d 569 (1999).

<sup>323</sup> RESTATEMENT (FIRST) OF CONTRACTS: PROMISE REASONABLY INDUCING DEFINITE AND SUBSTANTIAL ACTION §90 (1932).

<sup>324</sup> See S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE AND PRACTICE, 81 (fourth edition 2001) citing S. PUFENDORF, DE JURE NATURAE ET GENTIUM, Book III, Ch. v., sec. 11 (1688).

requested as consideration.<sup>325</sup> Furthermore, it has been said that this doctrine is a substitute for consideration or can also be seen as an exception to its classic requirements.<sup>326</sup> If someone has relied to his detriment on the words and acts of another, he has consequently suffered a loss.<sup>327</sup> Thus that person shall be able to recover from this loss. Of course the case would be different if a contract has been breached. Then the injured party cannot make a claim under the theory of promissory estoppel, and no reliance or out-of-pocket loss need be shown to allow this party to recover the loss. Therefore, when a contract is reached, the remedy of promissory estoppel cannot be used. Indeed, according to the court in Doe v. Univision Television Group, Inc.,<sup>328</sup> claims for promissory estoppel and breach of contract cannot be brought together - they are separate claims.<sup>329</sup> The doctrine of promissory estoppel is used when the elements of a contract are not met but the promise should be enforced in order to avoid injustice.<sup>330</sup> The reason for the promissory estoppel theory is fairness and reasonable reliance on the promise.<sup>331</sup> When one party relied on the other's promise, the party who made this promise shall be liable if he or she breaches the promise. The problem is that during the stage of negotiation there is no real "promise" except to conduct negotiations in good faith and with fair dealing.

Thus, the question is whether a party can claim a breach of negotiation under the promissory estoppel doctrine. In order to resolve that particular issue, the study of each element of the promissory estoppel theory remains important. In order to succeed in a promissory

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<sup>325</sup> 17A AM JUR 2D CONTRACTS §120

<sup>326</sup> *Id.* citing METZGER & PHILIPS, THE EMERGENCE OF PROMISSORY ESTOPPEL AS AN INDEPENDENT THEORY OF RECOVERY, 35 Rutgers LR 472, Spring, 1983: "it has been pointed out that a situation in which estoppel is allowed to serve as substitute for consideration is an example of a situation where promissory estoppel has become an independent theory of recovery in practical effect."

<sup>327</sup> See MURRAY, MURRAY ON CONTRACTS, Fourth edition 2001, §66 DETRIMENTAL RELIANCE – "PROMISSORY ESTOPPEL", 309, referring to Chapter 9 §119 EXPECTATION, RELIANCE, AND RESTITUTION INTERESTS – BREACH BY OWNER, 780.

<sup>328</sup> 717 So. 2d 63 (Fla. Dist. Ct. App. 3d Dist. 1998). Reh'g denied, (Oct. 1, 1998).

<sup>329</sup> *Id.* at 65, the court refers also to Youngman v. Nevada Irrigation District, 449 P.2d 462 at 468 (1969)

<sup>330</sup> *Id.* at 65. See Premier Technical Sales, Inc. v. Digital Equipment Corp., 11 F. Supp. 2d 1156 (N.D. Cal. 1998), aff'd in part, rev'd in part on other grounds, 1999 (9<sup>th</sup> Cir. 1999).

<sup>331</sup> FULLER & PERDUE, THE RELIANCE INTEREST IN CONTRACT DAMAGES (pts. 1 & 2), 46 Yale L.J. 52, 373 (1936).

estoppel claim, the plaintiff has to show three main elements: first, that there is a promise which was reasonably expected to induce action or forbearance;<sup>332</sup> second, that the promise did really induce such action or forbearance;<sup>333</sup> and third, that one party suffered detriment as a consequence.<sup>334</sup> Some other elements might be very useful to show and required, like the foreseeability by the promisor that the promisee would rely on the promise.<sup>335</sup> It is also necessary to show that the promisee relied on the promise of a “definite and substantial nature.”<sup>336</sup> However, it is important to note that, according to Miller v. Lawlor,<sup>337</sup> a promissory estoppel claim is not subject to the requirement of a false representation or concealment of material facts, or the absence of knowledge of the true facts by the promisee because the reliance is on the promise and not on a misrepresentation of facts.<sup>338</sup>

Following all these requirements for a promissory estoppel claim, it appears that such a cause of action “demands a promise involving commitment, or the manifestation of an intention to act or refrain from acting in a specified way.”<sup>339</sup> Moreover, the promise that the promisee relied upon must be clear and unambiguous.<sup>340</sup> It has been said that the promise must be clear and sufficiently specific in such a way that the obligations agreed by the parties can be understood and enforced according to its terms by a court.<sup>341</sup> In other words, if in a course of dealings the

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<sup>332</sup> 28 AM JUR 2D ESTOPPEL AND WAIVER, (2) PROMISSORY ESTOPPEL [§§55-59], §55, 481.

<sup>333</sup> *Id.*

<sup>334</sup> See *Viernow v. Euripides Development Corp.*, 157 F.3d 785 (10<sup>th</sup> Cir. 1998); *Skyline Intern. Development v. Citibank, F.S.B.*, 706 N.E.2d 942 (1<sup>st</sup> Dist. 1998).

<sup>335</sup> See *Skyline Intern. Development v. Citibank, F.S.B.*, 706 N.E.2d 942 (1<sup>st</sup> Dist. 1998); *Allied Vista, Inc. v. Holt*, 987 S.W.2d 138 (14<sup>th</sup> Dist. 1999).

<sup>336</sup> *United of Omaha v. Hieber*, 698 N.E.2d 869 (Ind. Ct. App. 1998), 701 N.E.2d 622 (Ind. Ct. App. 1998), 714 N.E.2d 172 (Ind. 1999).

<sup>337</sup> 66 N.W.2d 267 (1954).

<sup>338</sup> *Id.* at 273

<sup>339</sup> *Michelson v. Digital Financial Services*, 167 F.3d 715 (1st Cir. 1999).

<sup>340</sup> *Lange v. TIG Ins. Co.*, 81 Cal. Rptr. 2d 39 (2d Dist. 1998), review denied, (Mar. 9, 1999).

<sup>341</sup> See *Wyatt v. BellSouth, Inc.*, 998 F. Supp. 1303 (M.D. Ala. 1998). However, according to *Goff-Hamel v. Obstetricians & Gynecologists, P.C.*, 588 N.W.2d 798 at 801(1999), “promissory estoppel does not impose the requirement that the promise giving rise to the cause of action must be so comprehensive in scope as to meet the requirements of an offer that would ripen into a contract if accepted by the promisee.”

parties agreed to the terms of their promise in such a way that leaves the court able to identify their respective obligations, a promissory estoppel cause of action can be brought. Therefore, it would be difficult to identify the obligations of the parties since they are still negotiating and in theory they have yet to agree about the terms of their agreements. Thus, if the parties drafted a preliminary document, such as a letter of intent, a promissory estoppel claim cannot be brought before a court. It has to be a promise that is clear and definite. In addition, the court in Wright v. Miller<sup>342</sup> asserted that a “statement of future intent is not the unequivocal promise necessary to invoke the doctrine of promissory estoppel.”<sup>343</sup> Of course in a case of a conditional oral promise, a promissory estoppel cause of action cannot be brought because it is not reasonable for the party to rely on such a promise.<sup>344</sup>

In order to know whether a promissory estoppel claim can be successful and whether enforcement of a promise is necessary to avoid injustice, it may depend on the reasonableness of the promisee’s reliance,<sup>345</sup>

on its definite and substantial character in relation to the remedy sought, on the formality with which the promise is made, on the extent to which the evidentiary, cautionary, deterrent and channeling functions of form are met by the commercial setting or otherwise, and on the extent to which such other policies as the enforcement of bargains and the prevention of unjust enrichment are relevant.<sup>346</sup>

It seems that when a promise is made during the negotiation period, and the promise is not clear enough in such a way that there is no liability involved for the parties, promissory estoppel cannot operate to create liability where it does not otherwise exist.<sup>347</sup>

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<sup>342</sup> 93 Wash. App. 189 (1999).

<sup>343</sup> *Id.* at 202.

<sup>344</sup> *G & F Associates Co. v. Brookhaven Beach Health Related Facility*, 671 N.Y.S.2d 510 (N.Y. App. Div. 1998).

<sup>345</sup> *See Leonardi v. City of Hollywood*, 715 So. 2d 1007 at 1009 (Fla. Dist. Ct. App. 4th Dist. 1998) “The character of the reliance protected is explained as follows: the promisor is affected only by reliance which he does or should foresee, and enforcement must be necessary to avoid injustice.”

<sup>346</sup> *Id.* at 1009; *See also W.R. Grace & Co. v. Geodata Services, Inc.*, 547 So. 2d 919 at 924 (1989).

<sup>347</sup> *Allied Vista, Inc. v. Holt*, 987 S.W.2d 138 (1999).



There are some situations that occur during preliminary negotiations in which the parties understand that no contract has yet been formed and certain terms are left to be agreed upon. Such situations may be called as pre-contractual reliance.<sup>348</sup> In order to allow a reliance recovery in such cases on the basis of promissory estoppel, a court immediately confronts the rule that the promise upon which the promisee relied on must be “clear and definite.”<sup>349</sup> In the preliminary negotiations context, the well-known case Hoffman v. Red Owl Stores, Inc.<sup>350</sup> is important to analyze.<sup>351</sup> Hoffman and his wife, as plaintiffs in this case, relied on several assurances by authorized agents of Red Owl Stores, the defendant. The parties were negotiating. A contract about these assurances was supposed to be drafted and signed but it was never been formed. Instead of focusing upon the fact of the parties envisioned a bargain but never achieved one, or that the preliminary negotiations had not reached an adequate level of definiteness to constitute an offer, the court instead focused on the idea of fairness and equity and how to avoid manifest injustice caused by detrimental reliance. The reliance in this case was not only foreseen by the promisors but also urged upon the promisees. Here again, there is the idea of fairness and equity in transactions, whether a contract is reached at the end or not. Indeed, in *Hoffman*, no written agreement on the essential factors had been reached. The court asserted that if promissory estoppel were limited to only those situations where the promise giving rise to the cause of action must be so definite with respect to all details that a contract would result, then the defendant’s

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<sup>348</sup> MURRAY, MURRAY ON CONTRACTS: §66 DETRIMENTAL RELIANCE – “PROMISSORY ESTOPPEL.” 1. PRECONTRACTUAL RELIANCE – INDEFINITENESS – ABSENCE OF OFFER, 324 (Fourth Edition 2001).

<sup>349</sup> *Id.*

<sup>350</sup> 133 N.W.2d 267 (1965).

<sup>351</sup> *Id.* The facts summarized are the following: Lukowitz, agent for Red Owl, represented to and agreed with Hoffman that Red Owl would build a store building in Chilton and stock it with merchandise for Hoffman to operate in return for which Hoffman and his wife were to put up and invest a certain sum; that in reliance upon the above mentioned agreement and representations Hoffman and his wife sold their bakery building and business and their grocery store and business. They also, in reliance on the agreement and representations, purchased the building site in Chilton and rented a residence for themselves in the same place. Thus, they lost a lot of money from their income and expended large sums as expenses. Hoffman and his wife asked for recovery of damages for the breach of Lukowitz and Red Owl’s representations and agreements.

promises at issue would not meet this test.<sup>352</sup> To resolve this issue the court referred to Restatement First of Contracts §90,<sup>353</sup> which does not require that the “promise giving rise to the cause of action must be so comprehensive in scope as to meet the requirement of an offer that would ripen into a contract if accepted by the promisee.”<sup>354</sup> Thus, it would be an error to analyze an action on the ground of promissory estoppel as equivalent to an action for breach of contract.<sup>355</sup> In addition, the use of this theory in pre-agreement negotiations is bound to alter the well-known scheme of offer and acceptance because it imposes responsibility without regard to expressed intention.<sup>356</sup> Besides, the use of this doctrine in pre-agreement bargaining is “inconsistent with a line of authority that maintains that pre-agreement discussions and negotiations can at most constitute an agreement to agree, which is not generally enforceable.” It appears very difficult to know whether a promissory estoppel cause of action can be brought when the parties are in the negotiating process and reached a pre-agreement. It seems that it would depend on whether the promise upon which the promisee relied on is definite and substantive enough to warrant the remedy of promissory estoppel. It seems very difficult in the negotiation process to recognize such a promise as binding if not all the essential terms of the parties’ agreement are decided and agreed upon. Courts will have to look at the intention of the parties as well as the language used in their documents.<sup>357</sup> In addition, whether the promissory

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<sup>352</sup> *Id.* at 275

<sup>353</sup> RESTATEMENT (FIRST) OF CONTRACTS §90: PROMISE REASONABLY INDUCING DEFINITE AND SUBSTANTIAL ACTION. “A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.”

<sup>354</sup> *See Hoffman* 133 N.W.2d 267 (1965) at 275 citing that “the conditions imposed for promissory estoppel are: (1) was the promise one which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee? (2) Did the promise induce such action or forbearance? (3) Can injustice be avoided only by enforcement of the promise?”

<sup>355</sup> *Id.*

<sup>356</sup> HENDERSON, PROMISSORY ESTOPPEL AND TRADITIONAL CONTRACT DOCTRINE, 78 Yale L.J. 343, 358-60 (1969).

<sup>357</sup> *See Elvin Associates v. Franklin*, 735 F. Supp. 1177 (S.D.N.Y. 1990). The court asserts that “the central issue pertaining to plaintiff’s claim for breach of contract is whether or not the parties to that proposed contract evinced an intent not to be formally bound before execution of a written, integrated contract.” The court in this case recognized

estoppel claim can be brought really depends on the circumstances, which are different in each case. The fact that the promise is definite remains of great importance for a court in order to give an appropriate remedy. In another well-known case, Wheeler v. White,<sup>358</sup> the court of appeals found that the agreement between the parties was too indefinite to enforce.<sup>359</sup> The Supreme Court of Texas held that the agreement could not qualify as a contract because of its indefiniteness. However, the promissory estoppel cause of action was appropriate because the plaintiff's reliance on the defendant's assurances was justified. This case shows again that the original point of promissory estoppel was to give appropriate remedy for contract-like promises and then enable the courts to enforce these kinds of promises made unenforceable by technical defects or defenses.<sup>360</sup> Moreover, in Pop's Cones, Inc. v. Resorts International Hotel, Inc.,<sup>361</sup> the court indicated that the requirement of a "clear and definite" promise should be relaxed in situations where the plaintiff seeks to enforce an agreement not fully negotiated.<sup>362</sup> The court indicated that Restatement Second of Contracts §90 should be understood as not requiring a "strict adherence to proof of a 'clear and definite promise' which is being eroded by a more equitable analysis designed to avoid injustice."<sup>363</sup> However, the position of courts on this is not unanimous. Some agree that a promissory estoppel cause of action can be brought even if not all

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"the language inserted in a draft of the agreement has to be strong (though not conclusive) evidence of intent not to be bound prior to execution." However in this case the cause of action for breach of contract was dismissed because the parties were not contractually bound until the draft agreement was executed, thus the plaintiff has a right to recover on a theory of promissory estoppel.

<sup>358</sup> 398 S.W.2d 93 (Tex. 1965), the facts can be summarized as follow: the defendant promised to procure construction financing for the shopping center. The defendant failed to furnish such financing himself. Thus because the plaintiff relied on the defendant's promise, he proceeded to reconstruct the sit for the new center by tearing down existing structures. Thus, because of the non performance of the defendant, the plaintiff sought damages on the basis of the agreement between him and the defendant. *See* also for a description of the facts MURRAY, MURRAY ON CONTRACTS, §66. DETRIMENTAL RELIANCE – "PROMISSORY ESTOPPEL". C. APPLICATION AND EXPANSION OF DETRIMENTAL RELIANCE. 1. PRECONTRACTUAL RELIANCE – INDEFINITENESS – ABSENCE OF OFFER, 325 (Fourth Edition 2001).

<sup>359</sup> *Id.* Wheeler at 97

<sup>360</sup> Doe v. Univision Television Group., Inc., 717 So. 2d 63 (Oct 1, 1998).

<sup>361</sup> 704 A.2d 1321 at 1325 (1998).

<sup>362</sup> *Id.* at 1325

<sup>363</sup> *Id.* at 1326.

essential elements of a contract are met,<sup>364</sup> whereas some others require that all these elements are met to invoke promissory estoppel.<sup>365</sup>

Concerning the allowance of damages, the court indicated that usually the plaintiff should be placed in the position he would have been in if he had not acted in reliance on the promise.<sup>366</sup> Usually the recovery for breach of a contract promise is under the expectation interest.<sup>367</sup> Under this rule, the plaintiff will be placed in the same financial position in which he would have been placed if he had the promisor performed.<sup>368</sup> Damages for a promissory estoppel claim are not the price agreed to be paid on full performance.<sup>369</sup> However, when the action is based on promissory estoppel ground, the loss or injury will be measured based on reliance damages.<sup>370</sup> Indeed, reliance damages may be the most appropriate remedy in a case where a party has changed his position in reliance on the contract by incurring expenses in order to prepare to perform the said promise.<sup>371</sup> In fact, when a promise is broken on the grounds of promissory estoppel, the appropriate remedy is to allow reliance damages which are measured according to the loss.<sup>372</sup>

In French law, the concept of promissory estoppel does not exist. A similar concept is the “*théorie de l'apparence*” which applies if one party relied on the other’s acts because the other

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<sup>364</sup> See *Rosnick v. Dinsmore*, 457 N.W.2d 793 at 800 (1990); *Quake Constr., Inc. v. American Airlines, Inc.*, 565 N.E.2d 990 at 1004-1005 (1990); *Bixler v. First Nat’l Bank*, 619 P.2d 895 at 898-899 (1980).

<sup>365</sup> *Owasso Dev. Co. v. Associated Wholesale Grocers*, 873 P.2d 212 at 213 (1994).

<sup>366</sup> *Id.* See also *Wheeler v. White*, 398 S.W.2d 93 (1965).

<sup>367</sup> 22 AM JUR 2D §50 RECOVERABILITY OF FULL CONTRACT PRICE.

<sup>368</sup> *Id.*

<sup>369</sup> *Callicott v. Gresham*, 161 So. 2d 183 (1964); See also *Troitino v. Goodman*, 35 S.E.2d 277 (1945); RESTATEMENT SECOND OF CONTRACTS §349 DAMAGES BASED ON RELIANCE INTEREST, comment a. (which provides that the recovery for expenditures may not exceed the full contract price.)

<sup>370</sup> 22 AM JUR 2D §51 GENERALLY C) RELIANCE INTEREST.

<sup>371</sup> *Shovel Transfer and Storage, Inc. v. Pennsylvania Liquor Control Bd.*, 739 A.2d 133 (1999).

<sup>372</sup> See *Wartzman v. Hightower Productions, Ltd.*, 456 A.2d 82 at 86 (1983), the court asserts that “recovery for breach of contract based upon reliance interest is not without limitation. If it can be shown that full performance would have resulted in a net loss, the plaintiff cannot escape the consequences of a bad bargain by falling back on his reliance interest. Where the breach has prevented an anticipated gain and made proof of loss difficult to ascertain, the injured party has a right to damages based upon his reliance interest, including expenditures made in preparation for performance, or in performance, less any loss that the party in breach can prove with reasonable certainty the injured party would have suffered had the contract been performed.”

party let him believe that he has the right to conclude such an agreement.<sup>373</sup> Under this theory, the “*apparence*” has to be well-known, persistent, non equivocal, and based on common mistake (“*error communis facit jus*”), that is to say, it is shared by almost everyone and as a result is unavoidable. The plaintiff has to show these elements of “*apparence*” and also its legitimacy.<sup>374</sup> Nevertheless, this kind of action is not very often used in preliminary negotiations but rather in agency contracts.

Indeed, an action for breach of negotiations can be brought before a court and the responsibility of the party who wrongfully breached the negotiations will be under tort law. According to article 1382 of the French Civil Code, any injury which is caused to one person by another must be redressed by the person by whom this injury occurred.<sup>375</sup>

## II- Unjust enrichment (quasi contract or restitution)

The issue of pre-contractual services is a difficult one. The concept of unjust enrichment is based in the law of restitution in both American and French law. Unjust enrichment means that “for this by nature is equitable, that no one be made richer through another’s loss.”<sup>376</sup> Unjust enrichment has to be distinguished from the two principal sources of civil liability at common law: tort and contract.<sup>377</sup> In fact, American law has recognized that unjust enrichment constitutes

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<sup>373</sup> See B. MERCADAL AND P. MACQUERON, LE DROIT DES AFFAIRES EN FRANCE [BUSINESS LAW IN FRANCE], numéro 265, 153, (édition Francis Lefebvre) “si quelqu’un se présente comme le titulaire d’un droit ou d’un pouvoir qu’en réalité il n’a pas, toute personne traitant avec lui pourra opposer son acte au véritable titulaire du droit ou du pouvoir sous réserve que cette apparence soit notoire, persistante et sans équivoque ; fondée sur un erreur ‘commune’ et légitime, prouvée par celui qui l’invoque.”

<sup>374</sup> *Id.*

<sup>375</sup> Article 1382 C. CIV. provides that “tout fait quelconque de l’homme, qui cause à autrui un dommage, oblige celui par la faute duquel il est arrivé, à le réparer.”

<sup>376</sup> See ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, 112 (Fourth Edition 2001) citing POMPONIOUS (Circa 150 A.D.) in Justinian, Digest, 50.17.206 (circa 534): “*Inure naturae aequum est neminem cum alterius detrimento et iniuria fieri locupletioem.*”

<sup>377</sup> See G. PALMER, LAW OF RESTITUTION §1.1 at 1-2 (1978). According to G. GILMORE in “THE DEATH OF CONTRACT”, 87-88 (1974) citing in ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, Fourth Edition 2001, 143, the line between contract and torts

a complete distinguishable category of law.<sup>378</sup> Another term sometimes used for this doctrine is “restitution.” Nevertheless, restitution is often used to designate any kind of remedy at law or in equity that redresses unjust enrichment.<sup>379</sup> According to Puttkammer v. Minth,<sup>380</sup> an action for recovery grounded under unjust enrichment is based on the “moral principle that one who has received a benefit has a duty to make restitution where retaining such a benefit would be unjust.”<sup>381</sup>

According to Restatement of Restitution §1 (1937), when a person has been unjustly enriched at another’s detriment, he has the duty to make restitution to that person.<sup>382</sup> The unjust enrichment claim permits one party to seek reimbursement from another who benefited from his or her action (or property) without legal right. According to Sparks v. Gustafson,<sup>383</sup> unjust enrichment exists where the defendant has received a benefit from the plaintiff and as a matter of equity the defendant has to compensate the plaintiff for its value.<sup>384</sup> The plaintiff is entitled to compensation when the defendant has conferred a benefit upon him if it would be fair, just and equitable to require compensation under the circumstances.<sup>385</sup> A benefit is constituted by the giving to another person some interest in money, land or possessions, or is when one performs

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tends to disappear. He said that “contract is being reabsorbed into the mainstream of tort.” Furthermore, he indicates that it has been noticed “the insistence of the classical theorists on the sharp differentiation between contract and tort – the [early] refusal to admit any liability in “contract” until the formal requisites of offer, acceptance and consideration had been satisfied, the dogma that only “bargained-for” detriment or benefit could count as consideration, and notably, the limitations on damage recovery... With the growth of the promissory estoppel idea, it was breached on the detriment side. We are fast approaching the point where, to prevent unjust enrichment, any benefit received by a defendant must be paid for unless it was clearly meant as a gift; where any detriment, reasonably incurred by a plaintiff in reliance on the defendant’s assurances must be recompensed. When that point is reached, there is really no longer any viable distinction between liability in contract and liability in tort.”

<sup>378</sup> G. PALMER, LAW OF RESTITUTION §1.1 at 1-2 (1978).

<sup>379</sup> ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE: NOTE: VARIANT TERMINOLOGY: UNJUST ENRICHMENT, RESTITUTION, QUASI-CONTRACT, QUANTUM MERUIT, COMMON COUNTS, 138 (Fourth Edition 2001).

<sup>380</sup> 266 N.W.2d 361 (1978).

<sup>381</sup> *Id.* at 363

<sup>382</sup> RESTATEMENT OF THE LAW OF RESTITUTION §1 UNJUST ENRICHMENT (1937) provides that “a person who has been unjustly enriched at the expense of another is required to make restitution to the other.”

<sup>383</sup> 750 P.2d 338 (1988).

<sup>384</sup> *Id.* at 342

<sup>385</sup> *Id.* at 342

services beneficial to the other, or satisfies a debt of the other. In sum, gives a benefit to another.<sup>386</sup>

Three conditions must be met in order to show “unjust enrichment.”<sup>387</sup> first of all, the defendant is enriched or has a benefit; second, the plaintiff has been deprived because of the defendant’s enrichment (and the defendant had the knowledge of the benefit);<sup>388</sup> third and finally, the defendant has no legal reason to be enriched at the plaintiff expense.<sup>389</sup> Even if it is the case that someone confers a benefit upon another not required by contract or legal duty, the party who received that benefit is often unjustly enriched and therefore restitution of that benefit (or at least its value) is required.<sup>390</sup> However, this is not always the case. Indeed, the distinction between unjust enrichment and a mere gratuity remains very important. Of course, a gift is not considered as enrichment for the person who received it.

The first principle is that one who has given a benefit upon another with the intention to make a gift cannot seek relief afterwards against the person who received the benefit.<sup>391</sup> Such a principle is valid in absence of fraud, mistake, duress or undue influence.<sup>392</sup> Therefore, relief would not be granted for a gift. However, such situations are very difficult to find when preliminary negotiations are involved as a mere gratuity is rarely given when parties are dealing.

The second principle of unjust enrichment is that one who confers an advantage upon another without affording the other one the opportunity to refuse and reject the benefit, that

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<sup>386</sup> RESTATEMENT OF THE LAW OF RESTITUTION §1, comment b (1937).

<sup>387</sup> PAULA GILKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 97 (Kluwer Law International, 2002)

<sup>388</sup> *Watts v. Watts*, 405 N.W.2d 303 (1987).

<sup>389</sup> *Id.* at 313-314

<sup>390</sup> See ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, 120, Fourth Edition 2001, citing D. DOBBS, REMEDIES, 298-99 (1973).

<sup>391</sup> *Id.*

<sup>392</sup> *Id.*

person has no equitable claim for relief against the other who received the benefit.<sup>393</sup> This would be considered as an invasion of someone's own affairs. Besides, courts refer to the free choice principle in terms of intermeddlers.<sup>394</sup> An intermeddler is someone who imposed or conferred a benefit upon someone else against his will, or deprives him of choice in the matter.<sup>395</sup> If during the negotiations, when no contract is signed, one party has been unjustly enriched at another's expense and suffered a detriment as a result, the injured party can bring a suit under the unjust enrichment theory. That party will recover under the restitution theory. Indeed, restitution theory may refer to only one kind of remedy that one party seeks for breach of contract.<sup>396</sup>

Unjust enrichment theory refers also to the notion of quasi-contract, or a contract implied in law,<sup>397</sup> as the court indicates in Bloomgarden v. Coyer.<sup>398</sup> In fact, during the negotiations period most of the time no contract has been reached but some duties are still thrust upon the parties under some certain circumstances. According to *Bloomgarden*, this occurs when there is a quasi-contract which is "not a contract at all, but a duty thrust under certain conditions upon one party to require another in order to avoid the former's unjust enrichment."<sup>399</sup> Thus, it can be so in preliminary negotiations when one party acts in reliance upon another without any compensation, and that party is deprived whereas the other one is unjustly enriched. This would be the case if, for example, some money was paid during the negotiations.

This notion of quasi-contract dates back many years and has been developed by the common law in situations where no contract was made but one party has been enriched at

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<sup>393</sup> *Id.*

<sup>394</sup> *Id.*

<sup>395</sup> *Id.* sometimes courts will also refer to the term "volunteer" instead. However, this term is used in general to refer to a person who gives a gift to someone else.

<sup>396</sup> ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, 139, (Fourth Edition 2001).

<sup>397</sup> *Id.* See also *Anderco, Inc. v. Buildex Design, Inc.*, 538 F.Supp. 1139 (1982).

<sup>398</sup> 479 F.2d 201 (1973).

<sup>399</sup> *Id.* at 208



another's expense.<sup>400</sup> In preliminary negotiations the parties can truly believe that there was a contract between them but that they had not reached a mutual assent yet. In such a case, the common law gives the plaintiff a remedy and will ask for restitution damages under the theory of quasi-contract. Indeed, in order to recover under a quasi-contractual claim, the plaintiff must show that the defendant was unjustly enriched at his expense, and that the circumstances were such that in good conscience the defendant should make restitution. According to Anderson v. Schweigel,<sup>401</sup> in such situations the plaintiff is still entitled to recover the reasonable value of all services, materials or others, of what the defendant has benefited "as measured by the reasonable value of the benefit conferred."<sup>402</sup> Thus, a quasi-contract will be recognized in appropriate circumstance even if no intention of the parties to bind themselves contractually can be discerned.<sup>403</sup>

Furthermore, the notion of contract implied in law is also used to designate the unjust enrichment theory.<sup>404</sup> Under this notion, there are two different categories: contract implied-in-fact and contract implied-in-law. A contract implied-in-fact is a real and true contract which contains all necessary elements of an enforceable agreement but which differs from other contracts in that it has not been committed to writing or stated orally in express terms, but it is inferred from the conduct of the parties.<sup>405</sup> Some elements have to be shown in order to prove the existence of an implied-in-fact contract. They include establishing that the goods or services were given or performed for the defendant, were not rendered gratuitously, and did actually

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<sup>400</sup> MURRAY, MURRAY ON CONTRACTS, § 126. MEASURE OF RECOVERY FOR RESTITUTION INTEREST. B. CHOOSING THE RESTITUTION INTEREST AS THE INTEREST TO BE PROTECTED. 1. THE ABSENCE OF CONTRACT – QUASI CONTRACT, 826, (Fourth Edition 2001).

<sup>401</sup> 796 P.2d 1035 (1990).

<sup>402</sup> *Id.* at 1038

<sup>403</sup> See *Bloomgarden v. Coyer*, 479 F.2d 201 (1973).

<sup>404</sup> See ROBERT S. SUMMERS AND ROBERT A. HILLMAN, CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE, Fourth Edition 2001, p.139.

<sup>405</sup> See *Bloomgarden v. Coyer*, 479 F.2d 201 at 208 (1973), referring to 1 WILLISTON, CONTRACTS §3A (3d ed. 1957).

benefit the defendant.<sup>406</sup> In contrast, a contract implied in law refers to obligations arising under the theory of unjust enrichment when no agreement was made in fact.<sup>407</sup>

The notion of unjust enrichment or “*enrichissement sans cause*” is quite similar in French law. This notion can be translated as “unjustified enrichment.” However, French law adopts a more rigid formulation than American law. Indeed, “*enrichissement sans cause*” is used where other remedies are not effective. Therefore, the “*enrichissement sans cause*” theory has a subsidiary character, that is to say, the plaintiff has to consider possible actions in contract and tort before thinking of bringing a claim under “*enrichissement sans cause*.” The parties, as it is in American law, have to show that the plaintiff’s loss is the direct consequence of the defendant’s enrichment, and that gain is made without any cause or justification.<sup>408</sup> The origin of this notion is found in case law and not in the French Civil Code. This principle of “*enrichissement sans cause*” was recognized for the first time by the French Cour de Cassation in 1892, but since then French law has confined this notion to a residual role.<sup>409</sup> In the eighteenth century, two well-known authors in France, Domat and Pothier, were influential in the actions of “*condictio indebiti*”<sup>410</sup> and “*negotiorum gestio*”<sup>411</sup> which are recognized under the title of quasi-contracts in articles 1371 to 1381 of the French Civil Code, and lead afterwards to the known doctrine of unjust enrichment.

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<sup>406</sup> *Id.* at 209 “It is well settled that, in order to establish an implied-in-fact contract to pay for services, the party seeking payment must show (1) that the services were carried out under such circumstances as to give the recipient reason to understand (a) that they were performed for him and not for some other person, and (b) that they were not rendered gratuitously, but with the expectation of compensation from the recipient; and (2) that the services were beneficial to the recipient.”

<sup>407</sup> ROBERT S. SUMMERS AND ROBERT A. HILLMAN, *CONTRACT AND RELATED OBLIGATION: THEORY, DOCTRINE, AND PRACTICE*, 139, Fourth Edition 2001.

<sup>408</sup> See J. CARBONNIER, *DROIT CIVIL: LES OBLIGATIONS*, Presses Universitaires de France, 22<sup>e</sup> ed., Number 307-308, 2000; F. TERRE, P. SIMLER AND Y. LEQUETTE, *DROIT CIVIL, LES OBLIGATIONS* 7<sup>e</sup>éd Dalloz, 1999, Number 971-976.

<sup>409</sup> PAULA GILIKER, *PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT*, 67 (Kluwer Law International 2002).

<sup>410</sup> It is an action for money “not due”.

<sup>411</sup> It is an action which is known nowadays at “gestion d’affaires” of article 1375 C. CIV. (acts of administration or conservation).

The leading case in this field is L’Affaire Boudier,<sup>412</sup> in which Boudier sold fertilizer to a tenant for use on his land. The tenant failed to fulfill the conditions of his tenancy agreement and consequently, in partial discharge of the debt, his landlord had seized the crop on which the fertilizer had been applied and repossessed the property. Accordingly, Boudier brought an action de “*in rem verso*” in order to recover the purchase price from the landlord that was left unpaid. The landlord’s counter argument was that this recovery action would breach the principle of article 1165 of the French Civil Code,<sup>413</sup> which provides for the privacy of contract.<sup>414</sup> However, this argument was rejected by the French Cour de Cassation, which asserted that the plaintiff’s cause of action “lay not in contract but on a principle of equity, triggered by the personal and direct profit gained from the use of Boudier’s fertilizer. This action derives from a principle of equity, which prohibits an individual from enriching himself at the expense of another. It is not set out in any statutory provision and it is not subject to any specified conditions. To bring a successful action, it will suffice that the claimant allege as and proves the existence of a benefit, which was, by an act or omission, transferred to the defendant.”<sup>415</sup> After this famous case, one method of limitation was to absorb the theory within the action of either contract or tort.<sup>416</sup>

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<sup>412</sup> The Boudier Case is also well-known as “*l’Affaire Patureau-Mirand*”, Req June, 15, 1892, S 1893.1.281 note JE Labbé.

<sup>413</sup> Article 1165 C. Civ. provides that “les conventions n’ont d’effet qu’entre les parties contractantes; elles ne nuisent point au tiers, et elles ne lui profitent que dans le cas prévu par l’article 1121.” It can be translated as: contracts have only effects within contracting parties; contracts are not harmful to third parties, and can benefit to them only in cases provided in article 1121.

<sup>414</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT, 77, (Kluwer Law International 2002).

<sup>415</sup> Req. June 15, 1892, S 1893.1.281 note JE Labbé: “cette action dérivant du principe de l’équité qui défend de s’enrichir au détriment d’autrui, et n’ayant été réglementée par aucun texte de nos lois, son exercice n’est soumis à aucune condition déterminée; qu’il suffit, pour la rendre recevable, que le demandeur allègue et offre d’établir l’existence d’un avantage qu’il aurait, par un sacrifice ou un fait personnel, procuré à celui contre lequel il agit.”; See also PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT, 77, (Kluwer Law International 2002).

<sup>416</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT, 78, (Kluwer Law International 2002).

Some authors rely on the tort liability or “*responsabilité délictuelle*” provided by article 1382 of the French Civil Code.<sup>417</sup> In fact, the common element of compensation for unintentional harm in quasi-delict and *enrichissement sans cause* is that no one can harm another without a legal justification.<sup>418</sup> Other commentators rely on the objective theory of risk,<sup>419</sup> which says in sum that if there is a link between the plaintiff’s loss and the defendant’s benefit, the defendant shall be held responsible.<sup>420</sup> Thus, it seems that if there is a just cause of the plaintiff’s loss, then the defendant has not been enriched. However, the principle established in the *Boudier’s case* stated that “*nul ne peut s’enrichir aux dépens d’autrui*” still stands.<sup>421</sup> It seems that courts focus on equity. Later on in the *Clayette’s case*,<sup>422</sup> the Cour de Cassation affirmed that the remedy of unjust enrichment has to be seen as a subsidiary remedy.<sup>423</sup> All these cases, plus the *Briauhant’s case*,<sup>424</sup> held that any claim for unjust enrichment would be subsidiary to a claim in contract or tort.<sup>425</sup>

Under the French law of “*enrichissement sans cause*,” the plaintiff must show that the five elements are met. Indeed, this principle of “*enrichissement sans cause*” did not lead French law to grant recovery for every unauthorized gain.<sup>426</sup> Five elements must be shown under this principle:<sup>427</sup> first, the defendant received a benefit; second, the plaintiff suffered a loss as a result; third, the gain received was without justification or “*sans cause*;” fourth, the plaintiff did

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<sup>417</sup> OBLIGATIONS VII; Rev crit lég et jur 1904.224.

<sup>418</sup> *Id.* “ne pas nuire sans droit”

<sup>419</sup> However, other authors do not agree with that doctrine by saying that theory of objective risk created false scientific certainty and that it is more a question of morality. See LA RÈGLE MORALE DANS LES OBLIGATIONS CIVILES [THE MORAL RULE IN CIVIL OBLIGATIONS], Numéros 133-147, 4<sup>th</sup> édition LGDJ, 1949.

<sup>420</sup> ESSAI D’UNE THÉORIE DE L’ENRICHISSEMENT SANS CAUSE EN DROIT CIVIL FRANÇAIS, [ESSAY OF A THEORY OF UNJUST ENRICHMENT IN FRENCH CIVIL LAW], RTDC 1904. 727.

<sup>421</sup> No-one should benefit at the expense of another.

<sup>422</sup> Cass. Civ., May 12, 1914, S 1918.1.41 note E. Naquet.

<sup>423</sup> *Id.*

<sup>424</sup> Cass. Civ., March 2, 1915, DP 1920.1.102 (1<sup>re</sup> espèce [1<sup>st</sup> case]).

<sup>425</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT, 80, (Kluwer Law International 2002).

<sup>426</sup> *Id.* at 97

<sup>427</sup> *Id.*

not act in his own interest; and finally, the plaintiff had no alternative cause of action.<sup>428</sup> Indeed, if the defendant can justify his enrichment, there is no legal ground for an action. It seems that French law categorization is stricter than American law since each of these elements has to be shown in order to recover from the loss. Some authors assert that in order to have a successful claim under “*enrichissement sans cause*,” the plaintiff must be show that the situation of the parties is absent of fraud,<sup>429</sup> but this is not always the case. It is important to note that the final requirement, that the plaintiff must not have acted in his own interest or at his own risk, is quite related to the question of fault. Indeed, courts will not analyze claims which involve a situation where unjust enrichment was clearly a result of one party’s own interest.<sup>430</sup>

According to these elements, it seems that a party can bring a suit for unjust enrichment in a case of pre-contractual relations between the parties. This could occur when one party starts to perform a contract which has not been yet formed by purchasing some material, and as a result the other party is enriched by the purchase. In most cases, such a performance in anticipation of a contract will be analyzed as implicit acceptance of the risks involved.<sup>431</sup> It seems logical that in the negotiation process some risk remains that the work will not be completed or that some incidents might occur. It seems that, from the point of view of some authors,<sup>432</sup> in case of misconduct at the pre-contractual stage, a party can have a suit under tort responsibility even if an insufficient meeting of minds or “*accord de volontés*” exists to constitute an agreement.

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<sup>428</sup> *Id.*

<sup>429</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW: CHAPTER 3, UNJUST ENRICHMENT, p.78, Kluwer Law International; See e.g. concerning the “*faute lourde*” Cass. Civ., Dec. 15, 1998, D. 1999.425 note Saint-Pau, RTDC 199.400 note J Mestre; D. 1999 IR 27; Cass. Com., May 19, 1998, 406 note M. Ribeyrol-Subrenat, JCP 1999 II 10194 note A. Karm, RTDC 1999.106 obs J. Mestre; see also Cass. Com. May 19, 1999 D. 1999 IR 157; JCP 1999 éd. E 1127 note P. Morvan and J. Djoudi, D. 2000 Chron. 609.

<sup>430</sup> PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 101, (Kluwer Law International 2002), the author explains this situation by a simple and clear example of a miller “who paid a tariff to gain access to a water supply, suffered no loss when the supply was used by a mill further downstream. He was therefore unable to bring an action de in rem verso.” See Req June 22, 1927, S. 1927.1.338.

<sup>431</sup> *Id.* 103

<sup>432</sup> PRECONTRACTUAL LIABILITY: REPORT TO XIII<sup>TH</sup> CONGRESS, INTERNATIONAL ACADEMY OF COMPARATIVE LAW, ed EH Hondius (Boston: Kluwer, 1990) at 148 citing Professor Schmidt-Szalewski’s ideas.

Thus, it has been said that at the stage of pre-contractual negotiations when a contract is not complete enough to provide remedy under contract law, the appropriate remedy is under tort law.<sup>433</sup> Here, according to these authors, unjust enrichment would not be an appropriate remedy.<sup>434</sup>

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<sup>433</sup> *Id.* Professor Schmidt-Szalewski cites that “as long as a contract has not been concluded, compensation of any damage occurred during the pre-contractual process may only be treated in torts.”

<sup>434</sup> *See* PAULA GILIKER, PRE-CONTRACTUAL LIABILITY IN ENGLISH AND FRENCH LAW, 101, (Kluwer Law International 2002) which indicates that such considerations “bar the intervention of *enrichissement sans cause* and provide a compromise with freedom of contract.”

## CONCLUSION

Despite their differences, American law and French law reached the same result at the end regarding pre-contractual liability. While American law emphasized reliance, promissory estoppel or unjust enrichment theory as the valid bases for a pre-contractual liability cause of action, French law based its action on tort responsibility for lack of good faith. Nevertheless, the question of liability arising during the period of negotiations is and will always be problematic. Indeed, both the American law and French law of pre-contractual obligations do not fit within the traditional framework of the law of contract or obligations. As seen before, French law does not contain any regulations in its Civil Code regarding this subject matter. Thus, liability will be in tort, or “*responsabilité délictuelle*,” of article 1382 of the French Civil Code. French law refers to the principle of good faith or “*bonne foi*” in negotiations.

Furthermore, as seen in chapter one of this study, preliminary negotiations have to be distinguished from final contracts. This first part studied cases in which a contract is reached at the end of the dealing process. Preliminary negotiations do not constitute a contract even if they preclude the existence of one later on in the dealing process. Parties are free to contract and free to withdraw at will but they also have to understand the deal: during negotiations there is a risk that the agreement will not be concluded. Negotiations by their nature are uncertain, thus this risk is part of the game. Even though parties have to be aware, it remains that most of the time, if not all the time, obligations are imposed upon one party to disclose, to take reasonable care and not to mislead the other. These legal duties could also be the legal ground for a cause of action when there is misrepresentation. Nevertheless, in a lawsuit, when one party is trying to prove that

the other misled as to the facts, courts will refuse to resurrect some preliminary contracts, documents, written or oral, in accordance with the parol evidence rule. Sometimes, however, courts will allow some documents (letters, telex, etc) as evidence when the contract between the parties is ambiguous and the real intent of the parties must be found. That is the reason why most of the time the parties prefer to protect themselves by including a merger clause in their writing.

In the second chapter, the problem when a preliminary agreement is made but a formal contract is only contemplated but never executed. The situation remains difficult to resolve in both the American law and French law of obligations. First of all, in both legal systems the parties have to negotiate in good faith and with fair dealing. This implies that they cannot wrongfully breach the negotiations. Even though preliminary negotiations do not constitute a contract, in some cases, binding agreements can be made during this pre-contractual period. Thus, the parties may want to include a condition precedent or “*condition suspensive*” in their contract in order to regulate obligations arising from the written document until the condition cited comes to realization. Moreover, the parties may want to include essential terms that they agreed upon in their agreement. In a lawsuit, courts will analyze any document between the parties. After what the parties agreed upon as essential terms of their agreement is decided, there is greater chance that courts will recognize it as a binding contract. It seems that the closer the elements of a writing are to those of a contract, the greater chance courts will hold it enforceable. In addition, the parties may want to have an agreement to reduce their contract to writing or to make it more formal. Drafting a letter of intent remains the best way to protect parties because they can decide whether they want it to be contractually binding or not. They should be clear in their letter of intent in order to avoid a misinterpretation by courts. However, when the parties do not indicate their intent to be bound, courts will interpret the intent of the parties in light of the



words stated in their documents and the circumstances surrounding the signature of the letter of intent. Most of the time in American law a letter of intent will be recognized as an enforceable document when it contains all the essential terms necessary to constitute a valid contract and, of course, is supported by valid consideration. It is the same in French law except that there is no requirement of valid consideration.

In the third and final part, liability under contract law is almost impossible to find when the parties are dealing but have not yet reached an agreement. In some cases, however, when one party relies on another's words and acts, and when this reliance causes a detriment to the person who relied, courts may allow a remedy under promissory estoppel. This system exists only in American contract law, not in French contract law. However, French law will use tort liability or "*responsabilité délictuelle*" in such cases. Furthermore, if one party has been unjustly enriched at another's loss, the injured party could bring a claim under the unjust enrichment theory and recover for the loss. This theory is also adopted by French law. Nevertheless, French law prefers to analyze pre-contractual obligations when no agreement is reached under tort liability.

Risk in negotiations is an important factor to take into account. Understanding that negotiations involve inevitable risk and that parties are free to contract means that no responsibility could be issued. Therefore, the proper question to ask is whether a contract is formed between the parties at the end of the negotiation process. If a contract is formed, courts will focus on the contract to understand the relations and obligations between the parties. In case of ambiguity, the court may analyze other evidence. If no contract is formed, the obligations between the parties have to be treated under tort law according to French law, and under promissory estoppel or unjust enrichment according to American law. Damages will therefore be allowed under these theories. Accordingly, the parties should definitely draft at least one

document which will summarize their dealings and obligations. By doing this they will protect themselves from any misunderstanding and unexpected consequences.

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